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a closer look

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

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Global Tax Weekly – A Closer Look

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NEWS ROUND-UP

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Cyprus Tax Round-Up 2017: Part I

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As we approach the turn of the year it is an appropriate time to summarize the various changes that have taken place to date in 2017 and look forward to the changes on the horizon.

In this Part I of a two-part series, I review the double taxation agreements and direct taxation developments in Cyprus during 2017. In Part II, I shall reflect on value-added tax and tax administration developments.

Double Taxation Agreements (DTAs)

Deferral of new provisions regarding taxation of gains on disposal of shares in companies holding immovable property in Russia

One of the most important developments on the DTA front took place as 2016 drew to a close, with the announcement by the Cyprus Ministry of Finance that the Russian government had agreed to defer the introduction of source-based taxation of capital gains on shares in "property-rich" Russian companies (companies whose assets mainly comprise real estate), which was due to take effect from the beginning of 2017.

Under the 1998 DTA between Cyprus and Russia, gains on disposals of shares are taxable only in the country of residence of the person disposing of the shares. Since Cyprus does not impose any capital gains tax on disposals of shares in companies unless they own immovable property in Cyprus, this makes Cyprus a very advantageous location for holding shares in Russian companies. Most modern DTAs make an exception for gains on disposal of shares in companies which derive their value principally from immovable property (so-called "property-rich" companies), allowing such gains to be taxed in the country in which the property is physically located. The Cyprus–Russia DTA did not make any such distinction, making Cyprus even more attractive as a jurisdiction for holding shares in companies owning or developing real estate in Russia.

However, the 2010 Protocol to the DTA amended the DTA to provide that gains on the disposal of shares in companies which derive their value principally from immovable property in Russia would be subject to tax in Russia from January 1, 2017. Shares in other companies were not affected.

The application of this provision of the Protocol has now been deferred until similar provisions are introduced into Russia's DTAs with other European countries. As a result, disposals of shares in property-rich companies will continue to be taxable only in the country of residence of the person disposing of the shares, in the same way as other shares. At the time of the announcement it was announced that an additional Protocol was being prepared to formalize the deferral, but nothing has been published to date.

Entry into effect of DTAs with Bahrain, Georgia, India, and Latvia

At the beginning of 2017 new DTAs with Bahrain, Georgia, India, and Latvia entered into effect.[1] The agreement with India [2] took effect as regards Indian taxes three months later, on April 1, 2017, the beginning of the Indian tax year.

Like Cyprus's other DTAs, all four agreements closely follow the 2010 OECD Model Tax Convention. The agreements with Bahrain, Georgia and Latvia are brand new, and the agreement with India replaces an earlier DTA which had been in force since 1994. Ratification of the revised DTA with India was completed in record time. The agreement was signed on November 18, 2016, and entered into force less than a month later.

As was widely expected following similar changes to India's agreements with Mauritius and Singapore, the new DTA provides for source-based taxation of gains from the alienation of shares. However, investments undertaken before April 1, 2017 are grandfathered, with taxation rights over gains on the disposal of such shares at any future date remaining solely with the disponor's state of residence.

Entry into force of DTAs with Iran and Jersey

The DTA with Iran, which was signed on August 4, 2015, entered into force on March 5, 2017, following completion of the requisite ratification procedures.[3] It took effect with regard to Iranian tax on March 21, 2017 (the first day of the Iranian year 1396) and will take effect in Cyprus on January 1, 2018. The agreement, which again closely follows the OECD Model Tax Convention, limits withholding taxes on dividends to 5 percent of the gross dividend if the recipient is a resident of the other contracting state and the beneficial owner of the dividends, as long as it holds 25 percent or more of the share capital of the company paying the dividends.

Otherwise, withholding tax is limited to 10 percent. Withholding tax on interest is limited to 5 percent and to 6 percent on royalty payments as long as the recipient is the beneficial owner of the income. Cyprus does not levy any withholding taxes on dividend or interest. Gains from the sale of shares of property-rich companies are taxed in the country where the immovable property is located. Given Cyprus's geographical proximity to Iran, the Cyprus government hopes that the new DTA will help to establish Cyprus as the principal portal for investment between Iran and the European Union.

The DTA between Cyprus and Jersey,[4] which was signed on July 11, 2016, entered into force on February 17, 2017, and will take effect with regard to taxes withheld at source in respect of amounts paid or credited on or after January 1, 2018, and for other taxes in respect of tax years beginning on or after that date. Like Cyprus's other DTAs, it closely follows the OECD Model Tax Convention.

There is no withholding tax on dividends, interest and royalty payments between residents of the two contracting parties. Capital gains arising from the disposal of shares, including shares in property-rich companies, are taxable only in the state where the seller is tax resident. There is an exception for gains on shares of companies holding mineral exploration and exploitation rights or real property connected with them, which may be taxed in the state in which the rights or property are situated.

Unusually, the exchange of information provisions will take effect eight taxable years prior to the entry into force of the agreement. A protocol to the DTA provides robust safeguards against abuse of the information exchange provisions by requiring the contracting party that requests information to fulfill specified procedures to demonstrate the foreseeable relevance of the information to the request. No request is to be submitted unless the party making the request has reciprocal procedures and means of obtaining similar information, and every request must be accompanied by the comprehensive details prescribed in the protocol.

Signature of new DTAs with Barbados and Luxembourg

New DTAs with Barbados and Luxembourg [5] were signed on May 3, 2017 and May 8, 2017, respectively. Both DTAs closely follow the OECD Model Tax Convention.

Dividends, interest and royalties paid by a company resident in one contracting state to a resident of the other are taxable only in the contracting state in which the recipient is resident. In the case of interest and royalties, the amounts qualifying for exemption are limited to what would be payable on an arm's length basis. Capital gains derived by a resident of one contracting state from the disposal of immovable property situated in the other may be taxed in the contracting state in which the property is situated. Gains derived from the alienation of all other property (including ships or aircraft operated in international traffic) are taxable only in the contracting state in which the disponor is resident. Both DTAs also include comprehensive provisions regulating the taxation of offshore hydrocarbon exploration and exploitation activities, intended to ensure that each state's taxation rights in respect of offshore activities are preserved in circumstances where they might otherwise be limited by other provisions of the agreement, such as those dealing with permanent establishment and business profits.

Signature of new Protocols to the DTAs with San Marino and Mauritius

New Protocols to the DTAs with San Marino and Mauritius were signed on May 19, 2017 and October 23, 2017, respectively. The Protocols amend the exchange of information provisions in the existing DTAs to align them with the OECD Model Convention.

Signature of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI)

Cyprus was one of the initial signatories of the MLI, which opened for signature on June 7, 2017. The MLI will apply alongside DTAs, modifying their application in order to implement the relevant BEPS measures, without requiring any further bilateral negotiations between the countries concerned. It will automatically amend all existing DTAs of which both parties are signatory countries to the MLI, introducing measures to prevent base erosion and profit shifting, including anti-abuse and anti-avoidance clauses.

At the time they signed the MLI, jurisdictions submitted a list of double tax agreements they intend to be covered, together with a preliminary list of their reservations and notifications in respect of the various provisions of the MLI. Cyprus intends to include all its existing double tax agreements, and it is likely that the changes will start to take effect in 2019, though some DTAs could be affected before then.

Income Tax and Other Direct Taxes

New tax-residence route for individuals

Law 119(I) of 2017 amends the provisions of the Income Tax Law regarding residence of individuals with effect from the beginning of the 2017 tax year. Previously, the only way for an individual to qualify as tax-resident in Cyprus was to be physically present for at least 183 days in the tax year. However, the new law introduces an additional route to residence. With effect from January 1, 2017, individuals who meet all the following conditions in respect of a given tax year will be deemed to be tax-resident in Cyprus:

- They are physically present in Cyprus for one or more periods amounting to at least 60 days;
- They do not remain in another country for one or more periods exceeding 183 days in total;
- They are not tax resident in another country;
- They undertake business in Cyprus, have employment in Cyprus or hold a post in a Cyprus-resident company which continues to the end of the tax year; and
- They maintain a permanent residence at their disposal for their use in Cyprus.

Individuals who satisfy the criteria may obtain a tax residence certificate by completing the prescribed form (T.126 (2017)) and submitting it to the Tax Department together with evidence of arrival and departure in Cyprus, property title deeds or lease contract, and evidence of employment.

Reference rates for Notional Interest Deduction (NID) for 2017

Article 9(B) of the Income Tax Law of 2002 as amended provides for an NID for tax purposes on new equity capital (paid-up share capital and share premium) injected into companies and permanent establishments of foreign companies on or after January 1, 2015, to finance business assets, calculated by applying a reference rate to the new equity.

The reference rate is the higher of the ten-year government bond yield of Cyprus or the country in which the assets funded by the new equity are utilized, in each case plus three percentage points. The bond yield rates to be used are as at December 31 of the year preceding the year of assessment.

In February, the Tax Department announced the ten-year government bond yields at December 31, 2016, to be used as the basis for the interest deduction for the 2017 tax year, for the countries in Table 1.

Table 1	**Bond yield rate**	**Reference rate for 2017**
Cyprus	3.489%	6.489%
Germany	0.204%	3.204%
United Arab Emirates	3.326%	6.326%
United Kingdom	1.326%	4.326%
India	6.878%	9.878%
Latvia	0.894%	3.894%
Ukraine	8.705%	11.705%
Poland	3.627%	6.627%
Romania	3.748%	6.748%
Russia (expressed in US dollars)	8.380% 4.409%	11.380% 7.409%
Czech Republic	0.414%	3.414%

In September, the Tax Department announced bond yields and NID rates for the 2016 and 2017 tax years for three further countries, Greece, Italy and Kazakhstan, as follows:

	Reference rate for 2016	Reference rate for 2017
Greece	12.639%	11.361%
Italy	6.685%	6.489%
Kazakhstan	8.311%	7.204%

Abolition of the back-to-back minimum margin scheme and introduction of transfer pricing rules

Significant changes to the taxation of back-to-back financing arrangements between related companies took effect on July 1, 2017.[6] The existing minimum margin scheme, which was introduced in 2011, was abolished and replaced with detailed transfer pricing legislation based on the OECD transfer pricing guidelines. The rationale behind this development is to reduce base erosion and profit shifting by ensuring that transfer prices are based on real economic activity and sound valuation principles.

The minimum margin scheme, which was introduced in 2011, provides for a deemed interest rate to be imputed for tax purposes on back-to-back finance arrangements between group companies. The imputed rate ranges from 0.125 percent for loans of more than EUR200m to 0.35 percent for loans of less than EUR50m.

The new rules apply with effect from July 1, 2017, both for the purposes of issuing tax rulings as well as for assessing tax. Any existing tax rulings in relation to such arrangements ceased to apply from that date.

Under the new rules, intragroup financing transactions will be evaluated to ensure that the agreed remuneration complies with the arm's length principle (*i.e.*, it corresponds to the price which would have been accepted by independent entities in comparable circumstances, taking into account the economic nature of the transaction). A comparability analysis must be carried out by an appropriately qualified person to determine whether the transactions between the related entities are comparable to transactions between independent entities. There is a simplified regime for a limited range of transactions. Outside this limited range, a full transfer pricing analysis must be performed in order to determine arm's length remuneration. The arm's length principle is already incorporated in Article 33 of the Income

Tax Law, which allows the tax authorities to adjust reported taxable profits if transfer prices agreed between related parties differ from the prices that would have been agreed between independent entities.

Taxable profits for intragroup financing schemes which are in existence at July 1, 2017 will have to be recalculated based on two different sets of rules. The minimum margin scheme will apply for the first six months of 2017, and the new transfer pricing rules will apply for the second six months.

Extension of tax exemptions for loan restructuring

In December 2015, the Cyprus tax laws were amended to temporarily exempt loan restructurings from tax in order to facilitate and encourage the restructuring of non-performing loans. The amendments affected the Income Tax Law, the Capital Gains Tax Law, the Special Defence Contribution Law, the Stamp Duty Law, the VAT Law, the Collection of Taxes Law, and the Department of Lands and Surveys (Fees and Charges) Law. The amendments, which were effected by Laws 208(I)/2015 to 215(I)/2015, took effect on December 31, 2015.

In all of the laws a new definition of the term "restructuring" was introduced, referring to the direct or indirect sale and transfer of immovable property and transfer of rights under a sale contract deposited with the Department of Lands and Surveys, between one or more borrowers, debtors or guarantors regarding the same credit facility or debt and one or more creditors, in order to reduce or repay credit facilities or loans or debts granted to borrowers with one or more licensed credit institutions operating in Cyprus.

The exemptions introduced in 2015 were intended to be valid for two years from the date the various amending laws entered into force, and therefore would have expired on December 31, 2017.

However, Laws 131(I) of 2017 to 137(I) of 2017 inclusive, which were published in the government gazette on October 6, 2017, extend the exemptions for a further two years, until December 31, 2019.

Extension of accelerated writing down allowances

To stimulate the economy, the Income Tax Law was amended in 2012 to introduce accelerated capital allowances for tax purposes on assets purchased during the years 2012 to 2014 inclusive. The annual writing down allowance for plant and machinery was doubled from 10 percent to 20 percent (if a higher rate than 20 percent applied to the category of assets concerned, that higher rate continued to be available), and the annual writing down allowance for industrial buildings and hotels was increased from 4 percent to 7 percent. In 2015, as part of that year's economic stimulus package, the Income Tax Law was amended again to extend the new higher rates to assets purchased during 2015 and 2016.

Law 165(I) of 2017, which was published in the official government gazette on November 24, 2017, extends the higher rates for a further two years. For plant and machinery acquired up to the end of 2018 the annual writing down allowance rate will be 20 percent or any higher rate applying to the category of assets concerned, and for industrial buildings and hotels acquired up to the end of 2018 it will be 7 percent.

In addition, the new law introduces an annual writing down allowance of 7 percent for farm buildings and livestock production units acquired during 2017 and 2018.

Endnotes

1 For further details of these agreements, see *Global Tax Weekly*, Issue No. 127, April 16, 2015 (Bahrain); Issue No. 142, July 30, 2015 (Georgia); and Issue No. 189, June 23, 2016 (Latvia).

2 For a full analysis of the revised DTA with India, *see Global Tax Weekly*, Issue No. 213, December 8, 2016.

3 Full details of the DTA with Iran can be found in *Global Tax Weekly*, Issue No. 150, September 24, 2015.

4 A full analysis of the new DTA with Jersey can be found in *Global Tax Weekly*, Issue No. 198, August 25, 2016.

5 For further details of these agreements, *see Global Tax Weekly*, Issue No. 240, June 15, 2017 (Barbados); and Issue No. 241, June 22, 2017 (Luxembourg).

6 Full details of the changes can be found in *Global Tax Weekly*, Issue No. 244, July 13, 2017.

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Structuring Options For Individuals And The Unwanted Foreign Holding Company

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Introduction

Many taxpayers, particularly individuals, are in the habit of creating structures and making investments without consulting their tax advisors. This is seldom an ideal course of action, but it can be particularly dangerous in the foreign area, as the cross-border rules are complex and often far from intuitive. The purpose of this article is to describe certain structures in which individuals unwisely chose to hold assets through a foreign holding company, to explain the problems caused by the holding company, and to consider possible options for restructuring.

Scenario 1

Several years ago, Stuart, a US citizen residing in Florida, purchased a rental building (the "Building") located outside the United States, in the Republic of Freelandia, for USD1m.[1] For liability purposes, he did not purchase the building directly but instead organized a wholly owned Freelandia corporation ("Fco") to make the acquisition. Stuart dutifully told his accountant about Fco, and each year she prepared the necessary filings (*e.g.*, IRS Forms 5471 and 8938) to disclose Stuart's ownership of a controlled foreign corporation ("CFC").[2] She even addressed the Subpart F rules, concluding that Fco's net rental income was currently taxable to Stuart as foreign personal holding company income, *e.g.*, because the active rent exception set forth in Code Sec.

954(c)(2)(A) did not apply.[3] Fortunately, the Subpart F inclusions were minimal, so Stuart hardly noticed and was blissfully unaware that his tax structuring was less than ideal.

On October 1, 2017, a local developer offered Fco USD5m in cash for the Building. The Building had appreciated substantially, but even so this was a very generous offer. Stuart could not have been happier! Stuart spoke with the real estate broker in Freelandia and was advised that the USD4m of built-in gain will be subject to Freelandia corporate tax at a rate of 25 percent.[4] Stuart was a little disappointed at the prospect of paying USD1m of his hard-earned profits to Freelandia, but he cheered up when he realized he would have to pay roughly the same amount to the IRS anyway,[5] and he really did not care who got the USD1m of tax, so long as he could keep the other USD4m. Later that day, Stuart signed a contract on behalf of Fco, committing to sell the Building for USD5m on November 15, 2017.

The following week, Stuart was in a particularly good mood as he chatted with an acquaintance at a cocktail party about his great deal and what kind of yacht he should buy with the USD4m of after-tax proceeds. The acquaintance had a sinking feeling that something did not add up, so she urged Stuart to speak with someone about the US tax consequences of the sale. Stuart hated wasting time and money, but he did not want to offend his friend, so he agreed to hire Hilary, a local tax attorney, with some experience in cross-border matters.

Stuart met with Hilary and he explained that the engagement should not take her very long and should not cost him very much. Obviously, he said, the gain on "his" sale of the Building is capital gain, and the foreign tax "he" is paying to Freelandia qualifies for a foreign tax credit. Hilary made a few noncommittal grunts in reply and went to work. When she completed her analysis, and reported back, Stuart was in shock.

The first blow came when Hilary advised that capital gains rates do not apply. Hilary explained that, while Stuart could qualify for capital gains rates if he sold the Building, he cannot sell the Building because he does not own it: Fco does. She went on to explain that, under the special tax rules set forth in Subpart F of the Code, certain passive income of a CFC, such as gain from the sale of a building held for the production of passive rent income, generally is taxed to the CFC's US shareholder at *ordinary* income rates.[6] Stuart was not pleased.

Hilary then turned to the foreign tax credit issue. Unfortunately, she said, the wrong person will be paying the tax. While Stuart would qualify for a foreign tax credit (subject to applicable limitations) under Code Sec. 901 for Freelandia income taxes if such taxes were imposed on *him*, he cannot claim a credit for Freelandia income taxes imposed on Fco. Individuals are ineligible for the "indirect" foreign tax credit allowed to corporations under Code Sec. 902.[7] After turning a lovely shade of crimson and taking a few moments to regain his composure, Stuart asked Hilary if there are any steps that might be taken to obtain a better result. She promised to do some research and get back to him.

Hilary followed up several days later with a question and a proposal. First and foremost, Hilary asked if the sale could be put off until January 2018. Stuart made a face, as he did not wish to jeopardize the sale in any way, and asked Hilary if it was absolutely necessary. Hilary explained that, while the gain from Fco's sale of the building would normally be taxable to Stuart at ordinary income rates under Subpart F, such "inclusions" are required only if the foreign corporation is a CFC for an uninterrupted period of at least 30 days during the taxable year of the foreign corporation.[8] Hilary's plan was for Fco to elect to be disregarded as an entity separate from its owner as of January 2, 2018 (the "Election") and sell the Building on the same day, so that the 30-day requirement would not be satisfied.[9]

Hilary also had the foreign tax credit covered. She explained that, while the Freelandia income taxes on the sale will be paid by Fco in *form*, those tax payments should be treated as payments by Stuart for US federal income tax purposes because Fco will be a disregarded entity at the time such taxes are paid. This should be sufficient to convert the noncreditable indirect tax into a creditable direct tax. Hilary informed Stuart that, unfortunately, the Code does not allow the 3.8 percent "Medicare tax" to be offset by foreign tax credits,[10] but Stuart took it in stride.

There are some other technical details that Hilary included in her file memorandum but did not bother mentioning to Stuart. For example, Stuart's gain from the deemed liquidation of Fco will be recharacterized as a dividend, pursuant to Code Sec. 1248, but fortunately such deemed dividend should be a qualified dividend and should therefore be taxed at capital gains rates.[11] She also observed that the United States and Freelandia would have very different views of the transaction. From a US tax perspective, the tax is triggered by the deemed liquidation (and deemed dividend) arising from the Election to treat Fco as a disregarded entity; the subsequent sale of the Building triggers no US tax because the tax basis of the Building is "stepped-up" in the liquidation. From a Freelandia tax perspective, the Election is meaningless, and the tax is triggered by the sale of the Building.

After a bit of pondering, Hilary decided that none of these observations should make any difference. Code Sec. 904(a) generally limits the credit for foreign income taxes to the product of (1) the federal income tax otherwise imposed and (2) a fraction the numerator of which is the taxpayer's foreign-source taxable income and the denominator of which is the taxpayer's worldwide taxable income. Nothing in the mechanics of this limitation requires the transaction generating the foreign-source income to be precisely the same transaction that generates the foreign taxes. Pursuant to Code Sec. 904(d), the limitation is applied separately to separate "baskets" of income, but Hilary determined that both the deemed dividend and the Freelandia tax should be allocated to the "passive category income" basket.[12] There is a special rule for "base differences" that allocates foreign taxes to the basket for general category income when a foreign country taxes a type of item that does not constitute income under US tax principles,[13] but this is a fairly narrow category and would not apply merely because of a difference in tax basis.

The preamble to T.D. 8805 provides in part as follows:

> Treasury and the Service believe that a base difference exists within the meaning of §1.904-6(a)(1)(iv) only when a foreign country taxes items that the United States would never treat as taxable income, for example, gifts or life insurance proceeds. A sale that results in gain under foreign law but in loss for US tax purposes is attributable to differences in basis calculations rather than to a difference in the concept of taxable income and, therefore, does not constitute a base difference. The tax allocation rule of §1.904-4(c)(2)(ii)(A), allocating foreign taxes on a loss sale to the same group of passive income to which gain would have been assigned had the United States recognized gain on the sale, is conceptually consistent with the treatment of timing differences in §1.904-6(a)(1)(iv).

The example above specifically involves a transaction where a loss is realized for US tax purposes, but it should make no difference if, instead, there is no gain or loss under US tax principles.

Moreover, inasmuch as Fco's deemed sale of the Building arising from the Election and the actual sale of the Building by Fco following the Election are closely related, the IRS or a court might well view them as a single transaction for foreign tax credit purposes, if that were necessary in order to avoid a basket mismatch. In this regard, LTR 199918047 is instructive.

In LTR 199918047, a US subsidiary distributed shares of a foreign corporation to its US parent so that the US parent could then sell the shares to a third party. The subsidiary was subject to

US tax on the distribution (although such tax was deferred until the parent sold the shares of the foreign corporation), whereas the parent was subject to foreign tax on the sale. The problem that arose was that the gain on the distribution was US-source under the Code; it was resourced under an income tax treaty, but Code Sec. 865(h) provides that, as a condition of the treaty resourcing, the gain on the distribution must be placed in its own basket, potentially creating a potential mismatch since the foreign tax was imposed on the subsequent sale by the parent, not the initial distribution by the subsidiary. With little explanation, the IRS held that the foreign tax imposed on the parent's sale was "*related* to the gain derived [by the subsidiary on the distribution], and is therefore allocable to the separate section 865(h) income category for purposes of computing the foreign tax credit limitation." (Emphasis added.)

Following his conversation with Hilary, Stuart called the buyer. After some back and forth, and some consideration for the buyer's inconvenience, the closing was delayed. As Hilary had suggested, Fco elected to be classified as a disregarded entity, and Fco sold the Building, on January 2, 2018. Stuart was largely able to enjoy the favorable tax treatment that he originally anticipated and was finally quite pleased.

Scenario 2

The facts here are similar to those in Scenario 1, except Stuart owns Fco through an S corporation ("Sco"). Stuart gave Hilary a call.

Once she was fully briefed, Hilary explained that the basic problems are the same as in Scenario 1. Stuart understood why the Subpart F problem was the same but did not understand why Sco cannot claim an indirect foreign tax credit, since it is a corporation. Hilary patiently explained that, unfortunately, S corporations are treated as partnerships (or disregarded entities) for this purpose,[14] and that this makes sense, since the income earned by an S corporation passes through to the shareholders and is not subject to US federal corporate income tax.

Stuart did not like this answer but accepted it fairly gracefully since he assumed Hilary would recommend the same solution to the problem as in Scenario 1. He was surprised, however, and visibly upset, when Hilary advised that selling in January and electing to treat Fco as a disregarded entity would not suffice in this case. Unfortunately, Hilary explained, the deemed liquidation of Fco into Sco would be treated as a tax-free liquidation of a subsidiary under Code Sec. 332.[15] Normally, that is a good thing, but as the recipient of Fco's assets in a tax-free Code Sec. 332

liquidation, Sco would be subject to a corporate-level built-in gains tax, under Code Sec. 1374, when it sells the Building.[16] The built-in gains tax could be avoided by waiting until the five-year built-in gain period has elapsed, but that approach would hardly be feasible here, as Stuart expects to sell very soon. At Stuart's request, Hilary agreed to think further.

A week later, Hilary followed up and told Stuart that the Scenario 1 approach could work after all, but one critical change was needed. Before the entity-classification election takes effect, the ownership of Fco must be restructured so that Sco no longer owns stock meeting the 80 percent ownership requirement that must be met for Code Sec. 332 to apply.

As Hilary explained, Code Sec. 332 requires Sco's stock in Fco to represent 80 percent of both vote and value, so a restructuring that diminishes Sco's voting power in Fco below the 80 percent threshold should be sufficient to avoid the application of Code Sec. 332, even if Sco continues to possess nearly all of the equity in Fco. Upon Hilary's recommendation, Fco recapitalized immediately. Sco, which had held 100 shares of the only class of Fco stock, exchanged those shares for 99 shares of nonvoting common stock and one share of voting common stock.[17] Sco then distributed the one share of voting common stock to Stuart. Sco recognized gain on the distribution, and the gain passed through to Stuart, but the gain was attributable to only 1 percent of the stock, so Stuart could afford to be a sport. On January 2, 2018, Fco elected to be classified as a partnership and sold the Building.

Since the restructuring prevented Code Sec. 332 from applying,[18] the deemed liquidation arising from Fco's entity-classification election was fully taxable, just as in Scenario 1. Once again, Hilary saved Stuart's bacon, allowing him to enjoy capital gains rates (on a qualified dividend) and to claim a direct foreign tax credit for the Freelandia income tax paid by Fco.

Scenario 3

Junior, a close friend of Stuart, organized a Freelandia corporation ("Fco 2") several years ago to acquire three separate parcels of land (the "Properties") that have since appreciated substantially. Junior does not expect to sell any of them any time soon, and he has no particular reason to assume they will be sold at the same time. As in Scenario 1, Junior expects Fco 2 to pay Freelandia corporate income tax at a 25 percent rate. At Stuart's suggestion, Junior gave Hilary a call.

When they met, Junior told Hilary that he is totally familiar with the structuring she did for Stuart and is hopeful the same plan will work for him. Hilary explained that, unfortunately, the plan she implemented for Stuart would have the effect of marking Junior to market on all three Properties. If he expects to sell only one Property at a time, this may be extremely burdensome.

Fortunately, Hilary had another idea. She asked Junior if he could reasonably commit to waiting five years before selling any of the Properties and said that, if he can do so, the Subpart F and double tax problems can be eliminated, without any need to fit within the 30-day rule and without any other adverse consequences. The secret, Hilary explained, is to replace Fco 2 with a domestic corporation that elects S corporation status ("Newco") in a tax-free reorganization and then wait five years, until the built-in gain period has elapsed, before selling any of the Properties.[19] There are a number of possible mechanisms for replacing Fco 2 with Newco in a tax-free reorganization. A straightforward option is for Fco 2 to merge with and into Newco, with Newco surviving, as this should constitute an "A" reorganization described in Code Sec. 368(a)(1)(A). Alternatively, Junior can contribute the stock of Fco 2 to Newco and file an election to treat Fco 2 as a disregarded entity, which should be treated as an "F" reorganization described in Code Sec. 368(a)(1)(F), or alternatively a "D" reorganization described in Code Sec. 368(a)(1)(D).[20]

Junior would have preferred to avoid the five-year waiting period, but he viewed the Properties as long-term investments anyway and was willing to wait to solve his Subpart F and double tax problems.[21] He implemented Hilary's plan and, six years later, Newco sold the first of the Properties. Junior enjoyed capital gains rates and offset his federal income tax with a foreign tax credit. Another win for the good guys!

Endnotes

1 Everyone in Freelandia does business in US Dollars, so – mercifully – foreign currency issues are not presented.

2 Fco could have elected to be classified as a disregarded entity for US federal tax purposes, pursuant to Reg. §301.7701-3, but neither Stuart nor his accountant was familiar with this election.

3 Except as may otherwise be expressly stated, all "Section" references are to the Internal Revenue Code of 1986, as amended. The accountant also considered other exceptions, such as the high-taxed exception of section 954(c)(4), but sadly no luck there, either.

4 For the sake of simplicity, adjustments to basis for depreciation are disregarded. In addition, we shall also assume that the broker's understanding of Freelandia taxes is accurate (through brokers are not always the best source of accurate tax advice).

5 Rounding a bit, Stuart was thinking of the 20 percent long-term capital gains rate and the 3.8 percent Medicare tax, which comes to 23.8 percent in the aggregate.

[6] *See* Code Secs. 951(a)(1)(A)(i), 952(a)(2), and 954.

[7] There is an election that may be made under Code Sec. 962 to be taxed as a corporation, and this election essentially permits an individual to claim an indirect foreign tax credit, but the election comes at the cost of double taxation. Hilary determined that the election would not be desirable here and did not mention it to Stuart.

[8] Code Sec. 951(a)(1). It is assumed herein that Fco's taxable year is the calendar year. Pursuant to Code Sec. 898, Fco generally must use the same taxable year as Stuart, but a one-month deferral is permitted under Code Sec. 898(c)(2). If Stuart had been unable to push the closing to January, Hilary's fallback plan was to have Fco change to a taxable year ending November 30 and close in December.

[9] The deemed liquidation of Fco arising from the Election will be considered to occur immediately prior to the close of business on January 1, 2018. *See* Reg. §301.7701-3(g)(3). If the Election were instead effective as of January 1, 2018, the deemed liquidation would be considered to occur immediately prior to the close of business on December 31, 2017. Since Freelandia is fictional, the author asks the reader to take it on faith that Fco is an eligible entity.

[10] *See* Code Sec. 27 (allowing a foreign tax credit, to the extent provided under Code Sec. 901(a), against the tax imposed under Chapter 1 of the Code) and Code Sec. 1411 (imposing the "Medicare tax" under Chapter 2A of the Code). Hilary also determined that Stuart was not entitled to a credit under the US income tax treaty with Freelandia.

[11] Pursuant to Code Sec. 1(h)(11)(C)(i)(II), a foreign corporation that is eligible for the benefits of a comprehensive US income tax treaty that includes appropriate exchange-of-information provisions is (with limited exceptions not applicable here) a "qualified foreign corporation," the dividends of which generally constitute qualified dividend income under Code Sec. 1(h)(11)(B)(i). Thankfully, the United States and Freelandia are party to a comprehensive income tax treaty. Hilary determined that Fco qualifies for the benefits of that treaty, including under the treaty's limitation on benefits article.

[12] Pursuant to Code Sec. 904(d)(3)(D), the term "passive category income" includes dividends from a CFC to the extent allocable to earnings of the CFC attributable to passive category income. Since the Fco's gain from the deemed sale of the Building in connection with its deemed liquidation gives rise to passive category income (specifically, passive foreign personal holding company income under Code Sec. 954(c)), the dividend paid by Fco to Stuart should constitute passive category income under the look-through rule of Code Sec. 904(d)(3)(D). For the same reason, the Freelandia taxes imposed on the sale of the Building should also be allocated to the passive category income basket.

[13] *See* Reg. §1.904-6(a)(1)(iv).

[14] Code Sec. 1373(a).

[15] A deemed dividend would be triggered on any previously untaxed earnings of Fco under Code Sec. 367(b), but all of Fco's earnings to date have been taxed to Stuart under Subpart F.

[16] Pursuant to Code Sec. 1374(d)(8), the built-in gain rules apply to any asset acquired by an S corporation from a C corporation in a transaction where the S corporation's tax basis in the asset is determined, in whole or in part, by reference to the C corporation's tax basis in the asset.

[17] The exchange would appear to be a tax-free recapitalization under Code Sec. 368(a)(1)(E) and, moreover, a tax-free exchange of common stock for common stock under Code Sec. 1036.

[18] One may reasonably wonder whether the IRS or a court would allow Stuart to achieve this more favorable result through such a blatantly tax-motivated restructuring. However, the Tax Court has essentially characterized Code Sec. 332 as an elective provision and has been quite permissive in allowing taxpayers to elect out of Code Sec. 332 by manipulating ownership to avoid satisfying the 80 percent ownership requirements at the time of liquidation. *See G.L. Riggs, Inc.*, 64 TC 474, December 33,283 (1975).

[19] Alternatively, Hilary points out that the recognition of gain for US federal income tax purposes upon a sale could be avoided through a like-kind exchange under Code Sec. 1031, but for various business reasons, Junior was not interested.

[20] *See* Rev. Rul. 87-66, 1987-2 CB 168. The second approach may well be preferable from a Freelandia tax perspective.

[21] Furthermore, Hilary explained to Junior that if he were to sell one of the Properties during the built-in gain period he would have double tax issues with respect to that particular Property, but the structure would still be effective for the other two Properties. She also suggested that, with a reasonably cooperative buyer, they might work out an arrangement involving leases, puts and calls that defers the sale for a period of time but transfers significant benefits and burdens of ownership to the buyer (provided the parties are not too greedy).

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The European Union's Digital Tax Agenda

by Stuart Gray, Senior Editor, Global Tax Weekly

The EU has emerged as the leading candidate to offer concrete solutions to the challenge of ensuring the appropriate taxation of the digital economy. This article considers the European Commission's proposals to pin down the income of nebulous digital business models, and tax it.

The Future Is Digital

Against the backdrop of the OECD's BEPS project, tax reforms to reduce opportunities for the avoidance of direct and indirect taxes in general are a priority for governments globally. However, the EU considers that ensuring more effective taxation of digitalized companies has become critical given digital firms' rapid growth over the last decade and the relatively low effective rates of tax that they pay.

According to the European Commission,[1] only one digital company was among the top-20 firms by market capitalization in 2006, accounting for just 7 percent of the market capitalization. But by 2017, there were nine such companies in the top-20, accounting for 54 percent of total market capitalization.

The top five e-commerce companies' revenue growth has also massively outpaced that of "traditional" retailers, says the Commission. These e-commerce firms saw their revenues grow by 32 percent per year on average between 2008 and 2016, while revenue in the entire EU retail sector grew on average by 1 percent per year.

The Commission concludes in a fact sheet released as part of its digital tax strategy that the current pace of technological developments means that the digitalization is only going to become more pervasive across the global economy. It says:[2]

> "A new generation of information technologies will spur the development of the internet of things, artificial intelligence, robotics and virtual reality. Digital solutions are increasingly used and open up new opportunities for people, businesses, investors and public administrations."

There is already a debate taking place among academics and policymakers about how these technologies might impact societies and economies in the future. But how might these developments impact the world's treasuries? Based on the Commission's estimations, quite severely if current trends continue. It has calculated that domestic digitalized business models are currently subject to an effective tax rate of only 9 percent. Cross-border digital businesses, it claims, are able to reduce their exposure to tax to as low as zero, a fact largely attributable to their heavy reliance on intangible assets, which are highly mobile.

So the challenge as the Commission sees it is to "make the most of these digital opportunities to ensure Europe's competitiveness, while ensuring fair taxation." However, reforming international tax rules first designed in the early 20th century to ensure in the 21st century that digital company profit is taxed where value is created is a challenge in itself. For traditional "brick-and-mortar" businesses, with factories, offices, and warehouses – *i.e.*, a strong physical presence – these rules are still largely relevant. For digital companies, it is much harder to pinpoint where value is created, or indeed to quantify this value in the first place.

Digital Business Models

But what exactly is a "digital business"? The Commission groups them into five broad categories, as follows:

- Digital platforms granting access to a marketplace: these typically involves two services – access to users in exchange for a fee (either subscription or transaction based), and services offered by users among themselves;
- Digital platforms granting access to content: these offer access to a platform and to content such as music or video in exchange for a fee;
- The social media and advertising model: this offers access to social media networks and/or search engines for free, with users' personal data sold on to advertisers and other businesses;
- The distant sales model: goods are sold via a website before being physically transferred, with revenues generated from the sale of goods; and
- The collaborative platform model: this enables individuals to share "access" to assets rather than own them outright.

Taxing Rights And Profit Attribution

As part of its deliberations on this matter, the Commission has identified changes to international guidance on transfer pricing rules and definitions of permanent establishment as key to solving the problem. In other words, establishing and protecting taxing rights in a country where businesses can provide services digitally with little or no physical presence despite having a commercial presence; and attributing profit in new digitalized business models driven by intangible assets, data, and knowledge.

For example, in the case of a social media network run by a business located outside the EU, despite the company generating considerable income from selling information on its users, who are able to freely access the network, to advertisers (who deliver targeted marketing messages via the network), it does not have a taxable presence in the EU. "Under the current international tax framework, the business is not subject to corporate tax in the EU," the Commission observes.

In another example, the Commission describes how digital companies can shift mobile intangible assets between jurisdictions to substantially reduce their exposure to tax:[3]

> "Company A is located in a low-tax country outside the EU and owns the intellectual property for the multinational group. Companies belonging to the same group in the EU pay royalty fees to company A for the use of the intellectual property. Company A charges very high prices to the companies in the EU for these royalty fees, which facilitates the shifting of profits to company A in the low tax country. The current transfer pricing rules are unable to challenge the inflated prices charged for the royalty fees because they do not have a comparable transaction in the independent market and it is hard for the tax authorities to determine what the value of the intellectual property really is."

Short- And Long-Term Solutions

In a consultation exercise launched by the Commission on October 26, 2017,[4] it was conceded that developing new permanent establishment definitions and transfer pricing rules is a long-term project which is likely to need input from the international community. However, it also proposed some short-term, temporary solutions as part of a two-pronged strategy.

The consultation explains that the following temporary options have been identified:

- A tax based on revenues generated from "digital activities";

- A withholding tax based on payments to non-resident providers of goods/services ordered online;
- A tax based on revenue from digital transactions concluded remotely with a non-resident entity that has a significant economic presence; and
- A digital transaction tax that applies early in the value creation process.

The possible long-term solutions include:

- New permanent establishment and profit attribution rules introduced through a modified proposal for a common consolidated corporate tax base (CCCTB);
- New EU rules for permanent establishment and profit attribution to capture digital activities of businesses in a stand-alone EU Directive;
- The introduction of a destination-principle to corporate taxation, according to which the jurisdiction to tax is based on the consumer's location;
- A tax on a share of the world profit of digital companies, which could be attributed to each country on the basis of the percentage of revenue earned in that country; and
- A system where the profits of a company are declared and taxed in the member state of establishment – as is currently the case – but with the applicable rate being the turnover-weighted average of the tax rates of the countries where the turnover is generated.

CCCTB – The Preferred Solution

While these ideas are quite wide-ranging, the Commission has let it be known that its preferred option is the proposed CCCTB, which already provides an EU framework for revised permanent establishment rules and for reallocating the profit of large multinational groups using the formulary apportionment approach on the basis of assets, labor, and sales. This system, argues the Commission, should better reflect where the value is created. This proposal, it said, can also be adapted to ensure that "digital activities are effectively captured."

The CCCTB is a single set of rules that companies operating within the EU would use to calculate their taxable profits. Initially presented in draft form by the Commission in 2011, the CCCTB was repackaged and re-released in 2016 [5] after member states failed to agree on the original proposals.

The idea is that a company or group of companies would have to comply with just one EU system for computing its taxable income, rather than different rules in each member state in which it operates. In addition, under the CCCTB, companies active in more than one EU member state would only have to file a single tax return for the whole of their activity in the EU.

The single consolidated tax return would be used to establish the tax base of the company, after which all member states in which the company is active would be entitled to tax a certain portion of that base, according to a specific formula based on three equally-weighted factors – labor, assets, and sales by destination.

The CCCTB would be mandatory for large multinational groups with global revenues exceeding EUR750m (USD890m) – *i.e.*, the same threshold for country-by-country reporting requirements under the OECD's BEPS recommendations. However, these proposed reforms have faced ongoing political opposition from certain member states in the European Council, and so their introduction is far from guaranteed.

The Rise Of Unilateralism

But where is the OECD in all of this, and what of multilateralism under the banner of the BEPS project? The Commission makes clear that, ideally, new tax measures for digitalized companies would be developed at global level, "to ensure a consistent and comprehensive approach." However, it is also worried that different approaches being proposed and put into practice by individual EU member states could splinter the single market and "destabilize the level playing field," while increasing tax uncertainty and opening new channels for tax avoidance.

The United Kingdom is a particularly prominent example of a member state taking digital tax matters into its own hands. Indeed, a paper published alongside the 2017 Budget on November 22 [6] states the Government's belief "in the principle that a multinational group's profits should be taxed in countries in which it generates value," and, in a somewhat contradictory follow-up statement, goes so far as to state that the UK has taken "bold unilateral action where needed" as it led the implementation of the BEPS outputs. Examples include the controversial diverted profits tax, and the recently proposed withholding tax on royalties and payments for certain other rights made to low- or no-tax jurisdictions in connection with sales to UK customers.

Ominously perhaps for the OECD as it attempts to hold together an increasingly fractious coalition, the UK Government declares in the paper that "there is still more to be done." Pending reform of the international framework, the Government intends to explore interim options to raise revenue from digital businesses that generate value from UK users, such as a tax on revenues that these businesses derive from the UK market. And while it will continue to work with other countries to consider how such a tax could be targeted, designed, and coordinated, the paper states that the UK "stands ready to take further unilateral action in the absence of sufficient progress on multilateral solutions."

So by taking leadership of this issue, the Commission is attempting to get member states to rally around a single set of proposals. However, it is also hoping to influence the international debate on taxing the digital economy. "A common EU approach will strengthen our position in the international discussions to push for progress on this issue and the development of meaningful, multilateral solutions," it says.

But by seeking to head off unilateral responses at member state level, businesses warn that the EU approach to digital taxation could diverge from that decided at global level, with likely negative consequences. These include a more fragmented and uncertain international tax environment, and the possibility that specific digital tax measures would conflict with long-established principles in international taxation, such as those laid down in double taxation avoidance treaties.

Commenting on the proposal to develop a turnover (or equalization) tax, the International Chamber of Commerce has said that such a measure would not only negate generally accepted principles of taxing corporate profits, by taxing turnover, but could also have a negative impact on the solvency of, or investment opportunities for, businesses:[7]

> "Adopting an equalization levy would also adversely affect EU competitiveness and risk economic growth in the region. Some other options under consideration, such as a withholding tax on digital transactions, may also conflict with double-taxation treaties' general principle under which business profits should only be taxable in the state where the provider of the service is located."

Bernhard Welschke, Secretary General at the Business and Industry Advisory Committee to the OECD, has also expressed deep concerns that unilateral action for the taxation of the digital economy will lead to serious distortions in markets and global value chains:[8]

> "We recognize there are important and complex issues concerning the digitalization of our economies. However, unilateral action in this field will lead to costly fragmentation and threatens to diminish the considerable potential for growth and innovation. Only a comprehensive multilateral engagement between tax authorities, taxpayers, and other stakeholders will lead to outcomes that support a successful digital transformation."

And Carol Doran Klein, international tax counsel at the United States Council for International Business, has echoed these sentiments:[9]

> "For business to flourish in the digital economy, tax rules must be implemented in a coherent and coordinated manner. Fragmented rules are likely to result in double taxation and a negative impact on global trade and investment."

Next Steps And The Way Forward

The Commission's consultation will close on January 3, 2018.[10] In the meantime, the Commission continues to work on the detail for new proposals on digital taxation, which it will present in the spring of 2018. The contributions to the consultation and a report on the feedback received will be published in the first quarter of 2018.

For now, these ideas are very much at the formative stage, but with some member states as skeptical of their merits as parts of the business community, actually legislating for them at EU level could be a long and difficult process, if indeed doing so is possible at all.

Perhaps the key point here is that on this issue, the EU has shown a determination to break with the global consensus on BEPS currently held together by the OECD. That such an influential member of the international community is doing so could have major ramifications for the outcomes of the project as a whole.

Endnotes

1 http://europa.eu/rapid/press-release_MEMO-17-3341_en.htm

2 *Id*.

3 *Id*.

4 https://ec.europa.eu/info/consultations/fair-taxation-digital-economy_en

5 http://europa.eu/rapid/press-release_IP-16-3471_en.htm

6 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/661458/corporate_tax_and_the_digital_economy_position_paper.pdf

7 https://iccwbo.org/media-wall/news-speeches/icc-expresses-concern-eu-proposals-new-taxation-policy-digital-economy/

8 http://biac.org/wp-content/uploads/2017/09/2017-09-28_BIAC-promotes-a-multilateral-effort-for-addressing-the-tax-ch.._.pdf

9 https://www.uscib.org/multilateral-effort-needed-to-address-tax-in-digital-economy/

10 *Supra*, note 4.

Topical News Briefing: Time To Build Bridges On The Hill

by the Global Tax Weekly Editorial Team

As reported in this week's issue of *Global Tax Weekly*, the US Senate approved a heavily edited version of the tax reform bill that was passed by the Finance Committee last month, putting a comprehensive tax reform bill a step closer to the President's desk.

Indeed, it is now not out of the question that the legislative process can be wrapped up before lawmakers head off for their Christmas break later this month, as Republican leaders had hoped when the process began. It is certainly the case that we are nearer to witnessing a long-called-for shake-up of the US tax code than at any point in the last 30 years.

But, while there are reasons for optimism, there is also cause for some measure of caution.

That the Senate version has gone through some major changes reflects that, politically, this is a sensitive piece of legislation. It passed by the narrowest of margins – 51 votes to 49 – with a number of amendments designed to appease the concerns of several Republican members of the Senate over issues like individual tax deductions, small business taxation, and the legislation's impact on the federal budget deficit.

And as a result of these changes, there are many gaps that now need bridging between the version of the Tax Cuts and Jobs Act (TCJA) passed by the House of Representatives last month, and the TCJA approved by the Senate on December 1.

Corporations at least can be fairly confident that corporate tax will be slashed from 35 percent to about 20 percent. However, a particularly wide chasm continues to exist in the key area of pass-through business-income taxation. The Senate bill now includes a 23 percent deduction on pass-through income, up from the previous rate of 17.9 percent, after several Republican Senators complained that the original version was too in favor of large corporations. However, the income-deduction approach remains vastly different to the 25 percent tax cap provided by the House-approved bill.

Controversially, in an attempt to keep overall costs of the tax bill down, both the individual and corporate alternative minimum taxes would be retained by the Senate bill, whereas the House bill would eliminate both.

Individual tax rates differ between the two bills, from the House's five-bracket schedule (which includes a zero percent rate) to the Senate's seven-tier regime, while the House voted to repeal the estate tax, yet the Senate would merely increase the estate tax exemption on a temporary basis.

Indeed, to ensure that the TCJA doesn't add to the deficit beyond a ten-year budget window – a crucial requirement for the bill to avoid higher procedural hurdles in the Senate and to pass with a simple majority – many of the Senate's individual tax reform provisions, unlike the House's, are set to expire from 2025, raising the prospect that they would have to be periodically extended by Congress.

Legislating for temporary tax reform is hardly an ideal solution, given the headaches that temporary tax measures have given taxpayers and lawmakers in recent years, but it's evident that many compromises have already been made to make the tax reform bill politically acceptable, and many more could be made in the weeks ahead as lawmakers work to reconcile the two bills.

Russia's Federal Tax Service Issues Recommendations On Applying Article 54.1 Of The Tax Code (The Abuse Of Law Concept)

by Alexei Nesterenko and Ivan Rodionov, EY, Moscow

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What Has Happened?

On August 19, amendments to the Tax Code were made in the form of the introduction of Article 54.1, "Limits on the Exercise of Rights Relating to the Calculation of the Tax Base and (or) the Amount of a Tax, a Levy or Insurance Contributions."

On October 31, the Federal Tax Service issued detailed recommendations on applying the provisions of Article 54.1 of the Tax Code,[1] setting out its interpretation of the abuse of law concept, explaining how circumstances indicating abuse of law should be proven, and giving examples of such circumstances.

What's New?

The provisions of clause 1 of Article 54.1 prohibit a taxpayer from reducing the tax base by misrepresenting information on economic events and objects of taxation.

According to clause 2 of Article 54.1, where the circumstances specified in clause 1 do not exist for transactions (operations) which have taken place, the taxpayer has the right to reduce the tax base and (or) the payable amount of tax in accordance with the rules of the relevant chapter of Part Two of the Tax Code provided that the following two conditions are simultaneously met:

1. It is not the main purpose of a transaction (operation) to enable the non-payment (incomplete payment) and (or) crediting (refund) of an amount of tax;

2. The obligation arising from a transaction (operation) has been fulfilled by a person who is a party to a contract concluded with the taxpayer and (or) a person to whom the obligation to perform the transaction (operation) was transferred by contract or by law.

It is explained in the Letter that Article 54.1 represents a new approach to the problem of the abuse of rights by taxpayers, rather than a codification of the rules formulated in Ruling No. 53 of the Plenum of the Supreme Arbitration Court of October 12, 2006 "Concerning the Evaluation by Arbitration Courts of the Legitimacy of the Receipt of a Tax Benefit by a Taxpayer."

In the Letter, the misrepresentation of information on economic events is understood to include:

- Business splitting schemes;
- Actions aimed at artificially creating conditions required for the use of reduced tax rates, reliefs and exemptions;
- Schemes aimed at the improper application of tax treaty provisions;
- The absence of actual performance of a transaction (operation) by the parties involved;
- The non-disclosure by a taxpayer of income from sales of goods (work, services and property rights), including by reason of the involvement of persons controlled by the taxpayer;
- The provision by a taxpayer of knowingly false information on objects of taxation.

It follows from the text of the Letter that tax authorities must, on finding that information on economic events/objects of taxation has been misrepresented, prove all of the following circumstances:

- The substance of the misrepresentation;
- The causal link between the taxpayer's actions and the misrepresentations that have occurred;
- The premeditated nature of the taxpayer's actions, consisting in the conscious misrepresentation of information on economic events for the purpose of reducing the tax base;
- Losses to the budget.

It is stated in the Letter that the law places limits on a taxpayer's right to claim expenses and deductions in respect of a transaction where, in particular, the following circumstances exist:

1. The transaction was performed by a person other than the person specified in primary documents;
2. The occurrence of a business decision outside the normal run of business without a specific reasonable economic (business) purpose;
3. The main purpose of the transaction (operation) was to secure a tax saving;

4. There is no reasonable explanation for the conclusion and performance of the transaction (operation) from the point of view of business necessity;
5. There are indications of artificiality;
6. Related documentation is purely formal in nature.

What May Be Expected?

The Letter sets out the mechanisms by which tax authorities must disprove the genuineness of a disputed transaction, and in particular:

- Obtaining explanations from persons possessing information on the circumstances of the conclusion and performance of a transaction (operation);
- Conducting technology-aided inspections of sites, premises, documents and objects;
- Collating quantities of goods supplied with the size of storage premises (sites);
- Conducting an inventory of assets;
- Analyzing and recreating an enterprise's full balance sheet (product balance sheet, warehouse records, *etc.*);
- Requesting documents (information) and, where necessary, seizing documents (objects);
- Questioning officers of the taxpayer being inspected who are involved in production activity;
- Requesting documents (information) from clients and questioning their officers and persons in charge of technical supervision;
- Identifying other, "non-problematic" contract partners that perform similar work and services for the taxpayer, and carrying out control procedures in relation to them;
- Examining internal regulations on the establishment of access control for guarded facilities, entry passes and logbooks;
- Identifying documentation anomalies and deviations from normal business conduct by parties to a transaction (operation) and officers of a taxpayer in concluding, supporting and documenting the results of transactions (operations);
- Conducting expert examinations (handwriting analysis and other kinds), *etc.*

However, in carrying out tax control measures, tax authorities must consider the appropriateness of each individual information gathering mechanism rather than formalistically working through the entire range of mechanisms.

It is worthwhile adding that the process of proving the existence of the circumstances specified in clause 1 of Article 54.1 and (or) non-compliance with the conditions of clause 2 of that Article must take place in the context of tax control measures conducted by a tax authority.

This means that the principle of the presumption of a taxpayer's good faith, one of the core elements of the constitutional framework of tax regulation and public order, remains essentially intact.

How Should Companies Prepare For The Changes?

In order to be in compliance with the new legislative requirements and reduce the likelihood of disputes with the tax authorities, it is advisable for companies to proceed as soon as possible:

- To make an inventory of current contract partners and the current process for checking them;
- To update control systems;
- To develop a format for supporting documentation ("defence file");
- To automate control systems.

EY is ready to assist taxpayers at each stage of preparing for the implementation of the new requirements, including:

- Assessing the risk of current suppliers being classed as bad-faith taxpayers in the context of Article 54.1 and quantifying the scale of the problem;
- Considering the extent to which the company's current model for checking suppliers meets the new requirements of Article 54.1 and assessing vulnerabilities, including by:
  - Analyzing the provisions of standard contracts with suppliers;
  - Analyzing the company's business processes and internal control system at the stage of client acceptance and contract performance;
  - Analyzing internal regulations (policies, procedural rules) governing the checking of contract partners;
  - Analyzing the features of current IT systems;
- Updating the control model, including by developing standard contract provisions, regulating processes, and developing control procedures for checking contract partners;
- Developing the format and structure of the "defence file" to be used in potential disputes with the tax authorities;
- Assessing the scope for automating control procedures and facilitating the implementation of automated solutions.

Endnote

1 Letter No. YeD-4-9/22123@ of the Federal Tax Service of October 31, 2017 "Concerning Recommendations on Applying Article 54.1 of the Tax Code of the Russian Federation" ("the Letter").

Recent Tax Developments In Brazil

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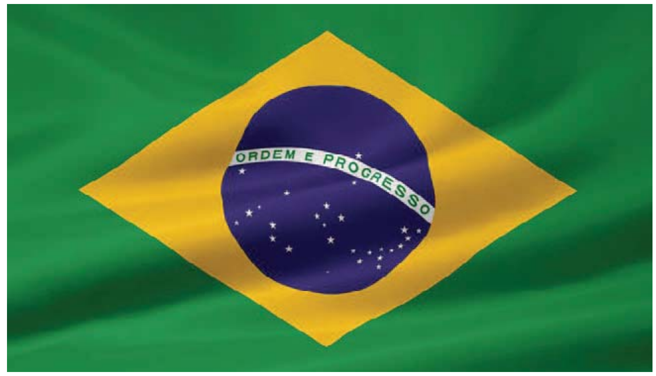


Taxation Of Capital Gains Earned By Non-Residents

Normative Instruction of the Brazilian Federal Revenue Service ("IN RFB") 1732/17, published on August 29, 2017, introduced changes in IN RFB 1455/14, which previously established the levy of 15 percent Withholding Income Tax ("WHT") on capital gains obtained by legal entities domiciled abroad upon the disposal of goods and rights located in Brazil.

IN RFB 1732/17 establishes the levy of Income Tax under progressive rates, which can be calculated based on the practical table below:

Taxable Basis	Rate (percent)	Deductible Share
Up to BRL5m (USD1.5m)	15%	—
From BRL5.1m up to BRL10m	17.5%	BRL125,000.00 (USD39,000)
From BRL10.1m up to BRL30m	20%	BRL375,000.00 (USD117,000)
Higher than BRL30.1m	22.5%	BRL1.125m (USD350,000)

This Normative Instruction also provides that:

i. The tax will be paid by the last business day of the month following the capital gain ascertainment;
ii. In case of disposal of the same asset in different transactions, if the second transaction occurs before the end of the calendar year following the first transaction, the capital gains arising as a result of the second transaction shall be added to the gains earned on the previous transactions, deducting the tax amount previously paid;
iii. The previous 15 percent WHT rate applies for taxable events which occurred until December 31, 2016 with the progressive rates applying as of January 1, 2017; and

iv. The tax should be withheld by the acquirer, if domiciled in Brazil, or its representative when the acquirer is domiciled abroad.

The levy of Income Tax using progressive rates on capital gains earned by individuals domiciled in Brazil was established by Law 13259/16 and entered into force as of January 1, 2017.

Since the publication of such Law, we understand that the progressive rates apply to capital gains earned by non-residents, regardless of whether they are individuals or legal entities, in light of Article 18 of Law No. 9249/95 ("the capital gain earned by a non-resident will be calculated and taxed in accordance with the rules applicable to Brazilian residents") and that the rules applicable to non-residents are those that regulate the taxation of individuals that are Brazilian residents.

Finally, if the beneficiary of the gain is tax resident in a country with favorable taxation, a WHT of 25 percent rate applies, regardless of the amount of capital gain.

Amending Protocol To The Brazil–Argentina Double Tax Treaty

Brazil and Argentina on July 21, 2017, signed an amending protocol to the Brazil–Argentina Double Tax Treaty. Among the main changes, we highlight the following:

i. Inclusion of rate limits on the payment of dividends (10 percent/15 percent), interest (15 percent), and royalties (10 percent/15 percent)[1], in case of taxation of the income in the source country;
ii. Inclusion of the concept of "technical services and technical assistance" provided by Brazilian tax legislation [2] for the purposes of Article 12 ("royalties") application;
iii. Replacement of the tax exemption in (a) Brazil of dividends received from Argentina; and (b) Argentina of income arising from Brazil for the offsetting of taxes; and
iv. Inclusion of a Limitation of Benefits ("LOB") clause, restricting the use of the treaty in abusive situations.

The amending protocol must still be incorporated in the domestic legislation of each country (in Brazil, the protocol shall be approved by the National Congress and enacted by the Executive Power).

The bilateral change on the Brazil–Argentine Double Tax Treaty shows the option of Brazil changing its double tax treaties bilaterally instead of modifying them by means of multilateral instrument.

ENDNOTES

1 The 10 percent rate on royalties applies to technology transfer agreements duly registered in accordance with domestic legislation and payments for the use of literary, theatrical, musical or any kind of artistic works, including software, to the author or successors.

2 The Brazilian Federal Revenue Service defines "technical services and technical assistance" as services rendered with the use of any specific knowledge or that involves administrative assistance or consultancy services, performed by independent professionals or under labor agreements or related to automated structures with clear technological content. As this definition is very broad, it encompasses almost all services, irrespective of any transfer of technology, even comprising services that are not usually classified as "technical" in other countries.

Topical News Briefing: Free Zones The New Black(listed)?

by the Global Tax Weekly Editorial Team

Companies operating in one of the world's many thousands of free zones often pay little in tax. Yet, such zones rarely attract the sort of criticisms that "tax havens," and the companies operating in them, do.

This issue is a particularly pertinent one at present, given that the European Union (as reported in this week's issue of *Global Tax Weekly*) has just issued its new blacklist of non-cooperative tax jurisdictions, while China is strengthening its links with free zones worldwide as part of its "Belt and Road" economic strategy.

Indeed, "tax havens" in the most pejorative sense of that phrase have dwindled in number in recent years, while free zones, the modern versions of which began to emerge in the aftermath of World War II, have continued to grow rapidly, reaching 5,000 by 2008, according to the OECD.

But are tax havens and free zones really all that alike? In some respects, yes. Companies qualifying for free-zone status are usually accorded legal, regulatory, or fiscal privileges – or a combination of some or all of these – not available to actors in the regular economy. Typically, these can include exemption from corporate income taxes, sales taxes, or value-added taxes; lower rates of tax on outbound dividend payments; no customs duty on goods temporary stored within the zone; reductions to import and export duties; and less stringent labor laws.

Also, many free zones are characterized as having a degree of autonomy from the government, and it is common for zones to be administered wholly by private sector organizations or under a public–private sector arrangement.

All quite reminiscent of a tax haven, one might conclude.

However, while traditional offshore jurisdictions are very much centered on finance, free-zone regimes are often skewed towards encouraging investment in certain industrial operations, the export of physical goods, and high-technology businesses. Indeed, their prevalence in emerging economies, particularly in Latin America and Asia, suggests they are increasingly being deployed by governments to quicken the pace of economic development and industrialization, and to provide high-skilled, well-paid jobs.

China has used free zones extensively as part of its wider economic modernization strategy. Indeed, increasingly, free zone operations are the economy itself in China; according to the World Free Zone Organization, China has more than 200 free zones, and these accounted for almost half of its exports in 2009. For example, the Shanghai Pilot Free Trade Zone, composed of a bonded area, high-tech park, financial area and export processing zone, and offering a number of tax preferences, is one of the China's fastest-growing free zones despite being one of its newest.

So are free zones merely the new tax havens, with their tax exemptions and other generous tax concessions? Perhaps. But the sorts of "harmful" tax regimes in the sights of the OECD and the EU at present are those that lead to the separation of profits from economic substance, particularly intellectual property tax schemes such as patent and royalty boxes. By contrast, free zones tend to encourage the shifting of production, rather than of profits.

Furthermore, the OECD's final report on Action 5 of the BEPS project, which focused on harmful tax regimes, stated that current concerns are as much about a lack of transparency, especially in connection with certain rulings, as they are about the tax rules themselves.

The vast majority of free zones therefore appear to be outside the scope of the BEPS initiatives and are likely to remain so while the separation of profits from substance and transparency are the major concerns. What's more, their promotion by the Chinese Government suggests that free zones have a long future in those jurisdictions keen to embrace Chinese investment.

US Lawmakers In Final Tax Reform Push

The Senate and the House of Representatives have formed a committee to finalize a consolidated Tax Cuts and Jobs Act, which Treasury Secretary Steven Mnuchin said should be presented to President Trump within the month.

"In the weeks ahead, we will send a bill to the President for the first time in 31 years that cuts taxes for families and job creators and ushers in a new era of economic growth," said House Ways and Means Committee Chairman Kevin Brady (R – Texas) on December 4, after being appointed to the Committee. "We are committed to delivering by the end of the year bold tax reform that creates more jobs, bigger paychecks, and fairer taxes."

A majority of both the House and the Senate delegations must sign a conference report representing the final agreed version of the tax reform bill. This will then go to both the House and Senate floors for a final vote, following which the bill will be sent to the President.

"I look forward to working with the House and Senate to send legislation to the President's desk this month," said Treasury Secretary Steven Mnuchin in a statement on December 2.

US Commerce Chamber, Tax Foundation Criticize JCT's Tax Bill Scoring

The Joint Committee on Taxation (JCT) failed to accurately estimate the economic impact of the Senate tax bill in its latest analysis, both the US Chamber of Commerce (USCC) and the Tax Foundation (TF) have claimed.

On November 30, the JCT released its dynamic scoring estimate of the Senate tax bill, which found that the proposal would increase the level of economic output by 0.8 percent per year over the ten-year window – substantially lower than the 3–5 percent growth rate estimated by the White House Council of Economic Advisors in October.

It stated that would increase revenues by USD458bn, reducing the amount the tax reform package will add to the deficit from USD1.414 trillion to just over USD1 trillion, after taking into account increased debt-servicing costs.

J. D. Foster, Senior Vice-President of the USCC's Economic Policy Division and Chief Economist, disagreed with the JCT analysis in a statement released on November 30.

"Credible analysis of the House and Senate bills, whether based on educated judgment or economic modeling, put the expected additional growth from tax reform in the range of 2 percent to 5 percent of GDP," he said.

He suggested the JCT analysis was based on "ill-chosen" assumptions and used incorrect predictions of potential Federal Reserve interest rate movements in its analysis, resulting in a lower prediction of annual growth.

"The JCT… cannot produce credible dynamic analysis," he said. "The JCT's work in this area should be quickly consigned to the circular file and serious questions raised as to the JCT's future in dynamic analysis."

Dynamic scoring (as opposed to static scoring), which has been championed for some time by the Republican Party, is said to recognize that tax changes do affect economic growth. For example, dynamic scoring assumes that reduced taxation will encourage work, saving, and investment, and increase economic growth, thereby raising the amount of revenue above the value predicted by static estimates.

"Static" revenue estimating techniques meanwhile assume that tax policy changes have no impact on the economy's performance. This methodology has been widely criticized on the grounds that it could provide policymakers with inaccurate numbers and create a bias against lower tax rates.

The TF raised similar concerns about the JCT report. "JCT's results should be viewed as likely underestimating the economic growth spurred by this tax bill," it said on November 30. "The range of estimates from JCT includes several important assumptions that limit its growth results, particularly, assumptions regarding the Federal Reserve's response to potential inflation and the United States being an open economy that assumes financial flows don't change quickly."

In a closed economy, businesses are limited to domestic savings for investment, which would be eroded by increased government borrowing, thus "crowding out" the opportunity for small businesses to invest. However, in an open economy, savings from foreign investors are also available.

"US businesses have access to a plethora of savings. As long as there are economically viable projects, foreign investors funnel savings into the US to take advantage of the opportunity. Moreover, US investors with assets in foreign countries can choose to sell their investment abroad and purchase US assets," said the TF.

Both the TF and the USCC suggested that the Federal Reserve would be unlikely to raise interest rates in response to the increased demand for investment, as assumed by the JCT. "The JCT's score includes Federal Reserve activity that would counteract the economic expansion from tax cuts," said the TF. "Given the interest rate is functionally near zero, it is unlikely that the Federal Reserve will increase the rate above and beyond its current schedule, which has already been priced into the economy."

US Senate Tax Bill Best For America's Top Earners

Individual tax cuts in the Senate's US tax reform bill would disproportionately cut taxes for wealthy individuals, the Tax Policy Center (TPC) said.

The TPC has released distributional estimates of the Tax Cuts and Jobs Act based on the bill passed by the Senate on December 2, 2017.

According to the TPC, compared with current law, "taxes would fall for all income groups on average in 2019, increasing overall average after-tax income by 1.6 percent. In general, tax cuts as a percentage of after-tax income would be larger for higher-income groups, with the largest cuts as a share of income going to taxpayers in the 95th to 99th percentiles of the income distribution."

"The pattern of tax changes across income groups would be similar in 2025 (the last year before nearly all the individual provisions sunset) although the magnitude of average tax decreases would be slightly smaller for most income groups."

"In 2027, the overall tax reduction would be just 0.3 percent of after-tax income. On average, relative to current law, low- and middle-income taxpayers would see little change and taxpayers in the top 1 percent would receive an average tax cut of 1.1 percent of after-tax income."

In terms of its impact on the economy, the TPC estimated that the legislation would boost GDP by 0.7 percent in 2018, and by 0.1 percent in 2027.

The analysis stated that the increase in taxable incomes would reduce the revenue loss arising from the legislation by USD179bn from 2018 to 2027.

In comparison, the White House Council of Economic Advisors has predicted higher GDP growth of between 3 and 5 percent as a result of the tax plan. The Joint Committee on Taxation in its latest dynamic scoring of the Senate proposal suggested a lower economic impact, of boosting GDP growth by 0.8 percent.

Countries Faster To Resolve MAP Cases Following BEPS Action 14

A new report from the OECD says countries are concluding Mutual Agreement Procedure (MAP) cases, to resolve businesses' double tax issues, more quickly following the international agreement on BEPS Action 14.

The OECD said it is now receiving considerably more information on countries' MAP activities, since members of its Inclusive Framework on tackling BEPS agreed to provide MAP statistics to the OECD and in a uniform way.

Releasing the stats for 2016, the OECD said: "Improving the effectiveness and timeliness of dispute resolution mechanisms is the aim of Action 14 of the BEPS Action Plan and is also part of the continuous efforts to enhance tax certainty. One of the elements of the Action 14 minimum standard [under the BEPS project] requires jurisdictions to seek to resolve [MAP] cases within an average timeframe of 24 months."

"To monitor compliance with this, members of the Inclusive Framework on BEPS have committed to report their MAP statistics pursuant to an agreed reporting framework. Such reporting provides a tangible measure of the effects of the collective implementation of some elements of the Action 14 minimum standard and now includes data from over 65 jurisdictions. These MAP statistics are now available for the 2016 reporting period."

According to the report, approximately 8,000 cases were in the inventory of the reporting jurisdictions as of January 1, 2016, and almost 25 percent of these were closed during 2016. In addition, 1,500 cases were newly initiated during 2016 and a quarter of these were also closed by the end of the year – that is, within less than 12 months.

According to the statistics, cases involving multinationals' transfer prices continued to take the longest to resolve. Such cases took an average of 33.5 months to resolve, compared with 26.5 months for all cases.

Countries are beginning to reduce the backlog of transfer pricing cases, with a reduction from the start to the end of 2016 of 4,451 to 4,032.

Of the cases closed in 2016, the average time taken was 22.5 months, considerably faster than for cases begun before January 1, 2016 (when the BEPS Action 14 standard was agreed).

According to the OECD, transfer pricing cases account for slightly more than half of the MAP cases in inventory. They take more time on average than other cases: approximately 30 months are needed for transfer pricing cases and 17 months for other cases.

Over 85 percent of MAP cases concluded in 2016 resolved the issue. Almost 60 percent were closed with an agreement fully resolving the taxation not in accordance with the tax treaty; almost 20 percent were granted a unilateral relief; and almost 5 percent were resolved via domestic remedy.

Of those not resolved, 5 percent of the MAP cases closed were withdrawn by taxpayers, while approximately 10 percent were not resolved for various other reasons.

Apple To Pay Irish State Aid Bill From 2018

Ireland and Apple have reached an agreement that will see the technology giant start paying the EUR13bn (USD15.4bn) it is alleged to owe in back taxes.

Irish Finance Minister Paschal Donohoe told reporters that the Government has "now reached an agreement with Apple in relation to the principles and operation of the escrow fund." He added that the Government expects "the money will begin to be transmitted into the account from Apple across the first quarter of next year."

In September 2016, a European Commission investigation concluded that two rulings provided by the Irish Government had "substantially and artificially lowered the tax paid by Apple in Ireland since 1991."

Both the Irish Government and Apple have appealed the Commission's ruling. In July, Ireland launched a procurement process for an escrow agent/custodian for an escrow account into which the funds would be placed and held until the European courts issue their final ruling on the Government's appeal.

The Commission estimated the amount of illegal state aid to be recovered by the Irish authorities to be around EUR13bn, plus interest. The deadline for Ireland to recover the money expired in January 2017. In October, the Commission referred Ireland to the European Court of Justice for its failure to do so.

Earlier this month, Irish Prime Minister Leo Varadkar said he did not "want to be in a situation where the Irish Government has to take Apple to court because the European Commission is taking the Irish Government to court."

OECD Releases First Peer Reviews On Tax Ruling Info Exchange

On December 2, the OECD released the first analysis of individual countries' progress in spontaneously exchanging information on tax rulings in accordance with Action 5 of the BEPS package of measures released in October 2015.

The first annual report on the exchange of information on rulings evaluates how 44 countries, including all OECD members and all G20 countries, are implementing one of the four new minimum standards agreed in the OECD/G20 BEPS Project.

According to the OECD, "A key aim of the project was to increase transparency, which resulted in a new minimum standard to ensure that information on certain tax rulings is exchanged between relevant tax administrations in a timely manner (Action 5). This minimum standard requires tax administrations to spontaneously exchange information on rulings that have been granted to a foreign related party of their resident taxpayer or a permanent establishment which, in the absence of exchange, could give rise to BEPS concerns. As a minimum standard, all members of the Inclusive Framework on BEPS have committed to implement this standard, and to have their compliance with the standard reviewed and monitored by their peers."

The standard covers rulings such as advance pricing agreements (APAs), permanent establishment rulings, related party conduit rulings, and rulings on preferential regimes. More than 10,000 relevant rulings were identified up to the end of 2016.

The annual report includes almost 50 country-specific recommendations on issues such as improving the timeliness of the exchange of information; ensuring all relevant information on the taxpayer's related parties is captured for exchange purposes; and ensuring that exchanges of information are made with respect to preferential tax regimes that apply to income from intellectual property.

The OECD said the next annual peer review will cover all members of the Inclusive Framework, except for the developing countries that requested a deferral of their review to 2019.

Bermuda To Exchange MNE Tax Info With UK

Bermuda and the UK recently signed an agreement providing for the automatic exchange of country-by-country (CbC) reports.

Bermuda is the first UK Overseas Territory to sign a CbC Competent Authority Agreement with the UK, which enables the automatic reporting of corporate income on a country-by-country basis for UK-related transfer pricing enforcement purposes.

The CbC report is one element of a three-tiered standardized approach to transfer pricing documentation proposed under BEPS Action 13. Multinational enterprise (MNE) groups are required to provide aggregate information annually for each jurisdiction where they do business, including the global allocation of income and taxes paid; indicators of the location of economic activity within the group; and information about which group entities do business in a particular jurisdiction, as well as the business activities they engage in.

At the conclusion of the signing of the agreement, Bermuda's Premier, David Burt, said: "I am pleased to sign this important agreement with the UK on behalf of the people of Bermuda. We are the first Overseas Territory to sign the agreement which further solidifies Bermuda's position as a global leader in international tax transparency. Bermuda remains a jurisdiction with an excellent reputation for quality. We continue to demonstrate leadership in global tax transparency and we encourage other countries to meet the 'Bermuda Standard'."

OECD Issues Further Guidance On CbC Reporting

The OECD has published additional guidance on the implementation of the country-by-country (CbC) reporting requirement proposed under Action 13 of its BEPS project.

The guidance, issued on November 30, addresses the following issues:

- How to report amounts taken from financial statements prepared using fair value accounting;
- How to treat a negative figure for accumulated earnings in Table 1;
- How to treat mergers/acquisitions/de-mergers;
- How to treat short accounting periods, and
- The definition of total consolidated group revenue.

Releasing the guidance, the OECD said: "Since the BEPS Action 13 Report was released, jurisdictions have made great efforts to establish the necessary domestic and international legal and administrative frameworks for the filing and exchange of CbC reports in accordance with the Action 13 minimum standard and the global landscape for CbC reporting by MNE groups is still evolving."

"This initial period may be challenging for both tax administrations and [multinational enterprise (MNE)] groups seeking to be compliant with CbC reporting, which may call for a pragmatic approach that takes into account best efforts made to comply with CbC related obligations. These challenges should diminish over time, as the global landscape for CbC reporting becomes more settled and both tax administrations and MNE groups gain in experience."

The CbC report is one element of a three-tiered standardized approach to transfer pricing documentation proposed under Action 13 of the BEPS project. Under the framework, MNEs are required to provide aggregate information annually for each jurisdiction where they do business, relating to the global allocation of income and taxes paid, together with other indicators of the location of economic activity within the MNE group. It also covers information about which entities do business in a particular jurisdiction and the business activities each entity engages in.

Australia, UK Discussing Future Trade Deal

The early completion of a new free trade agreement (FTA) between Australia and the UK is a post-Brexit priority for both governments, according to their trade ministers.

Australian Trade Minister Steven Ciobo and his UK counterpart Liam Fox met in Sydney on November 30.

According to a joint statement issued by the ministers, they noted the progress being made in the Trade Working Group to "scope out the parameters of a future ambitious and comprehensive free trade agreement between the two nations."

Australia was the first country with which the UK established a Trade Working Group following its vote to leave the EU.

The ministers confirmed that the early completion of an FTA is a priority for both governments, once the UK is "in a position to negotiate new trade deals."

The ministers instructed officials to report back to them in the second half of 2018, and to provide "their conclusions on scoping the parameters of a future FTA." They also asked officials to continue building momentum in the Working Group, and to identify practical steps that could be taken to enable companies in both countries to trade and do business with one another more easily.

The statement added that both members hoped that negotiations toward an EU–Australia FTA would commence in the near future.

MEPs Say Not Enough Progress Made On Brexit

The European Parliament's Brexit Steering Group (BSG) has argued that more progress is needed on citizens' rights and on the situation on the island of Ireland before negotiators can move on to discussing the future EU–UK relationship.

On November 29, the BSG met with the chairs and coordinators of the European Parliament's committees on Employment and Social Affairs, Legal Affairs and Civil Liberties, and Justice and Home Affairs.

Following the meeting, Guy Verhofstadt wrote on the BSG's behalf to the EU's chief Brexit negotiator, Michel Barnier, to set out its concerns over the lack of progress made to date.

In the case of Ireland, the letter explained that the BSG wants the UK to "make a clear commitment, to be enshrined in a form which would guarantee its full implementation in the withdrawal agreement," that it will protect the Good Friday Agreement. In addition, it wants the UK to guarantee that there will be no "hardening of the border on the island of Ireland," and that the rights of people in Northern Ireland will not be diminished as a result of Brexit.

Regarding citizens' rights, the letter acknowledged that progress has been made since the start of negotiations but stressed that "considerable problems remain, which pose a fundamental question as to whether sufficient progress has been achieved."

The European Council will meet on December 14–15 to decide whether "sufficient progress" has been made in phase one of Brexit negotiations to warrant the discussion of the future trading relationship between the UK and the EU.

The European Parliament must approve any withdrawal agreement.

UK Releases Consultation On Royalties WHT Proposal

The UK Government has released a consultation on the royalty withholding tax (WHT) targeting digital firms announced in its most recent Budget.

Under the proposal, the Government intends to introduce legislation in Finance Bill 2018–19 to broaden the circumstances in which certain payments made to non-UK residents have a liability to income tax. These changes will have effect from April 2019, in what is said to be an expansion of the UK's arsenal to combat base erosion and profit shifting activities by multinational companies.

The consultation, which is intended to support the development of the legislation, notes that the Finance Act 2016 (FA16) included provisions to reinforce that all royalties arising from the UK will be subject to the deduction of income tax – a withholding tax – at source unless the UK has explicitly given up its taxing rights under an international agreement (such as a double tax avoidance agreement).

At Autumn Budget 2017, the Government announced a further extension to the FA16 rules. This measure will mean that payments for the exploitation of certain property or rights in the UK that are made to connected parties in low- or no-tax jurisdictions will be subject to "appropriate taxation."

The Government said in the consultation: "This is another step towards the Government's longer term ambition of domestic and international reform of the taxation of digital businesses. Whilst this measure will predominantly affect digital businesses, it may also affect groups operating in other sectors." It explained that the measure is proposed to be "a targeted rule aimed at intragroup arrangements that achieve an artificially low effective rate that is distortive to competition in the markets in which they operate, including the UK."

The consultation is to intended to support the development of a WHT that delivers on these policy aims. The consultation will close on February 23, 2018, and legislation is to be tabled in the summer of 2018.

Most FTSE 100 Firms Already Publishing UK Tax Strategy

Over half of all FTSE 100 companies (59 percent) have already published a UK tax strategy as part of their Annual Report, according to analysis published by Deloitte on December 4.

The firm's fourth Annual Review of FTSE 100 tax disclosures, which looks at tax transparency trends in the largest companies' annual reports, found that out of the 94 companies with a year-end of December 31, 2016 or later, 59 percent (55 companies) have disclosed some form of tax strategy statement.

Of those strategies that were published, 64 percent (35 companies) made a stand-alone statement, while 36 percent (20 companies) included the strategy in their annual report. The majority of businesses disclosing their tax strategy (75 percent) made a global statement reflecting the scale of their organizations. While 55 percent emphasized the tax contribution they made and provided headline values, most (84 percent) steered clear of providing detailed country-by-country analysis. Moreover, tax strategies were typically concise; half of them (28) were summarized in less than a page, while only nine companies wrote more than four pages.

The UK Government introduced a package of measures in September 2016 requiring many large businesses and partnerships to publish a UK tax strategy by the end of their next financial year, which for those with a calendar year-end is December 31, 2017.

Mark Kennedy, Partner in Deloitte's Tax Management Consulting Group, said: "All FTSE 100 businesses can expect to be in the scope of the legislation, and as of November nearly 60 percent had already published their strategy. Other companies are likely to try and gain visibility on trends, conventions, and the public response to those trends before making their strategy public."

"While it is not yet a legal requirement for all companies to have disclosed their tax strategy, we are already seeing a lot of interest from HM Revenue & Customs as to the nature of these statements and how the principles expressed in them are embedded within the organization."

Alexandra Warren, Tax Reporting Specialist Partner, said: "Having looked at tax reconciliations of FTSE 100 companies in scope we found a greater degree of disaggregation and more meaningful explanations of adjusting items. Companies were also clear about factors which could have a future [effective tax rate] impact, with many groups citing factors such as the OECD's Base Erosion and Profits Shifting project, US tax reform, and potential EU State Aid challenge."

Warren added: "We found improvement in the way tax risk provisions for groups that had identified tax as a key area of judgment or estimation uncertainty were disclosed. In many cases they explained both the process by which tax risk provisions are quantified, the nature of the uncertainty and quantification of the uncertain tax risk provision."

Kennedy concluded: "It's important that businesses are able to prove that they operate in line with the standards and behaviors set out in their public statement. Making these statements and operating to them should go a long way to giving the public confidence that the companies they work for, buy from, and invest in are operating in line with acceptable standards. Communications on tax from large businesses should meet the regulatory requirements and broader stakeholder needs, with key risks and uncertainties clearly disclosed. However, regulators also need to create a coherent standard for the tax disclosures of large businesses that can be understood readily by companies."

Offshore IFCs Absent From EU's New Tax Blacklist

EU member states have agreed to a new EU list of non-cooperative tax jurisdictions, featuring 17 jurisdictions and notably relatively few offshore international financial centers (IFCs).

The 17 countries that feature in the "blacklist" agreed by EU finance ministers on December 5, 2017, are: American Samoa, Bahrain, Barbados, Grenada, Guam, Macao, the Marshall Islands, Mongolia, Namibia, Palau, Panama, Saint Lucia, Samoa, South Korea, Trinidad and Tobago, Tunisia, and the United Arab Emirates.

A further 47 countries have committed to address deficiencies in their tax systems and to meet the required criteria, following contact with the EU.

Placement on the blacklist will result in the countries losing EU funds, it has been reported. Further penalties are to be agreed.

Pierre Moscovici, Commissioner for Economic and Financial Affairs, Taxation and Customs, said: "The adoption of the first ever EU blacklist of tax havens marks a key victory for transparency and fairness. But the process does not stop here. We must intensify the pressure on listed countries to change their ways. Blacklisted jurisdictions must face consequences in the form of dissuasive sanctions, while those that have made commitments must follow up on them quickly and credibly. There must be no naivety: promises must be turned into actions. No one must get a free pass."

The idea of an EU list was originally conceived by the European Commission and subsequently taken forward by member states. The Commission said work is to continue as the 47 territories should meet EU criteria by the end of 2018, or 2019 for developing countries without financial centers, to avoid being listed.

The EU listing process is a dynamic one, the Commission said. It added, as a first step, that a letter will be sent to all jurisdictions on the EU list, explaining the decision and what they can do to be de-listed. A first interim progress report should be published by mid-2018, and the EU list will be updated at least once a year.

India, Netherlands Conclude First Advance Pricing Deals

India's Central Board of Direct Taxes (CBDT) has entered into its first bilateral advance pricing agreements (APAs) with the Netherlands.

The two APAs, signed in November, cover the tax affairs of companies engaged in the electronics and technology sectors. The international transactions covered in these agreements include distribution arrangements, and the provision of marketing and business support services.

India has so far entered into 15 bilateral APAs, of which eight are with the UK and five are with Japan. A first bilateral APA between India and the US has been "resolved" but not yet concluded.

The APA scheme was introduced in the Income-tax Act in 2012 and "rollback" provisions were introduced in 2014.

"The progress of the APA scheme strengthens the Government's commitment to foster a non-adversarial tax regime," the CBDT said.

Ecofin Approves VAT Overhaul For Digital Economy

The European Commission has welcomed an agreement reached among EU finance ministers on the introduction of simpler and more efficient rules for businesses that sell goods online.

"This revamp of the rules will make our VAT system fit for the digital economy," said Toomas Tõniste, Minister for Finance of Estonia, which currently holds the European Council presidency. "By reducing red tape, we will achieve both cost savings for businesses and increased tax revenues for the member states. This was a major priority for our presidency." The proposals will also help to reduce VAT fraud involving distance sales in the EU, which is estimated to be worth EUR5bn (USD5.9bn) each year.

The new rules extend an existing EU-wide portal (the mini "one-stop shop") for the VAT registration of distance sales and establish a new portal for distance sales from third countries with a value below EUR150 (USD177.5). This is intended to reduce the costs of complying with VAT requirements for business-to-consumer transactions.

Most goods imported for distance sales currently enter the EU VAT-free, resulting in unfair competition for EU businesses. VAT will be paid in the member state of the consumer, ensuring a fairer distribution of tax revenues among member states.

Additionally, online platforms will become liable to collect VAT on the distance sales that they facilitate. This was not foreseen in the Commission's proposals, but was seen as an essential provision of the package by EU finance ministers meeting on December 5.

The one-stop shop will relieve online traders of having to register for VAT in each of the member states in which they sell goods. According to the Commission, such obligations cost businesses around EUR8,000 for every EU country into which they sell. The proposals would enable administrative burdens for companies to be reduced by 95 percent. The one-stop shop will generate an overall saving of EUR2.3bn for businesses, the Commission estimates, and a EUR7bn increase in VAT revenues for member states.

For start-ups and SMEs, the new rules introduce an important simplification. For those firms with yearly cross-border online sales below EUR10,000, businesses will be able to continue applying VAT rules used in their home country. Furthermore, the new rules remove an exemption for consignments from outside the EU worth less than EUR22. Around 150m small consignments are imported free of VAT, and the current system is open to abuse. While EU businesses have to apply VAT regardless of the value of the goods sold, imported goods benefit from the exemption and are often undervalued in order to do so.

The package – a directive and two regulations – was adopted without discussion at a meeting of the Economic and Financial Affairs Council (Ecofin).

The new rules set out the following timeline:

- Introduction by 2019 of simplification measures for intra-EU sales of electronic services;
- Extension by 2021 of the one-stop shop to distance sales of goods, both intra-EU and from third countries, as well as the elimination of the VAT exemption for small consignments.

The rules also provide for enhanced administrative cooperation between member states to accompany and facilitate this extension.

The provisions that will apply from 2021 will be addressed in greater detail in a further Commission proposal under a non-legislative procedure. Ecofin approved a statement highlighting issues to be considered by the Commission in the implementing phase. The provisions that will apply from 2019 are already covered by the package.

The member states will have until December 31, 2018, and December 31, 2020, to transpose the corresponding provisions of the directive into national laws and regulations. The regulation on administrative cooperation will apply from January 1, 2021.

Following the agreement, Andrus Ansip, Vice-President for the Digital Single Market, said: "This is a new step to boost e-commerce in Europe, a few days after reaching an agreement to end unjustified geo-blocking for consumers shopping online. Companies selling abroad online will deal with VAT in the same way as they do for sales in their own countries. This will also make public services more efficient and increase cooperation across borders."

Following the agreement, Pierre Moscovici, Commissioner for Economic and Financial Affairs, Taxation and Customs, said: "Brick by brick and piece by piece, a new VAT system is being built that is fit for purpose and within which internet companies operating across borders can thrive. At the same time, we are making sure that non-EU businesses do not get preferential treatment when selling to EU consumers – both directly and through online marketplaces. Today's agreement also bodes well for the more fundamental VAT reform in the EU that is so urgently needed."

Indian Economic Recovery Proof GST Is Working, Firms Say

The Federation of Indian Chambers of Commerce and Industry (FICCI) on November 30 welcomed news that the economy is strengthening, praising the Government for how the goods and services tax (GST) has been implemented.

Latest statistics show that the economy is currently growing at 6.3 percent of gross domestic product, up from 5.7 percent in the previous quarter.

FICCI President Pankaj Patel said: "Growth numbers are in sync with the expectations and re-affirm that signs of recovery are in sight. The performance of industrial sector has noted an improvement after dropping to the lowest in almost five years in the previous quarter."

"After the massive destocking undertaken by companies before implementation of GST, production lines are once again coming back on track. It is encouraging to see Government's approach towards resolving GST-related issues. We are confident of moving to a seamless GST regime in a few months from now."

EU States To Work Together To Stamp Out VAT Fraud

On November 30, the European Commission released new tools intended to make the EU's value-added tax (VAT) system more resilient to fraud.

The package includes numerous changes to how member states will communicate and cooperate with one another. It will alter the mandate of law enforcement agencies, and will establish a new European Public Prosecutors Office (EPPO).

VAT fraud is estimated to cause losses for EU member states of about EUR50bn (USD59.2bn) each year, and there are growing concerns that terrorist organizations are branching out into carrying out VAT fraud schemes to fund their activities.

According to the Commission, the proposal will enable member states to communicate more quickly to challenge fraudsters, as fraud can happen nearly instantaneously. The proposal would put in place an online system for information sharing within Eurofisc, a network that connects anti-fraud experts from the member states. This system would enable member states to process, analyze, and audit data on cross-border activity to make sure that risk can be assessed as quickly and accurately as possible. New powers would also be given to Eurofisc to coordinate cross-border investigations.

To boost the capacity of member states to check cross-border supplies, joint audits would allow officials from two or more national tax authorities to form a single audit team to combat fraud. The Commission said this is especially important for cases of fraud in the e-commerce sector.

The new measures would open new lines of communication and data exchange between tax authorities and European law enforcement bodies on cross-border activities suspected of leading to VAT fraud: OLAF, Europol, and the newly created EPPO. Cooperation with European bodies would allow for the national information to be cross-checked with criminal records, databases, and other information held by Europol and OLAF, in order to identify the real perpetrators of fraud and their networks.

Many of these measures will help member states and law enforcement agencies to better tackle carousel fraud, which costs member states tens of billions in revenue each year. Carousel fraud involves a fraudulent seller charging VAT but not remitting that VAT to the relevant tax authority and disappearing. The name of the fraud is derived from the typical circular chain of transactions set up by the criminals to maximize profits, and often entails sham paperwork and the creation of temporary companies to engage in the trades. In order to hide the fraud, the circle sometimes involves compliant honest traders.

The Commission said: "The measures announced today would have a profound effect on how member States exchange information around cross-border VAT fraud in the EU, allowing them to consolidate information on the businesses taking part in this activity in different countries and to investigate suspicious activity more easily. Once agreed, the rules would put in place a mechanism by which member states would be able to jointly process and analyze data on VAT fraud via the Eurofisc network of member state experts. At the same time, member states would be able to jointly audit and assess companies operating cross-border where there is reason to believe that fraudulent activity is taking place. EU countries would also be able to send officials abroad to assess cases of VAT fraud in other member states where their country has been losing out on tax revenues."

Other actions are planned to tackle fraud in other areas.

The Commission has proposed that member states should share key information on imports from outside the EU and on vehicle registration. According to the proposal, information sharing between tax and customs authorities would be further improved for certain customs procedures that are open to VAT fraud.

Presently there is a special arrangement that enables goods arriving from outside the EU with a final destination in another member state to transit onwards VAT-free. VAT is charged only when the goods reach their final destination. This feature of the EU's VAT system aims to facilitate trade for honest companies but can be abused to divert goods to the black market and circumvent the payment of VAT altogether. Under the new rules, information on incoming goods would be shared and cooperation strengthened between tax and customs authorities in all member states.

Among other things, in respect of goods, the relevant information about the imported goods (*e.g.*, VAT numbers, value of the imported goods, type of commodities, *etc.*) already submitted electronically with customs declarations will be shared by the member state of import with the tax authorities in the member state of destination.

The plan will include providing law enforcement agencies with access to car registration data. The Commission explained: "Trading in cars is also sometimes subject to fraud due to the difference in how VAT is applied to new and used cars. Recent or new cars, for which the whole amount is taxable, can be sold as second-hand goods for which only the profit margin is subject to VAT. In order to tackle this type of fraud, Eurofisc officials would also be given access to car registration data from other member states."

The measures will enter into force as soon as they are agreed by the member states and the European Parliament has given its opinion, the Commission said. As the implementation of the automated access to the information collated by the customs authorities and to vehicle registration data will require new technological developments, their application will be deferred until January 1, 2020, to allow the member states and the Commission to carry out those developments, it said.

UAE Finalizes Adoption Of New VAT Framework

The Prime Minister of the United Arab Emirates (UAE) has officially approved regulations that set out rules for the value-added tax (VAT) framework the country will adopt, alongside Saudi Arabia, from January 1, 2018.

The Executive Regulation for the Federal Decree-Law No. (8) of 2017 on Value Added Tax was unveiled at a Cabinet meeting on November 7.

According to the Ministry of Finance, among other things, the Regulation defines terms used; discusses how to categorize supplies and a taxable event; and discusses mixed supplies and deemed supplies.

The Regulation sets out administrative rules, such as the requirement to register and voluntary registration; the treatment of supplies between related parties; conditions to be met to register a tax group and appointing a representative member; deregistration; exceptions from the requirement to register; transitional registration rules; and the rules surrounding reregistration.

The Regulation also looks at how to determine when a supply takes place; the place where a supply is deemed to have occurred; the place of supply of services connected with immovable property; the treatment of transport services, telecommunications services, and electronic services, and intra-GCC supplies; rules concerning valuation of supplies; and pricing rules, including rules concerning discounts, subsidies, and vouchers. It also discusses reverse charges; reporting and documentation rules; and the treatment of cross-border supplies.

The Regulations are available on the Ministry of Finance's and the tax agency's websites.

Businesses are required to register to collect and remit VAT if at any time during the past 12 months the value of their taxable supplies exceeded the mandatory registration threshold of AED375,000 (USD102,000), or if the entity anticipates that it will exceed the threshold within the next 30 days.

Taxpayers can register voluntarily if the total value of their taxable supplies exceeded AED187,500, or if the business expects to exceed that threshold within the next 30 days.

Younis Al Khouri, Undersecretary at the Ministry of Finance, said: "Now that Mohammed bin Rashid Al Maktoum has signed off on the [Regulation], we are on the cusp of a new stage in the implementation of an effective tax system in the UAE – one that meets international standards and upgrades services, strategic sectors, and overall quality of life in the emirates."

"Over the past few months, the Ministry of Finance has been working together with the Federal Tax Authority to carry out extensive awareness campaigns to prompt businesses across the UAE to prepare for the upcoming tax system," Al Khouri said. "We do expect that they have benefited from this preparation phase to align their operations with the requirements of the VAT system in time for the execution phase, beginning on January 1, 2018."

It had been intended that the 5 percent levy be introduced across all GCC states (Saudi Arabia, Kuwait, the UAE, Qatar, Bahrain, and Oman) simultaneously. However, just the UAE and Saudi Arabia are to introduce the tax from January 1, 2018, with approvals and preparations delayed in the other territories.

Philippines' Senate Approves Latest Tax Reform Package

The Philippines' Senate on November 28 approved its version of the Tax Reform for Acceleration and Inclusion (TRAIN) bill, which is expected to exempt 6.8m workers from paying income taxes.

Senate Bill (SB) 1592, sponsored by Senator Sonny Angara, Chairman of the Ways and Means Committee, was approved on third and final reading with 17 affirmative votes and one negative vote.

The passage of the TRAIN bill has been identified by leadership in both houses of Congress and the Duterte administration as a priority. The Senate version consolidated 31 Senate bills, three House bills, and three Senate resolutions.

Under the Senate-approved SB 1592, the first PHP250,000 (USD4,930) of annual taxable income will be exempted from tax, and a PHP82,000 tax exemption for 13th month pay and other bonuses will be introduced. The bill will also expand the value-added tax base, specifically by removing exemptions for cooperatives, low-cost housing, renewable energy, and senior citizens except for medicine.

An amendment to the bill, which was passed by a significant majority, proposes to hike the coal tax from PHP10 per metric ton to PHP300 per metric ton. Senator Joel Villanueva, who sponsored the amendment, noted that coal tax rates had not been amended since 1988. In respect of the mining sector, the Senate also approved to increase the excise taxes on metallic and non-metallic mining resources from 2 percent to 4 percent.

OECD Reports On Swiss Tax Reform Efforts

The OECD has said that Switzerland's efforts to meet its international commitments to reform its corporate tax regime are welcome, but noted there is some uncertainty around the proposed reform package.

The Swiss federal government's original tax reform proposals – the Corporate Tax Reform III package – were rejected in a referendum in February. The Government has since produced Tax Proposal 17 (TP17), which includes plans to abolish special cantonal tax regimes, increase the taxation of dividends, and provide for the equal tax treatment of all resident companies. It also intends to introduce a patent box regime under TP17, and to allow the cantons to introduce a super-deduction for research and development expenditure.

The Government hopes that the new regime will enter into force in January 2021.

In its latest Economic Survey of Switzerland, the OECD stated that there is "some uncertainty around corporate tax reforms, which were initially rejected by referendum but are necessary to align Switzerland's tax system with its international commitments," but added that while it is "too early to assess the final reform package, Switzerland's efforts to meet its international commitments are welcome."

The OECD explained that the total budgetary impact of the reforms is also "difficult to gauge because of the complexity of the tax system and uncertainty around the cantonal response."

According to the report, in 2011, 7 percent of all taxable corporate entities in Switzerland were under a special tax regime and that, together, these entities paid around half of all federal corporate taxes and 20 percent of cantonal corporate tax. The OECD said that federal government revenue is expected to be CHF755m (USD766.6m) lower in 2021, equivalent to 1 percent of projected revenue.

The OECD also observed that the cantons are expected to lower their corporate income tax rates as a result of the broader reform package, with some cantons having previously announced plans to reduce their rates by between 3 and 10 percentage points. It recommended that the federal government work with the cantons to pre-announce these cuts and detail how they will cover the consequent revenue shortfalls.

BAHRAIN - HONG KONG

Draft

Bahrain's Cabinet has approved the signing of a new DTA with Hong Kong, the state news agency said November 13, 2017.

CANADA - ANTIGUA AND BARBUDA

Signature

Canada and Antigua and Barbuda signed a TIEA on October 31, 2017.

CYPRUS - IRAN

Effective

The DTA between Cyprus and Iran will become effective from January 1, 2018.

ESTONIA - SINGAPORE

Ratified

According to preliminary media reports, Estonia has ratified a DTA Protocol signed with Singapore.

FINLAND - GERMANY

Effective

Finland on November 2, 2017, confirmed that a new DTA signed with Germany will be effective from January 1, 2018.

HONG KONG - BELARUS

Into Force

The Hong Kong–Belarus DTA entered into force on December 1, 2017.

HONG KONG - VARIOUS

Into Force

Hong Kong announced on November 24, 2017, that its DTAs with Pakistan and Latvia had entered into force.

LIECHTENSTEIN - UNITED ARAB EMIRATES

Effective

According to an update from the Liechtenstein Government, the new DTA with the United Arab Emirates will become effective from January 1, 2018.

NETHERLANDS - LIECHTENSTEIN

Negotiations

According to preliminary media reports, the Netherlands and Liechtenstein held a first round of DTA negotiations over three days ending November 17, 2017.

SAUDI ARABIA - BULGARIA

Signature

According to preliminary media reports, Saudi Arabia and Bulgaria signed a DTA on November 30, 2017.

SWITZERLAND - KOSOVO

Forwarded

Swiss lawmakers on November 15, 2017, approved a new DTA with Kosovo.

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

THE AMERICAS

Hedge Fund Tax 101 and K-1 Boot Camp

1/24/2018 - 1/25/2018

Financial Research

Venue: The Princeton Club, 15 W 43rd St, New York, NY, USA

Key Speakers: TBC

http://events.frallc.com/events/hedge-fund-tax-101-and-k-1-boot-camp-b1079-/event-summary-22badeb84b1c456a9f91595d120eba96.aspx?dvce=1

STEP Cayman Conference 2018

1/29/2018 - 1/30/2018

STEP

Venue: Kimpton Seafire Resort and Spa, 60 Tanager Way, Grand Cayman, Cayman Islands, KY1-9008

Key speakers: Sherice Arman (Maples and Calder), Maxine Bodden TEP (Maples and Calder), Sarah Cormack (Withers LLP), Oliver Court TEP (Withers LLP), Andrew De La Rosa (ICT Chambers), Antony Duckworth TEP (Collas Crill), among numerous others

http://www.step.org/cayman2018

STEP Orange County 7th Annual Institute on Tax, Estate Planning and The Economy

2/15/2018 - 2/16/2018

STEP

Venue: Island Hotel Newport Beach, 690 Newport Center Drive, Newport Beach, California, 92660, USA

Key speakers: Lawrence Brody (Bryan Cave LLP), Keith Schiller (Schiller Law Group), Jane Peebles (Karlin & Peebles LLP), Paul Lee (Northern Trust), Justin Miller (BNY Mellon), among numerous others

http://www.step.org/events/save-date-step-orange-county-7th-annual-institute-tax-estate-planning-and-economy

TP Minds Americas 2018

2/20/2018 - 2/21/2018

informa

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

Key speakers: Karl Soukup (European Commission), John Hughes (IRS), Michael Lennard (United Nations), Norman Wingen (OECD), among numerous others

https://finance.knect365.com/tp-minds-americas-conference/

In-Depth HST/GST Course

5/27/2018 - 6/1/2018

CPA

Venue: 48 John Street, Niagara-on-the-Lake, ON LOS 1J0, Canada

Key speakers: David Robertson (CPA), Janice Roper (Deloitte)

https://www.cpacanada.ca/en/career-and-professional-development/courses/core-areas/taxation/indirect-tax/in-depth-hst-gst-course

Transcontinental Trusts: International Forum 2018

6/3/2018 - 6/5/2018

informa

Venue: The Hamilton Princess, 76 Pitts Bay Rd, HM08, Bermuda

Key speakers: The Hon. Premier David Burt (Premier, The Goverment of Bermuda), The Hon. Justice Indra Charles (Justice, Supreme Court of The Bahamas), Anthony Poulton (Baker & McKenzie), Jonathan Conder (Macfarlanes), among numerous others

https://finance.knect365.com/transcontinental-trusts-international-forum/

ASIA PACIFIC

International Taxation Conference 2017

12/7/2017 - 12/9/2017

IBFD

Venue: ITC Maratha Hotel, Sahar Elevated Rd, Sahar, Airport Area, Andheri East, Mumbai, Maharashtra 400099, India

Chair: Pascal Saint-Amans (OECD)

https://www.ibfd.org/sites/ibfd.org/files/content/pdf/International-Taxation-Conference-2017.pdf

CENTRAL AND EASTERN EUROPE

CIS Wealth Moscow 2018

2/19/2018 - 2/20/2018

CIS Wealth

Venue: Marriott Moscow Grand, 26/1 Tverskaya Street, Moscow, 125009, Russia

Key speakers: Svetlana Hohlova (Bell Moore S), Ekaterina Varadi (LAVECO Ltd), Maxim Simonov (Duvernoix Legal), Anna Modyanova (PwC)

http://cis-wealth.com/en/konferencii/19-cis-wealth-moscow-2018.html

Wealth Management & Private Banking Summit – Russia & CIS

4/17/2018 - 4/18/2018

Adam Smith Conferences

Venue: Marriott Grand Hotel, 26/1, Tverskaya Street, Moscow, 125009, Russia

Key speakers: Michael Addison (UBS), Evgenia Tyurikova (Sberbank Private Banking), Katerina Mileeva (Alfa-Bank), Evgeny Sivoushkov (PwC), among numerous others

http://www.russianwealthmanagement.com/

WESTERN EUROPE

Advanced VAT Optimization

12/7/2017 - 12/8/2017

IBFD

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

Key speakers: Shima Heydari (EY), Wilbert Nieuwenhuizen (University of Amsterdam), Caspar Jansen (EY)

https://www.ibfd.org/Training/Advanced-VAT-Optimization

Private Investor: Russia & CIS

12/11/2017 - 12/12/2017

Adam Smith Conferences

Venue: The Waldorf Hilton, Aldwych, London, WC2B 4DD, UK

Key speakers: Evgenia Tyurikova (Sberbank), Anastasia Soldatova (CITI Bank), Phanos Theophanous (Barclays), Karen Aslanian (Lombard Odier), among numerous others

http://www.privateinvestorrussia.com/

Current Issues in VAT

12/13/2017 - 12/13/2017

Mercia

Venue: RAF Museum, London, Grahame Park Way, London, NW9 5LL, UK

Key speaker: Simone Hurst (VATease)

http://www.mercia-group.co.uk/GetEvent/CurrentIssuesinVAT/9554

7th Annual IBA Tax Conference

1/29/2018 - 1/30/2018

International Bar Association

Venue: etc.venues, 8 Fenchurch Pl, London, EC3M 4PB, UK

Speakers: TBC

https://www.ibanet.org/Conferences/conf856.aspx

Russian Wealth Advisors Forum

1/31/2018 - 2/1/2018

Adam Smith Conferences

Venue: Zürich Marriott Hotel, Neumühlequai 42, 8001 Zürich, Switzerland

Key speakers: Graham Povey (UBS), Michael Vlahovic (EFG Bank), Stefan Liniger (Rothschild Trust Group), John Riches (RMW Law), among numerous others

http://www.russianwealthzurich.com/

Swiss & Liechtenstein STEP Federation Alpine Conference

1/31/2018 - 2/1/2018

STEP

Venue: Congress Centre Kursaal Interlaken, Strandbadstrasse 44, 3800 Interlaken, Switzerland

Key speakers: Mark Barmes (Lenz & Staehelin), Professor Hans Peter Beck (CERN), Juerg Birri (KPMG), Nicholas Capt (Capt & Wyss Attorneys), among numerous others

http://www.step.org/events/save-date-swiss-liechtenstein-step-federation-alpine-conference-31-january-1-february-2018

Current Issues in International Tax Planning

2/21/2018 - 2/23/2018

IBFD

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

Key speakers: Emma Barrögård (IBFD), Premkumar Baldewsing (IBFD)

https://www.ibfd.org/Training/Current-Issues-International-Tax-Planning-0

Principles of International Taxation

2/26/2018 - 3/2/2018

IBFD

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

Key speakers: Bart Kosters (IBFD)

https://www.ibfd.org/Training/Principles-International-Taxation

23rd Annual International Wealth Transfer Practice Conference

3/5/2018 - 3/6/2018

International Bar Association

Venue: Claridge's, Brook Street, Mayfair, London, W1K 4HR, UK

Key Speakers: TBC

https://www.ibanet.org/Conferences/conf839.aspx

IBFD Seminar: The Future of VAT

3/13/2018 - 3/13/2018

IBFD

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

Key speakers: Robert van Brederode (Crowe Horwath), Werner Engelen (LEGO Group), Toon Beljaars (Uber)

https://www.ibfd.org/IBFD-Tax-Portal/Events/IBFD-Seminar-Future-VAT#tab_program

European Value Added Tax – Selected Issues

3/14/2018 - 3/16/2018

IBFD

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

Key speakers: TBC

https://www.ibfd.org/Training/European-Value-Added-Tax-Selected-Issues-1

Transfer Pricing Masterclass

3/28/2018 - 3/29/2018

IBFD

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

Key speakers: TBC

https://www.ibfd.org/Training/Transfer-Pricing-Masterclass

Principles of Transfer Pricing

4/9/2018 - 4/13/2018

IBFD

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

Key speakers: TBC

https://www.ibfd.org/Training/Principles-Transfer-Pricing-0

Global VAT

4/17/2018 - 4/20/2018

IBFD

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

Key speakers: TBC

https://www.ibfd.org/Training/Global-VAT

Global VAT – Specific Countries

4/19/2018 - 4/20/2018

IBFD

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

Key speakers: TBC

https://www.ibfd.org/Training/Global-VAT-Specific-Countries-1

US Corporate Taxation

4/24/2018 - 4/26/2018

IBFD

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

Key speakers: John G. Rienstra (IBFD)

https://www.ibfd.org/Training/US-Corporate-Taxation-0

3rd International Conference on Taxpayer Rights

5/3/2018 - 5/4/2018

IBFD

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

Key speakers: Philip Baker, QC (Field Court Tax Chambers), Kevin M. Brown (PwC), Juliane Kokott (Advocate General, ECJ), Andrew Roberson (McDermitt Will & Emery), among numerous others

https://www.ibfd.org/IBFD-Tax-Portal/Events/3rd-International-Conference-Taxpayer-Rights

Tax and Technology

5/3/2018 - 5/4/2018

IBFD

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

Key speakers: Bart Janssen (Deloitte), Aleksandra Bal (IBFD), Monica Erasmus-Koen (Tytho), Eliza Alberts-Muller (Tytho)

https://www.ibfd.org/Training/Tax-and-Technology

International Tax, Legal and Commercial Aspects of Mergers & Acquisitions

5/7/2018 - 5/9/2018

IBFD

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

Key speakers: Frank de Beijer (Liberty Global), Femke van der Zeijden (PwC), Rens Bondrager (Allen & Overy) https://www.ibfd.org/Training/International-Tax-Legal-and-Commercial-Aspects-Mergers-Acquisitions

Transfer Pricing and Intra-Group Financing

5/24/2018 - 5/25/2018

IBFD

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

Key speakers: TBC

https://www.ibfd.org/Training/Transfer-Pricing-and-Intra-Group-Financing

Introduction to European Value Added Tax

6/5/2018 - 6/8/2018

IBFD

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

Key speakers: TBC

https://www.ibfd.org/Training/Introduction-European-Value-Added-Tax-0

Private Investor Middle East International Conference

Western Europe

9/26/2018 - 9/27/2018

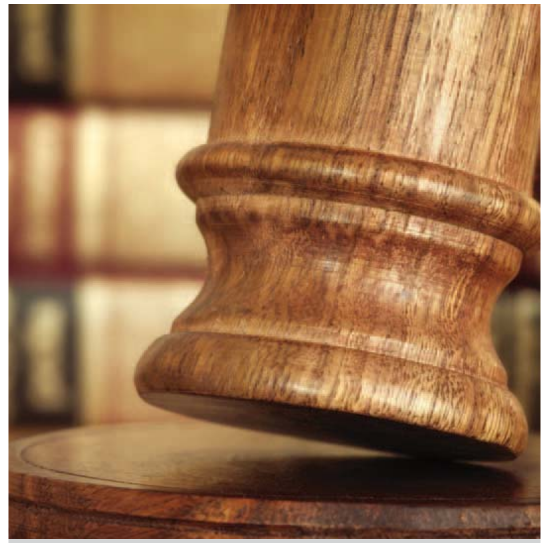
Adam Smith Conferences

Venue: The Montcalm London Marble Arch, 2 Wallenberg Place, London, W1H 7TN, UK

Key speakers: Jeffrey Sacks (Citi Private Bank), Michael Addison (UBS), Paul Stibbard (Rothschild Trust), Ian Barnard (Capital Generation Partners), among numerous others

http://www.privateinvestormiddleeast.com/

THE AMERICAS



A listing of recent key international tax cases.

United States

A US court has agreed that cryptocurrency trading platform Coinbase must share information about its customers with the Internal Revenue Service (IRS).

In March 2014, the IRS issued Notice 2014-21 ruling that virtual currencies such as bitcoin are to be treated as property rather than as fiat currency for tax purposes.

In November 2016, Coinbase launched a legal challenge to a summons issued by the IRS for details of all Coinbase transactions undertaken by US taxpayers between 2013 and 2015.

The IRS request was based on the gulf between the number of estimated US users of Coinbase and the number of taxpayers reporting cryptocurrency gains (taxable under a 2014 ruling).

Of an estimated 6m Coinbase customers, just 800 taxpayers reportedly declared gains.

The San Francisco District Court ruled that Coinbase must disclose identifying information concerning 14,355 customers, covering those users undertaking transactions worth USD20,000 or more in a single year between 2013 and 2015.

The currency platform said it had secured a "partial victory" in court, stating: "First, the Government vastly narrowed the scope of its summons. Thanks to Coinbase's efforts, more than 480,000 customers' records were preserved from disclosure. This is a 97 percent reduction in the number of customers impacted by this summons."

"Second, the quantity of data we must produce for the approximately 14,000 customers who remain in scope has been significantly reduced. In narrowing the scope of the summons, we are pleased that the Court acknowledged the privacy rights at stake in this matter."

This ruling was delivered on November 28, 2017.

https://regmedia.co.uk/2017/11/30/coinbaseirsorder.pdf

US District Court, Northern District of California: *United States v. Coinbase (Case No. 17-cv-01431-JSC)*

WESTERN EUROPE

France

France's Constitutional Court has ruled that a proposed temporary additional tax on large companies, recently approved by parliament, does not breach the country's constitution.

The Court considered the constitutionality of the tax after members of parliament challenged the manner in which the measure was passed, as well as the legality of the tax itself.

In its ruling, the Court said that the tax was not "confiscatory" or discriminatory against the companies in question, and was in conformity with the French Constitution.

The amendment, approved by parliament on November 14, 2017, effectively increases the corporate tax from 33.3 percent to 38.3 percent for companies with turnover in excess of EUR1bn (USD1.2bn) and to 43.3 percent for companies with turnover in excess of EUR3bn.

The temporary surcharge will apply for financial years ending between December 31, 2017, and December 30, 2018.

The measure is intended to raise an additional EUR5bn in revenue, which, when combined with proposed spending cuts, will allow France to meet its 2.9 percent of GDP budget deficit target for 2017.

The French Government is facing a bill of around EUR10bn to refund companies that paid a surtax ruled illegal by the Constitutional Court on October 6, 2017.

The current ruling was issued on November 29, 2017.

http://www.conseil-constitutionnel.fr/conseil-constitutionnel/francais/les-decisions/acces-par-date/decisions-depuis-1959/2017/2017-755-dc/decision-n-2017-755-dc-du-29-novembre-2017.150219.html

French Constitutional Court: *Decision No. 2017-755 DC*

Ireland

The European Court of Justice (ECJ) has ruled that the EU principle prohibiting abusive practices remains effective, enabling the Irish tax authority to prevent a taxpayer from obtaining an inappropriate value-added tax (VAT) benefit – even though Irish law does not contain provisions to that effect.

The case concerned a dispute between property developers and the Irish Revenue Commission dating back to 2004, in which the Revenue Commissioners argued that the taxpayers had structured the sale of holiday homes with the sole intention of circumventing VAT on the sale.

The developers jointly owned a development site in Ireland on which they constructed 15 holiday homes intended for sale. Before making the sales, those co-owners entered into two lease arrangements with an associated company, Shamrock Estates, in March 2002.

In April 2002, the two leases, which included a long lease and a short lease, were extinguished by mutual surrender of the lessees, and the co-owners therefore recovered full ownership of the properties. Then in May 2002, the co-owners sold all the properties to third parties.

Under Irish VAT legislation, no VAT was payable on those sales, as the properties had previously been the subject of a first supply on which VAT was chargeable, when the long lease was granted.

However, the Revenue Commissioners took the view that the leases constituted a first supply artificially created in order to avoid the subsequent sales being liable to VAT and that supply should therefore be disregarded for the purposes of assessing VAT. Consequently, in an assessment dated August 27, 2004, the Revenue asked the co-owners to pay additional VAT in respect of the sales.

On appeal, the High Court (Ireland) held that, as the leases lacked commercial reality, they constituted an abusive practice within the meaning of the case law stemming from a previous ECJ ruling, *Halifax plc and others v. HM Customs & Excise*.

The co-owners launched a further appeal to the Irish Supreme Court, which subsequently asked the ECJ whether the principle that abusive practices are prohibited – a general principle of EU law – is capable, regardless of measures giving effect to it in national law, of being applied directly in order to refuse to exempt sales of immovable property from VAT. In addition, the Supreme Court raised the issue of whether the application of the principle was consistent with the principles of legal certainty and of the protection of legitimate expectations, given that the transactions at issue were carried out before the judgment in *Halifax* was delivered.

In its ruling, the ECJ said that based on case law, the principle at issue "may be relied on against a taxable person to refuse him, *inter alia*, the right to exemption from VAT, even in the absence of provisions of national law providing for such refusal."

The ECJ also confirmed that the application of the principle in this instance is "consistent with the principles of legal certainty and of the protection of legitimate expectations, even if its application concerns transactions carried out before the judgment in *Halifax* was delivered."

This judgment was released on November 22.

https://curia.europa.eu/jcms/upload/docs/application/pdf/2017-11/cp170123en.pdf

European Court of Justice: *Edward Cussens and Others v. T.G. Brosnan (Case C-251/16)*

Poland

The European Court of Justice (ECJ) has provided another ruling on the value-added tax (VAT) treatment of pastry goods and cakes.

A Polish court sought clarification from the ECJ after a taxpayer questioned a Polish legal provision providing that the 8 percent reduced VAT rate should apply only to those pastry goods or cakes that have a use-by date or best-before date not exceeding 45 days.

In a preliminary ruling, the ECJ said that states have discretion to set the limitations for the application of a reduced VAT rate to foodstuffs for human consumption, providing such provisions do not contravene the principle of fiscal neutrality.

The ECJ ruled that it is for the national court to assess whether, in the Polish market, there are pastry goods or cakes whose shelf life does not exceed 45 days but which nevertheless are similar in the eyes of that consumer to pastry goods and cakes which have a best-before date exceeding 45 days, such as those produced by the taxpayer, and which are interchangeable with the latter. In such cases, the principle of fiscal neutrality would preclude such a provision and Poland would be required to amend its VAT law.

The ECJ ruled:

> "Article 98 of Council Directive 2006/112/EC of November 28, 2006, on the common system of value-added tax, must be interpreted as meaning that it does not preclude – provided that the principle of fiscal neutrality is complied with, which is for the referring

> court to ascertain – national legislation, such as that at issue in the main proceedings, which makes the application of the reduced VAT rate to fresh pastry goods and cakes depend solely on the criterion of their 'best-before date' or their 'use-by date'."

The preliminary ruling was delivered on November 9, 2017.

http://curia.europa.eu/juris/document/document.jsf?text=&docid=196498&pageIndex=0&doclang=EN&mode=req&dir=&occ=first&part=1&cid=2446652

European Court of Justice: *AZ v. Polish Finance Minister (Case C-499/16)*

United Kingdom

A London-based Employment Appeal Tribunal ruling has raised the potential for gig economy companies such as Uber to face increased employment tax liabilities in the same way as for "traditional" employers.

Uber had appealed against a November 2016 ruling by London's Employment Tribunal (LET) that it should offer its drivers the same employment rights as traditional taxi service operators, rather than its drivers being unconnected self-employed persons. That case had been brought by professional drivers' union the GMB on behalf of two drivers. The Tribunal had determined that Uber had acted unlawfully in not providing the drivers with basic workers' rights, and that they are entitled to receive holiday pay, a guaranteed minimum wage, and breaks.

Uber appealed on the basis that:

- There was no contract between them and the drivers, but the agreements in place between them were inconsistent with the existence of a worker relationship;
- The LET had erred in relying on regulatory requirements as evidence of worker status;
- The LET had made numerous internally inconsistent and perverse findings of fact in concluding the claimants were required to work for Uber; and
- The LET had further failed to take into account relevant matters relied on by Uber as inconsistent with worker status and as strongly indicating that the claimants were carrying on a business undertaking on their own account.

The Appeal Tribunal held that the LET had been entitled to reject the characterization of the relationship between the drivers and Uber as stated in the written contractual documentation. It found in the context of an agency relationship that:

> "the reality of the situation was that the drivers were incorporated into the Uber business of providing transportation services, subject to arrangements and controls that pointed away from their working in business on their own account in a direct contractual relationship with the passenger each time they accepted a trip. Having thus determined the true nature of the parties' bargain, the [LET] had permissibly rejected the label of agency used in the written contractual documentation. The [LET] had not thereby disregarded the principles of agency law but had been entitled to consider the true agreement between the parties was not one in which [Uber] acted as the drivers' agent.
>
> … In particular, the [LET] had permissibly concluded there were obligations upon Uber drivers that they should accept trips offered by [Uber] and that they should not cancel trips once accepted (there being potential penalties for doing so). It was, further, no objection that the [LET's] approach required the drivers not only to be in the relevant territory, with the app switched on, but also to be 'able and willing to accept assignments'; that was consistent with Uber's own description of a driver's obligation when 'on-duty'. These findings had informed the [LET's] conclusions not just on worker status but also on working time and as to the approach to be taken to their rights to minimum wage."

Although the ruling did not discuss tax implications for Uber, the ruling could open the door to Uber becoming liable to taxes in the UK for its drivers, such as National Insurance (social security) contributions. It could also potentially result in a change to its VAT treatment. Uber has since indicated that it is considering an appeal to the Supreme Court.

The Good Law Project has launched legal action concerning Uber's VAT arrangements. Jolyon Maugham QC is seeking a decision from the High Court over whether the supplies facilitated by Uber should be liable to VAT – specifically he is asking whether a supply is made by an Uber driver, or whether the supply is made by Uber, by asking questions about his eligibility to an input tax credit for VAT that would be liable on a fare paid.

The Employment Appeal Tribunal ruling was handed down on November 10, 2017.

https://assets.publishing.service.gov.uk/media/5a046b06e5274a0ee5a1f171/Uber_B.V._and_Others_v_Mr_Y_Aslam_and_Others_UKEAT_0056_17_DA.pdf

London Employment Appeal Tribunal: *Uber v. Mr Aslam and others (UKEAT/0056/17/DA)*

United Kingdom

HM Revenue & Customs (HMRC) has said that a ruling from the UK's Supreme Court on November 15, 2017, against users of a failed tax avoidance film partnership scheme will save taxpayers over GBP1bn.

HMRC explained that the scheme sought to use legitimate investment in the film industry as a hook for tax avoidance.

HMRC had previously defeated the avoidance scheme in *HMRC v. De Silva and another ([2016] EWCA Civ 40)*. The appellants sought to argue on a technicality that HMRC could not overturn their loss relief claims. However, the Supreme Court disagreed, and ruled in favor of HMRC.

Summarizing the ruling, the Supreme Court said the appellants had invested in and became limited partners of various partnerships in implementing marketed tax avoidance schemes. The schemes were aimed at accruing substantial trading losses through investment in films.

The partnerships had claimed they had suffered such losses in several tax years and claimed relief for film expenditure by taking advantage of tax incentives under section 42 of the Finance (No. 2) Act 1992. In the early years of trading, a limited partner could use the provisions of sections 380 and 381 of the Income and Corporation Taxes Act 1998 to set off his allocated share of trading losses of a partnership against his general income for that year, or any of the previous three years of assessment.

HMRC did not accept the claims for relief and initiated inquiries into their tax returns under section 12AC(1) of the Taxes Management Act 1970 (TMA). HMRC disallowed the partnerships' claims for expenditure funded by non-recourse or limited recourse loans to individual partners and also expenditure paid as fees to the promoters of the schemes. The partnerships appealed.

Thereafter, on August 22, 2011, the partnership losses were stated at much reduced levels in a partnership settlement agreement. Between September and November 2011, HMRC wrote to the appellants to intimate that their carryback claims in their personal tax returns would be amended in line with the lower figures for the partnership losses stated in the partnership settlement agreement.

The appellants raised judicial review proceedings against HMRC's decisions. They asserted that HMRC was entitled to inquire into their claims only under Schedule 1A to the TMA and that, because the statutory time limit for such an enquiry had expired, the appellants' claims to carry back the partnership losses in full had become unchallengeable. The Upper Tribunal rejected the appellants' claim, and the Court of Appeal dismissed their appeal. The appellants then appealed to the Supreme Court, which has unanimously dismissed the appeal.

HMRC Director General for Customer Strategy and Tax Design, Jim Harra, said: "This is another great success in HMRC's drive against tax avoidance. HMRC defeated [the appellants'] tax avoidance scheme but they still argued on a technicality that the department could not collect the tax. The Supreme Court's decision in favor of HMRC on this point will ensure that these taxpayers and others waiting behind their case will have to pay what they owe."

The Supreme Court judgment was delivered on November 15.

https://www.supremecourt.uk/cases/docs/uksc-2016-0053-judgment.pdf

UK Supreme Court: *De Silva and another v. HMRC ([2017] UKSC 74)*

Dateline December 7, 2017

Globally, we are witnessing **ambitious reforms** being attempted in the area of taxation. In the **United States**, Congress is on the brink of finalizing the most ambitious tax reform in more than 30 years. More on that later. In the **European Union**, certain member states and the Commission are pushing hard for harmonization of corporate tax rules and the creation of new tax rules for the **digital economy**. And globally the tax landscape is changing on a daily basis thanks to BEPS.

Major tax reform efforts are often undertaken with the intention of making life easier for taxpayers. But they can be **enormously disruptive** for tax planning in the short-term, as taxpayers adjust to life under a new regime. Spare a thought then for taxpayers in **India**. There, they are still getting used to the idea of the national **goods and services tax** (GST), often described as one of the most significant economic reforms in India's post-colonial history. Now they could be faced with a **shake-up of direct taxation** as well.

By putting in place the GST regime this year, the current Government was congratulated for achieving in three years what the previous administration had failed to do in ten. Will it be able to pull off a similar achievement with the direct taxes code?

Reforming the outdated direct tax regime in a similarly expedient manner would represent a spectacular success for the Modi Government with regards to tax policy. But viewed in the light of the indirect tax reforms, perhaps it would be easy to underestimate the scale of the task at hand.

This wouldn't be the first time such an undertaking has been attempted. Indeed, direct tax reform has a history stretching back as far as the GST legislation. But this project wasn't nearly as successful. The Modi Government eventually cancelled the Direct Taxes Code, first introduced in 2009, as the proposed legislation was known, because it had hung around Committee Land so long it had become outdated, which was rather ironic given its intent was tax code modernization.

So perhaps taxpayers shouldn't get their hopes up too much. Indeed, the prospect that direct taxation may or may not be subject to reform may merely **increase tax uncertainty** for taxpayers in India. But at least they are already well used to that.

Nevertheless, on a global scale, taxes are, apparently, getting less taxing, thanks largely to **increasing automation** and digitalization **of tax compliance processes**. This was one of the main conclusions of PwC's recently published 2018 Paying Taxes report, which shows that it's getting easier for businesses to calculate their taxes, file their returns, and pay. However, that the average **length of time** it takes the average-mid sized business to comply with its tax requirement is down to just **240 hours** is surely a sign of the times – *i.e.*, tax administration might be a bit easier, but tax rules certainly aren't. After all, 240 hours is 20 solid days (and nights). If you were to spend each eight-hour working day on a project that was to take 240 hours, you'd be at it for a month, give or take.

It should be emphasized, however, that this is very much an average. Just as no two companies are identical, each tax jurisdiction is unique. So the experiences of an individual company, be it small, medium-sized, or large, will vary greatly depending on the activities of that business, and where it is located. But, undeniably, the PwC ranking does give a good indication of the wide disparity in tax requirements across the world for businesses.

In **Venezuela** – 189th and last in the ranking – it takes 792 hours for a medium-size business to fulfill its tax obligations. But believe it or not, there are places where it takes even longer for a business to comply with tax rules. Businesses wrangling with the infamously complex tax environment of **Brazil** spend about 1,000 hours more a year on their tax obligations than they would in Venezuela. And it's also saying something about the modern international tax environment that as far as Brazil is concerned this is a considerable improvement on previous years.

Indeed, South America generally retains its reputation as a nightmarish place to comply with tax obligations. **Bolivia** for instance features in 186th place in the list, with compliance taking an average of 1,025 hours and with a total tax rate – made up of corporate, labor, and other taxes paid by businesses – of 83.7 percent. It makes you wonder if businesses there have time to do any business at all, or if they are simply in the business of paying tax.

It will be interesting to see if **tax reform in the United States** will improve the country's ranking in the PwC index (currently 36th). It is very likely to be the case that corporations would pay substantially less tax, but whether calculating these taxes, given the US is stuck with its dual federal/state system, would become easier, remains to be seen. Still, tax reform legislation is now beginning to move through Congress at what feels like light speed compared with the gridlock us observers have grown accustomed to watching over the years, especially after the Senate version scraped through a full vote by the upper chamber last week. Nevertheless, perhaps we shouldn't get too giddy with excitement that generational tax change could be just around the corner. For while there were a few revenue-raisers in the last-minute revisions so that the bill can squeeze under the budget bar set by the **Byrd rule**, there were also a few eyebrow-raisers as a result.

Controversially, one of America's most disliked tax provisions, the **alternative minimum tax**, makes a reappearance in the Senate bill to help the sums add up, while the individual income tax cuts expire after 2025 so they don't add to the deficit outside of the ten-year budget window.

There are also other significant differences. Notably, House and Senate lawmakers are going to have to decide what they want in the crucial area of **pass-through business taxation** – a 25 percent tax cap, or a 23 percent tax deduction? Do they want a slimmer five-bracket income tax schedule, or a reconfigured seven-bracket system with slightly lower rates? Obamacare individual mandate or not? An estate tax or no estate tax?

With events on the Hill often taking unexpected turns, it would be unwise to speculate too much what a **final bill** might look like, and when it could be finalized. But perhaps one thing's more certain: tax advisors had better not plan too much time off this Christmas.

The Jester