

TAX LINK

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Australia Welcome improvements to Australian employee recruitment and retention regime

For existing businesses and new businesses setting up in Australia, one of the major challenges is the recruitment and retention of key employees: those that can make a difference between a successful venture and one that may not last the course. Giving those employees an interest in the company, through providing them with access to shares in the company, is one of the tools available in the toolbox. Whilst many countries will have such a regime, the challenge often is how to avoid or minimise the employee's tax charge, especially before the employee has any proceeds with which to pay the tax. And it is here that things are changing for the better in Australia.

In 2009, the Australian Government at the time, introduced legislation revising the taxation of Employee Share Acquisition Schemes in Australia. The basic principle of the both the current and former rules is to tax any discount given in relation to shares or rights acquired by an employee under an Employee Share Scheme. Broadly, the discount represents the difference between the market value of a share or right and the consideration paid to acquire it.

By default, both rules result in taxation of the discount in the year that the interest is acquired. However, prior to 2009, it was possible (and relatively easy) to defer the taxation of this discount until the earlier of:

- 1) when the share/right was disposed of
- 2) when there are no restrictions on the exercising of the right
- 3) when the employment in respect of which the share/right was acquired ceases
- 4) when there are no restrictions on the disposal of the share/right; or
- 5) ten years from the date of acquisition of the share/right.

Since the revised legislation took effect in 2009, the rules were tightened such that there must be a 'real risk', under the conditions of the Employee Share Scheme, that the interest could be forfeited or lost in order to defer the taxation of any discount.

As a result of the 2009 legislation, Employee Share Schemes lost popularity as in many instances, employees would be required to pay tax in the year of receipt of the shares/rights without having the ability to be able to sell any portion of their shares/rights to fund the cost of their tax liability.

The current Australian Government has announced that they are intending to revoke the existing rules and are considering allowing employees to be taxed once the shares are sold. It

is likely that any changes to the legislation will be subject to eligibility rules (excluding some higher income earners and large corporations from participating). The changes will be welcomed by start-ups seeking to provide an equity incentive for employees contributing to the early growth of the business.

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Belgium The fairness tax: An eyesore for international tax planning

As of tax year 2014 (ie financial years ending as of 31/12/2013) a new Belgian tax measure has been implemented, the so called "fairness tax" on distributed dividends. This new tax can have an impact on (inter) national tax planning of Belgian companies distributing dividends, whilst using tax losses or notional interest deduction to offset their Belgian taxable profits.

The fairness tax is applicable to all Belgian companies that do not qualify as a 'SME company' (on a consolidated basis) under the Belgian company code.

In a nutshell, a separate assessment of 5% (to be increased with a 3% crisis surcharge) will potentially be due in case of a dividend distribution when (part of the) distributed profits have not been effectively taxed at the nominal Belgian corporate income tax rate.

If this is the case and the taxable basis is reduced due to the notional interest deduction or tax losses carried forward, the fairness tax will be due.

Hence there are three conditions in order to assess a possible fairness tax exposure:

- 1) is the Belgian company distributing the dividend not a SME company (specific criteria)?
- 2) does the distributed dividend exceed the taxable basis of the Belgian company?
- 3) does the Belgian company use the notional interest deduction or tax losses carried forward in order to lower its effective tax rate?

If the answer on all three questions is affirmative, then the complexities of the new tax measure kick in.

The way to calculate the actual fairness tax is rather complex and consists of four steps. We will briefly elaborate on the mechanism. However, for more

information we strongly suggest to contact Nexia's Belgian member firm.

First we calculate the "untaxed" part of the dividend distribution by determining the positive difference between the dividends distributed and the taxable result that is effectively subject to the nominal corporate tax rate. If the actual taxable basis equals zero, the entire dividend has to be taken into account. However if the dividend includes retained earnings for past years, these have to be excluded (exceptions to be taken into account).

The "untaxed" part will then be limited by a percentage taking into account the amount of tax losses carried forward and notional interest deduction that has been effectively used to lower the taxable basis. On the outcome a separate tax of 5.15% will be levied.

Note that this tax can't be reduced with tax deductions ie the notional interest deduction, tax losses carried forward, etc. and will thus always be due.

Example

BelCo distributes a dividend of EUR4,000k. The dividend exceeds the taxable basis of the company due to the use of notional interest deduction.

Calculation:	in (k)EUR
Taxable result (excl. disallowed expenses and dividend distribution)	1,000
Disallowed expenses	200
Distributed dividend [A]	4,000
Taxable result (incl. disallowed expenses and dividend distribution) [F]	5,200
Minus:	
Notional interest deduction [D]	-2,000
Tax losses carried forward [E]	0
Taxable result subject to nominal corporate income tax rate [B]	3,200

Fairness tax: calculation

Step 1: [A] - [B]	800 (i)
Step 2: No formerly taxed reserves included in dividend	-
Step 3: Application of percentage = ([D] + [E]) / [B]	38.46% (ii)
Step 4: Calculation of the fairness tax basis = 800 x 38,46%	308
Fairness tax due equals (= 308 x 5.15%)	16

Conclusion:

This new "fairness tax" can have an impact on the (inter) national tax planning of large company structures. International tax structures involving Belgian companies should be re-examined in order to assess a possible tax exposure. Most likely the fairness tax is the result of the increasing awareness of base erosion and profits shifting (BEPS).

However, is it "fair" that a company is "taxed" for using a "tax deduction" that has been implemented in the Belgian tax code for years?

For more information, contact Nexia's Belgian member firm.

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Canada U.S. intergovernmental agreement and recent foreign affiliate issues

U.S. “FATCA” and the concern for Canadians under new intergovernmental agreement

In 2010, many of us recall the news of the U.S. passing legislation called “The Foreign Account Tax Compliance Act”, otherwise known as “FATCA”, in an effort to battle the tax evasion by U.S. citizens and residents using offshore accounts and investments.

Under FATCA, non-U.S. financial institutions are required to report certain information to the U.S. Internal Revenue Service (IRS) regarding financial accounts held by U.S. persons. In the event of non-compliance, the IRS can impose a 30% withholding tax on U.S. source payments to the financial institution or its clients.

The news quickly spread drawing the attention of Canadian financial institutions, given the significant amount of cross-border activity with the U.S., and the concerns with still adhering to domestic privacy and other laws. Although changes were subsequently made to avoid the 30% withholding tax in most situations, much of the legislation still has an impact.

Following the responses from many financial institutions, the U.S. realized that non-U.S. financial institutions may have difficulties complying with FATCA due to such conflicts with domestic laws. As a result, the U.S. offered a deal to countries to avoid much of FATCA by entering into an intergovernmental agreement (IGA).

On 5 February 2014, the Canadian government announced its entry into an IGA with the U.S. The announcement was quickly followed by draft legislation to implement the IGA into Canadian law under the existing Canada-U.S. Tax Convention, taking effect 1 July 2014.

Under the IGA, financial institutions in Canada will still be required to report the necessary information under FATCA regarding accounts of U.S. persons. However, the information will be collected by Canada Revenue Agency (CRA), instead of sending directly to the IRS. The CRA will then exchange the information with the IRS pursuant to the IGA.

Perhaps some of the unintended consequences of the IGA are Canadian trusts that could potentially be treated as “foreign financial institutions” under FATCA. As with anything, the devil is in the details and the issue certainly exists in this case. Although the IGA defines a “financial institution” for FATCA purposes, the Canadian legislation takes a narrower approach to define entities considered a “Canadian financial institution” for the purposes of the IGA. The Canadian legislation excludes entities such as personal trusts, but does include entities such as those promoted to the public as venture capital funds, mutual funds, hedge funds, exchange traded funds or other similar investment vehicles established to trade or invest financial assets.

With this narrower definition of “Canadian financial institutions”, the concern is U.S. tax authorities objecting and requiring the definition to conform to the IGA’s, as was done by the U.S. in another jurisdiction. If the definition of “financial institution” was revised to the U.S. interpretation, many who may not consider themselves Canadian financial institutions could fall within this broader interpretation and be delinquent in reporting obligations under FATCA, in addition to other implications moving forward. As a result, entities with potential exposure would be well advised to follow the legislative developments as more details arise.

Court limits scope of foreign affiliate anti-avoidance rule
Pursuant to a recent Canadian Federal Court of Appeal’s (FCA) decision, a longstanding anti-avoidance rule maintained by the CRA and Tax Court of Canada (TCC) has become restricted to the delight of many taxpayers and advisors. In *The Queen v. Lehigh Cement Limited* and *The Queen v. CBR Alberta Limited* (Lehigh), the FCA rejected the broad interpretation of the provision previously relied on by the CRA and TCC to deny benefits to certain Canadian taxpayers with foreign affiliates.



Paragraph 95(6)(b) of the Income Tax Act (ITA) (Canada) is a broad anti-avoidance rule which may deem foreign affiliate shares not to have been issued under certain circumstances. The provision generally applies where the acquisition of shares of a foreign corporation may reasonably be considered to have been for the principal purpose of avoiding, reducing or deferring taxes.

Under the ITA, a “foreign affiliate” (in general terms) is a foreign corporation in which a Canadian taxpayer owns 10% or more of any class of shares. The significance of foreign affiliate status is extensive, including such benefits as allowing dividends from the foreign corporation to be deducted by the Canadian shareholder corporation when paid from after-tax earnings. Where the foreign affiliate status is not met, such dividends would still be included in income by the shareholder, but without the ability to claim the offsetting deduction available only on dividends from foreign affiliates.

In contrast, a “controlled foreign affiliate” (CFA) requires the Canadian parent to recognize passive income of the CFA, otherwise known as “foreign accrual property income” (FAPI), as if the income was earned directly as its own. In such situations, the Canadian taxpayer would be motivated to reduce its ownership to a lesser percentage and avoid recognising FAPI.

Under the ITA general anti-avoidance rule (GAAR), it must be shown that the transaction, or series of transactions, are structured in a manner that is considered abusive and results in the avoidance of taxes with rules in place to recharacterise the transaction(s). However, under Paragraph 95(6)(b), the shares are simply deemed not to have been acquired or disposed of for the purposes of determining foreign affiliate status, without similar rules to limit the use by the CRA and TCC to situations where abuse is evident. With respect to the Lehigh decision, the FCA concluded it would not agree to the CRA exercising such “unlimited and ill-defined discretion”. In short, the FCA confirmed the provision should only be used where the foreign affiliate status is artificially created or, in the case of controlled foreign affiliates, artificially avoided.

‘Foreign affiliate dumping’ rules- A recap

Originally proposed in the 29 March 2012 Federal Budget, the “foreign affiliate dumping” rules (“FA dumping rules”) were introduced to discourage foreign-based multinational corporations from using their Canadian subsidiaries to invest in other foreign subsidiaries to result in an erosion of their Canadian tax base. On 16 August 2013, additional proposals were also released to amend various aspects of the FA dumping rules, however most rules continue to apply to all transactions (or series of transactions) occurring on or after 29 March 2012. Although the rules have been in place for some time now, it is an issue worth reviewing

given the extent they may impact foreign investors. The rules are extremely complex and apply very broadly, beyond the scope of the original target. Therefore, this article is intended only to highlight some of the issues and to encourage seeking advice where such corporate structures exist.

In general, the FA dumping rules apply where a corporation resident in Canada (CRIC) is controlled by a foreign corporation (“foreign parent”) and makes an investment in a foreign affiliate. The Department of Finance (Canada) released Explanatory Notes to provide details as to its intent of the legislation and how the Canadian tax base was eroding. They summarised two ways the tax erosion can occur; (i) interest deductions in Canada reduce income subject to Canadian tax while avoiding Canadian tax on foreign source income; or (ii) surplus taken out of Canada while not subject to Canadian non-resident withholding tax.

The FA dumping rules seek to prevent this by deeming downstream “investments” by the CRIC to the foreign affiliate to be dividends paid to the foreign parent, subject to Canadian non-resident withholding tax, unless the payment is treated as a reduction to share paid-up capital (PUC). The term “investment” is applied very broadly and includes virtually any downstream payment limited by few exceptions. Some more common examples are; acquisition of foreign affiliate shares, contributions of capital (value) to the foreign affiliate, indebtedness by the foreign affiliate to the CRIC outside the ordinary course of business and not repaid within 180 days, the CRIC acquiring shares of the foreign affiliate indirectly through another Canadian corporation, or the CRIC acquiring an option to acquire the shares of the foreign affiliate.

A foreign corporation is generally a foreign affiliate of the CRIC if the CRIC owns (directly or indirectly) at least 1% of any class of the foreign corporation’s shares and owns (directly or indirectly and together with related persons) at least 10% of any class of the foreign corporation’s shares. Three exceptions are available: (i) more closely connected business activities, (ii) certain internal reorganizations, and (iii) pertinent loans or indebtedness.

As noted previously, the FA dumping rules are extremely complex and have broad exposure going well beyond the items outlined above. In the event of such corporate structures, we strongly recommend seeking advice and a thorough review of the applicability of the FA dumping rules.

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China Cross-Border services into China: A case study

Whenever an overseas company provides services for a client situated in China, careful planning of the transaction is necessary, and the terms of a service contract between the overseas service provider and the service recipient must be consistent with the plans. Proper preparation will not only ensure that potential China-related taxes are minimised, but will also ensure that the service fees can be paid to and received by the overseas service provider. As cross-border transaction advisors, we are often called upon to assist clients with problems that result from a failure to plan in advance. In many cases, too much China tax is paid. In the worst of cases, the overseas service provider is not even able to receive payment of the service fees. In the following paragraphs, we offer a true case study that highlights common transaction planning issues.

Case background

A design company (“DesignCo”) is headquartered in Los Angeles, California and is the 100% owner of a small subsidiary (“DesignSub”) in Beijing, China. At the time of this case, DesignSub did not have the capability to manage large design projects and was generating revenues barely sufficient to earn a slight profit each year. Thus, when the opportunity for a USD2 million project appeared in Beijing, DesignCo from the USA directly contracted with the Beijing customer (“BeiCo”). This was a two-year design project during which DesignCo committed to sending its own employees to perform the work in China. DesignSub was not a party to the contract. In spite of this, DesignCo agreed – at BeiCo’s insistence – to let BeiCo pay the service fees into DesignSub’s Beijing bank account using RMB currency. This payment method allowed BeiCo to avoid the administrative responsibility, time and cost for acting as tax withholding agent and handling the required procedures for making a cross-border payment in US Dollars. Based on minimal inquiry, DesignCo assumed that only 10% withholding tax would apply to the transaction, and that once the tax was paid, DesignSub would be able to transfer the USD2m in service fees to DesignCo’s USA bank account.

DesignCo’s assumptions proved to be incorrect. Certainly a more thorough investigation into applicable Chinese taxation would have been helpful in the transaction planning. However, in the end, it was the contract payment terms that proved most fatal, causing a snowball of negative events that resulted in DesignCo ultimately receiving only about 58% of the contracted fees charged.

Why didn’t it work?

China’s State Administration of Foreign Exchange (SAFE) rules require that any cross border services payment be accompanied by evidence of a “genuine and consistent” transaction. Proof of a “genuine” transaction would include a service contract between a named overseas service provider and a named service recipient in China, in which specific services and fees are described, as well as payment terms between the parties. Evidence of a “consistent” transaction would include an invoice issued directly from the service provider named in the contract to the service recipient that is named in the contract. Payments generally cannot be made to or from third parties on behalf of the service provider and service recipient that are named in the service contract.

In this case, DesignSub was not the named service provider in the service agreement, and technically, naming DesignSub’s Beijing bank account as the recipient of the payment on behalf of DesignCo was not allowed. In order for BeiCo to make the payment to DesignSub, DesignSub first had to issue an invoice. On receipt of the payment, DesignSub had to book the payment as service revenue. Business Tax plus local surcharge taxes amounting to 3.39% immediately applied to the payment and was paid by DesignSub (now, since the VAT reforms are in place, 6% VAT would have to be charged to BeiCo). SAFE does not monitor domestic transactions involving only RMB, so this part of the transaction proceeded without detection.

However, when DesignSub attempted to transfer the payment to DesignCo, the transaction was not allowed to proceed. No “genuine and consistent” transaction existed that would allow DesignSub to send the funds to DesignCo. The two companies had no service agreement in place under which DesignCo could issue an invoice, and DesignSub was not named as a service recipient in the original contract with BeiCo. The payment thus became “trapped” in China.

The only SAFE-compliant method available for DesignSub to transfer the funds to DesignCo was a profits dividend distribution, which could only be made after DesignSub completed its annual Enterprise Income Tax (EIT) filing and settlement for the tax year. Having booked the BeiCo payment as service revenue, and having only the 3.39% business tax as a deduction, 96.61% of the USD2m was taxed at 25% for EIT. DesignSub thus paid nearly 28% total tax on the payment, leaving 72% as after-tax profit. Before making a dividend payment, however, DesignSub was required to deposit 10% of the after-tax profit into its statutory reserve fund, reducing the amount of the dividend to about 64.5% of the original \$2 million. Further reducing the amount that was sent to DesignCo was the 10% withholding tax that applies to dividends sent to a USA parent company. When the entire process was completed, DesignCo finally received approximately 58% of their contracted fees for the BeiCo project.

Workable alternatives

Of course the simplest solution, which would also maximise the amount of fees that DesignCo could receive, would be for DesignCo to insist that BeiCo make the fee payment directly to DesignCo's USA bank account. In this case, BeiCo would have to act as tax withholding agent, but not for 10% withholding tax. Because of the long-term presence in China of DesignCo employees during the project, DesignCo would have to pay 25% EIT as a Permanent Establishment. The tax would be based on a "deemed profit." There are several methods that tax bureaus use to calculate the "deemed profit," each method dependent on the service transaction records that are submitted. A very common method would arrive at a "deemed profit" of 30% of the total service fee. With appropriate planning and record keeping by DesignCo, the "deemed profit" could be lower still.

Indirect Tax would also apply to this transaction. Because of the timing under which the original contract in this case was executed, Business Tax would apply, just as it did for the payment made to DesignSub. However, with the payment going directly to DesignCo, the 3.39% Business Tax would have to be withheld from the payment. As a brief note here, a similar contract executed today would fall under the VAT reform regulations, and as such, the transaction would be subject to 6% VAT (plus the local surcharges). As it is the service recipient who should pay VAT, DesignCo would have to negotiate this responsibility into the contract, as we specified in our May 2013 TaxLink article on cross border transactions.

If BeiCo insisted that they would only do the business if they could make the payment locally in RMB, DesignSub would have to be the primary contractor with BeiCo. DesignSub would then contract with DesignCo to be a subcontractor in the project, and this contract would then provide the evidence of a "genuine" transaction. However, in this case, DesignCo would have to consider "arm's length" transfer pricing principles in the service fees charged to its subsidiary, DesignSub. Certainly, DesignSub would have to keep at least some percentage of the total fees, but the fees paid to DesignCo would be tax deductible. Given that

DesignCo employee presence is still required, Permanent Establishment EIT would still apply to DesignCo's "deemed profits," and indirect tax would also apply. Under the conditions of this arrangement, DesignCo would indeed receive a lower percentage of the fees than if properly contracting with BeiCo directly, but there is no doubt that the total tax impact would be far less than what occurred in the unplanned transaction.

In closing

One can deduce from the above that there are many aspects of cross border transactions to be considered and planned for in advance. It would be impossible in a short article to expand on all the details of this case, but the brief descriptions offered here do shed light on the fact that when foreign entities do business in China, many different regulations and regulatory agencies are involved. They are all interwoven and interconnected. A failure to account for one aspect can negatively affect all the others. The best advice anyone can offer is that every overseas service provider should enter into China transactions with eyes fully open. Seek knowledgeable help and understand the rules. From that base, it then becomes possible to find workable methods of gaining tax efficiency in the transactions.

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Hong Kong Receipt of dividend earnings from PRC: The tax advantages and difficulties encountered by Hong Kong companies

From 1 January 2008, subject to the tax treaties entered into by the PRC Government and various foreign governments, with the implementation of the new "Corporate Income Tax Law" and "Implementation Regulations of Corporate Income Tax Law", the PRC Government imposed a 10% corporate income tax on the dividends that foreign investors receive from PRC local enterprises.

Under "The Arrangement between the Mainland of China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation on Income and the Prevention of Fiscal Evasion" the PRC Government only imposes a reduced, 5%, corporate income tax on the dividend earnings obtained from PRC local enterprises provided that the recipients are Hong Kong companies which hold 25% or above of the shareholding in those PRC local enterprises ('Benefited Hong Kong Companies').

Hence, it provides potential opportunities to those operating through Hong Kong. As a result, Hong Kong has become a favourable place for those investors who seek a lower tax impact on their operations.

However, the PRC tax authority imposes strict criteria on those companies seeking Benefited Hong Kong Company status. They will challenge whether the Hong Kong company (ie the applicant) is the 'Beneficiary' of those dividend earnings. 'Beneficiary' means those having the control power and disposal power over such dividend earnings and the rights to them. Agent or vessel companies are not accepted as a 'Beneficiary'. As a result, in practice, Hong Kong companies will encounter many difficulties if they are to enjoy this benefit.

In October 2009, The State Administration of Taxation (SAT) issued Guoshuihan [2009] 601 ('Notice 601'), for existing tax treaties. It stated how the tax authorities would assess whether the applicant is a 'Beneficiary'. Notice 601 emphasizes that the assessment will follow the principle of 'Substance over Form'. It also stated 5 relevant negative factors:

- 1) the applicant has an obligation to pay or distribute all or the majority of its dividend earnings to foreign residents within a specific period
- 2) except having rights to receive dividend earnings, the applicant does not carry any significant business activity
- 3) there is a non-matching of the dividend earnings to applicant's assets, size and number of personnel
- 4) the applicant does not have any significant control power or disposal power over the dividend earnings or rights. It also does not bear significant risks to gain the dividend earnings
- 5) no tax on the dividend earnings will be charged in those contracting countries or they impose a very low tax rate on the dividend earnings.

Since the provisions of Notice 601 were based on principles, there were many disputes on whether the applicant qualified as a 'Beneficiary'. The SAT issued State Administration of Taxation Bulletin [2012] 30 ('Bulletin 30') and Shuizonghan [2013] 165 ('Notice 165') on 29 June 2012 and 12 April 2013 respectively to provide further explanation and directions on Notice 601.

Bulletin 30 emphasizes that when assessing whether the applicant is a 'Beneficiary', the tax authorities should consider all the factors stated in Notice 601. They should not conclusively decide on eligibility on the basis solely of the existence of any stated negative factor, avoidance of tax, reduction of tax, or the non existence of purposes for transferring or accumulating dividend earnings.

Bulletin 30 stated that when assessing whether the applicant is a 'Beneficiary', the tax authorities may require the applicant to provide a variety of detailed supporting documents, such as articles of association, audited financial statements, records of cash flow, board minutes, board resolutions, human resources and other resources information, expenses records, purpose of the entity and risk

taking information. Consequently, taxpayers need to have good internal control systems to keep all corporate information properly from the start of the business so as to prepare for the tax benefit approval process as taxpayers may be required to provide some unexpected information.

In addition, if 'Beneficiary' status cannot be proved within a specific time period, the tax authorities can decide to withhold the tax benefit. However, the tax authorities will return the excess tax paid after the taxpayers have obtained the approval. Unfortunately, under the PRC foreign exchange regulations, the rebate process may be complicated and prolonged.

Taxpayers may also want to consider the following suggestions in order to satisfy 'Beneficiary' status:

- 1) having sufficient capital. Hong Kong company laws do not impose a minimum issued capital requirement on Hong Kong incorporated companies. PRC tax authorities tend to question the 'Beneficiary' status for the reason of the non-matching of their capital and dividend earnings
- 2) strict compliance to the laws when handling corporate matters, including the separate legal entity concept. Some Hong Kong companies are controlled by upper layer companies, and the PRC tax authorities tend to regard those companies as vessel companies due to a lack of control power and disposal power of the dividend earnings
- 3) having an appropriate local management team. With investment holding companies having investments in subsidiaries, if they do not have other business activities, the PRC tax authorities may have concerns regarding their 'Beneficiary' status due to the negative factor of non-matching of number of personnel and dividend earnings
- 4) it is better to pay or distribute the dividend earnings to upper layer companies in a progressive way. If Hong Kong intermediate holding companies pay or distribute their dividend earnings received from PRC local enterprises to their holding companies within a short period, the PRC tax authorities will challenge their 'Beneficiary' status for the reason that the applicant may have an obligation to pay or distribute all or the majority of its dividend earnings to foreign residents within a specific period.

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India Modinomics: Is India's economy on the road to recovery?

The period between 2004 and 2014 can be easily described as the "lost decade" for an Indian economy marred with political scandals, slow economic growth, mismanaged public finances, high inflation and weakened economic sentiment. In such a scenario, the 2014 general elections gave a clear decisive electoral mandate to the charismatic leader Mr. Narendra Modi and its party – Bhartiya Janata Party (BJP). Looking at the enormity of the mandate given to Mr. Modi, it certainly looks like people of India have for the first time voted for development and investment reform and ignored the usual class, caste, religion and vote bank politics. Given its majority in the Parliament (the first single party majority in India since 1984), BJP will be free to make laws and take decisions which it deems fit without wasting time and energy building consensus and negotiating with alliance partners. In view of above, India Inc has high expectations of the Modi Government. This article tries to capture the essence of the expected tax reforms from this Modi Government.

The first document which provides an insight into the possible future reforms is the BJP Election manifesto¹. The same clearly advocates for better governance and removal of draconian/unfriendly business laws. The manifesto states that the previous government unleashed uncertainty and anxiety amongst the business class in terms of Tax Policy, which negatively impacted the investment climate and dented the image of the country. The BJP led government realizes the importance of having a Tax Policy Roadmap and lays stress on providing non adversarial and conducive tax environment with simplified tax regime.

1 www.bjp.org/manifesto2014

Issue of black money

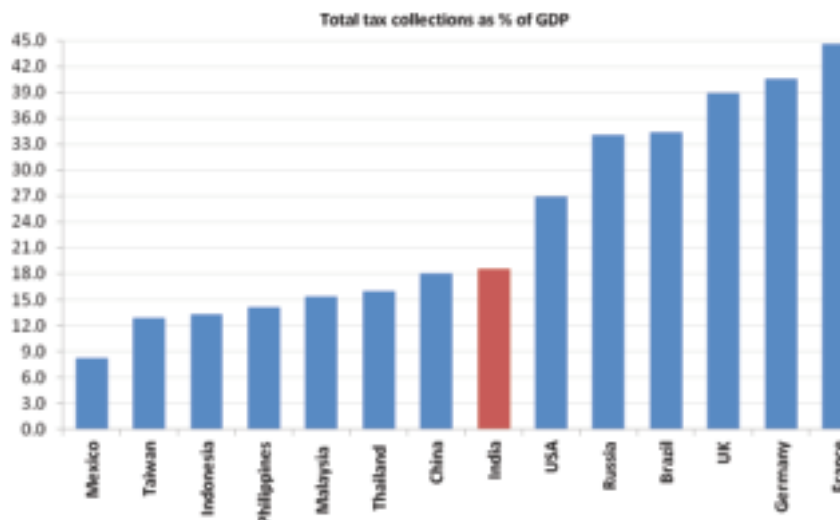
The party manifesto speaks in length about the issue of black money prevailing in the Indian economy - one of the hotly debated topics during the election campaign. The BJP government defines black money as assets that haven't been reported to the authorities at the time of their generation or disclosed at any point during their possession. According to data from Global Financial Integrity, Indians had moved \$644 billion (52% of the GDP) to tax havens as of 2011. Modi's BJP said in a 2011 report that Indians had \$250 billion, or 20 percent of the previous year's gross domestic product hiding in Switzerland alone². Furthermore, as the Bureau of International Narcotics & Law Enforcement Affairs of United States Department of State in its report "Money Laundering & Financial Crimes" published in March 2010, observed that, as per private analyst estimate, India's Black Market ranges from \$2.1-\$2.5trillion (100% of the GDP).

The extent of black money prevailing in the Indian economy is highlighted by the fact that despite having the greatest young working class population, India has the lowest tax to GDP ratio amongst its emerging market peers.

This issue of Black Money has always had sporadic voter attention for the last 20 years, until recently when in June 2011 the government received information from French authorities about 700 Indians who had accounts at HSBC Holdings Plc's Swiss branches. That data, along with details about more than 23,000 other HSBC clients, had been stolen from the bank by a former employee and eventually found its way to French officials. Since then this issue has caught the media and voter attention. Capturing the public mood, the election manifesto committed that the BJP government will track down and bring back black money stashed abroad in foreign banks and offshore accounts.

Consequently, on being elected, in a symbolic move, the first cabinet decision of the BJP government was to set up a Special Investigation Team (SIT) to unearth and bring back black money stashed abroad. The team comprised of

2 www.bloomberg.com/news/2014-06-08/hidden-assets-seen-worth-2-trillion-targeted-by-india.html



Source: "2011 Index of Economic Freedom", Raw data download from <http://www.heritage.org/>

multi-disciplinary experts and top tax officials led by a retired Supreme Court Judge.

The SIT on black money sought details of all major cases of tax evasion and criminal financial fraud being probed by various investigative agencies which are mandated to keep a check on such instances. At present there are nine of these agencies - Department of Revenue (under the Ministry of Finance), Reserve Bank of India, Intelligence Bureau, Enforcement Directorate, Central Board of Investigation (CBI), Income Tax department, Narcotics Control Bureau, Directorate of Revenue Intelligence, Financial Intelligence Unit, Research and Analysis Wing and the Foreign Tax and Tax Research wing under the Central Board of Direct Taxes (CBDT).

In its first interim confidential report submitted to the Apex Court of India, it is reported that the SIT has suggested that over-invoicing of power equipment imports has been one of the modes of routing money abroad. Moreover, sources report that the following key suggestions have been included in the report:

- i. major overhaul of tax treaties with different countries.
The report says that countries like Mauritius can't have a one sided formula as far as information sharing is concerned.
- ii. the SIT report asks for new and stringent provisions to be included in the Money Laundering Act
- iii. Enforcement Directorate should have the power to attach properties being amassed abroad by Indian nationals if they are found guilty of hawala (a popular way of transferring wealth abroad).

Similarly many nodal agencies of the government (FICCI, ASSOCHAM) have given suggestions to the government as to how to tackle this issue. The important ones are listed below:

- opening a window for a voluntary disclosure scheme for people declaring assets in form of bank deposits, investment in shares /property etc
- providing Immunity under Direct & Indirect Tax Laws, Companies Act, Foreign Exchange Management Act including Money Laundering Act etc
- adopt a flat rate of 40% of tax on such disclosed income
- investing 10% of the assets in Infrastructure Bonds
- the funds so collected will be earmarked and used by the government only for development of infrastructure Projects.

Taking the discussion ahead, other tax reforms envisaged and recently announced by the Modi Government to simplify tax regime are detailed below.

Retrospective amendments to tax laws

There were a lot of expectations of the Modi Government regarding neutralisation of the retrospective amendments regarding indirect asset transfers introduced in 2012 to nullify the Apex Court decision in the Vodafone case. However, this has not happened.

But on a positive note, there has been a clear acknowledgment now that there will be no resort to

retrospective taxation in future. Finance minister Mr. Arun Jaitley, in his budget speech has clearly stated – “The government will not ordinarily bring any change retrospectively which creates a fresh liability.” He added that the BJP government is committed to providing a stable and predictable taxable regime which would be investor friendly and spur growth.

Mr. Jaitley also commented on the existing tax disputes, arising out of the 2012 retrospective amendment. He stated that the said disputes are at different levels of pendency in the courts and they will be allowed to reach their logical conclusions. So for matters already under litigation like the Vodafone case, the law will take its course. To review those matters not under litigation as of now, Mr. Jaitley has announced the formation of a high-level committee of the Central Board of Direct Taxes (CBDT).

Goods & Service Tax (GST)

GST is the one indirect tax reform that every businessman is eagerly looking forward to. The first deadline for the introduction of this was April 2010 but it is yet to see the day light. The biggest roadblock is the lack of consensus between Central Government and state governments.

As per its manifesto, the BJP government is committed to bringing all the State Governments on board in adopting GST and addressing their concerns. Further, with the BJP government in power at the centre as well as in a majority of states, implementation is expected to be sooner rather than later.



Policy reforms

Foreign Direct Investment (FDI) norms:

- changes pertaining to Defense are to go through; changes pertaining to Insurance will be easier to pass with a joint session of Parliament. The budget proposals indicate an increase in the composite FDI cap from 26% to 49% in the Defense and Insurance sectors, with full Indian management and control
- the reform for Foreign Direct Investment (FDI) in Defense is likely to go through
- however, for Insurance, the increase in FDI limit will require a constitutional amendment in the Insurance Bill. This will require approval in both the Houses of Parliament. Since the NDA government does not have the required numbers in the Upper House, a joint session of Parliament is more likely to result in safe passage of the Bill
- FDI norms were also eased based on built-up area and capital conditions in the construction development sector.

Cross-border debt funding to be taxed at a concessional rate of 5%

- interest on cross-border debt funding by way of: (i) external commercial borrowings, (ii) any foreign currency denominated long-term bonds, and (iii) business trusts is to be taxed at 5%.
- the window of concessional tax rate has been extended up to 30 June 2017.

Conclusion

Amid high expectations from all business quarters, the BJP government has set an ambitious target for itself. Within the first 100 days of coming to power, the Modi government has made the right noises in the right areas, got investor attention globally and improved the overall sentiment. The recent spate of news articles bears testimony to the fact:

- 5.7% Q1 growth has generated huge positive sentiment, says PM Modi – Economic Times – 1 September 2014
- Global CEOs, top bankers queue up to meet Modi – Hindustan Times – 1 September 2014

India today stands at the cusp of economic growth and it is well poised to take advantage of the excess global liquidity, lower inflationary expectations and stable commodity prices. The government should expedite assisting this process by simplifying tax laws and removing policy uncertainties to jump start the economy and this Modi Government is the one on which India Inc is relying to “walk the talk”.

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Mexico

Tax reform in effect 2014 - Mexican BEPS

An important tax reform took place in Mexico at the end of last year, which became effective in January 2014.

Aware of the everyday greater globalisation in the way of doing business, which involves various companies within one group, each in a different country and therefore subject to different tax treatments, this reform introduced provisions contemplating the OECD's base erosion and profit sharing initiative (BEPS), in order to limit abusive tax planning.

Tax treaty benefits (Art. 4, Income Tax Law)

Starting this year and in order to be able to apply the benefits of treaties to avoid double taxation, besides having to demonstrate residency in a foreign country, in cases of transactions between related parties, the Mexican tax authorities may request proof of the existence of juridical double taxation from the foreign resident.

As “proof”, the authorities will be requesting a statement under oath, signed by the legal representative, saying that the items of income subject to tax in Mexico and upon which the benefits of a treaty are intended to be applied, are also subject to tax in its country of residence. The statement must also quote the relevant legal provisions which would result in double taxation and the taxpayer should include all documental proof of taxes having been paid in the country of residence of the related party.

This provision has been criticized in the sense that it gives power to local tax authorities to impose an obligation on a non-resident of that country, while also, single-handedly, imposing conditions on the availability of benefits of what is a bilateral treaty.

Non deductible expenses (Art. 28 XXIX and XXXI, Income Tax Law)

Mexican tax authorities, in an early effort to adopt recommendations made by the OECD in its BEPS reports, incorporated in the Income Tax Law new assumptions under which several expenses will not be considered as allowable deductions for the payer.

Such is the case of payments which are deductible for the Mexican resident and also deductible for a related party, unless that related party includes that item in its gross income, for the same year or the following year.

In other words, for the expense to be treated as an allowable deduction for the Mexican taxpayer, the new law requires that within a maximum of two years, any effect of double deduction be “nullified” by that same item of deduction being also treated as taxable income by the related party. His provision is intended to prevent a double benefit or base erosion from a deduction by using conduit companies with preferential tax regimes. Nevertheless, the same provision allows for expenses to be rightfully deducted by two parties, as long as it doesn't result in a double benefit.



It is said to be aimed to avoid an abuse of the US benefit referred to as “check the box” which can be obtained by being share-holders of a Mexican Limited Liability Entity (S. de R.L.).

Moving on to more specific concepts, payments of interest, royalties and technical assistance, of which the recipient is a foreign entity that controls or is controlled by the payer, the expense is now considered non-deductible if either one of the following situations occur:

- the foreign entity that receives payment is considered transparent
 - an exemption is contemplated when the transaction takes place at market value and the shareholders or members of such entity are subject to income tax for that income
- entities qualify as transparent when they are not considered income tax taxpayers in the country in which they are incorporated or in which their main administration or effective headquarters are established, and their income is attributed to their members, partners, shareholders, or beneficiaries
- payment is considered non-existent for tax purposes of the country where the foreign entity is located
- the foreign entity does not consider such payment as income subject to tax under applicable tax provisions.

For the purposes of this provision, control is deemed to exist whenever one of the parties has effective control over the other or control over its administration, in such degree that it may decide upon the moment of allocation or distribution of income, profits or dividends of the other, either directly or through third parties. It is intended to limit entities agreeing to share profits while avoiding corresponding taxes.

Final comments

To avoid base erosion and profit shifting is a growing challenge and is on the agenda of tax authorities worldwide. Nevertheless, there is concern that the Mexican authorities have adopted these provisions and put them into effect too soon rather than waiting until international provisions had been agreed-on and implemented.

Time will show the actual effects obtained by this reform and it is probable that further provisions will be introduced to eliminate unintended side effects.

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Pakistan Paradise on Earth

Pakistan is a paradise on earth for investors - especially to foreign investors.

This is evident from the case of an acquisition of the largest knitwear exporter in Pakistan, Masood Textile Mills Limited, a listed company, by Shandong Ruyi Science & Technology Group Company China (‘Shandong Ruyi’) and further investments by Shandong Ruyi and other Chinese Companies in industrial parks, independent power producers (IPPs), etc. as part of USD32 billion worth of investments in Pakistan by China.

It also gives me great pleasure in stating that my firm, Riaz Ahmad & Company, Chartered Accountants, is playing an instrumental role in rendering a wide range of advisory and tax services to Chinese investors. Our Partner, Transaction Advisory Services worked day and night on convincing Shandong Ruyi and other Chinese investors to invest in Pakistan.

The main reasons for foreign investors’ interest in Pakistan are: 0% income tax rate for Independent Power Producers (IPPs); 27% to 29% guaranteed returns for investors in IPPs (a sovereign guarantee is issued to IPPs); 0% income tax (federal) on agricultural income; 0% income tax on any income received by a person from a corporate agriculture enterprise, distributed as dividend out of its income from agriculture; 0% income tax on exports of computer software or IT services or IT enabled services; hefty export rebates to exporters of value added textiles; subsidized mark-up rates on loans to export oriented sectors; exemptions from payment of income tax, sales tax and customs duty on import of goods meant for export by 100% exporters; cheap labour; cheap agro-based industry’s raw material; booming stock market and the list goes on. All the law and order problems in Pakistan are confined to specific places; hence, industry continues to thrive when managed and financed properly.

Corporate income tax rate in Pakistan is 33%. Minimum tax is 1% of turnover. However, in recent years, various incentives have been introduced in the Income Tax Ordinance, 2001 for investors. Through Finance Act, 2014 (effective from 1 July 2014) an incentive of a reduced corporate tax rate has been provided to companies setting up new industrial undertakings for a period of five years. The corporate tax rate shall be reduced to 20% of

taxable income for a company setting up industrial undertakings between 1 July 2014 to 30 June 2017, for a period of five years beginning from the month in which the industrial undertaking is set up or commercial production is commenced, whichever is later, if 50% of the cost of the project including working capital is through owner equity foreign direct investment.

Tax credit for newly established industrial undertakings

Where a taxpayer being a company formed for establishing and operating a new industrial undertaking including corporate dairy farming sets up a new industrial undertaking including a corporate dairy farm, it is given a tax credit equal to 100% of the tax payable, including on account of minimum tax and final taxes payable, on the taxable income arising from such industrial undertaking for a period of five years beginning from the date of setting up or commencement of commercial production, whichever is later.

A tax credit, as stated above, is admissible where:

- the company is incorporated and the industrial undertaking is set up between the 1 July 2011 and 30 June 2016
- the industrial undertaking is managed by a company formed for operating the said industrial undertaking and registered under the Companies Ordinance, 1984 and having its registered office in Pakistan
- the industrial undertaking is not established by the splitting up or reconstruction or reconstitution of an undertaking already in existence or by transfer of machinery or plant from an industrial undertaking established in Pakistan at any time before 1 July 2011; and
- the industrial undertaking is set up with 100% equity raised through issuance of new shares for cash consideration.

However, short term loans and finances obtained from banking companies or non-banking financial institutions for the purposes of meeting working capital requirements do not disqualify the taxpayer from claiming this tax credit.

Tax credit for enlistment

Where a taxpayer, being a company, opts for enlistment in any registered stock exchange in Pakistan, a tax credit equal to 15% of the tax payable is allowed for the tax year in which the said company is enlisted.

Tax credit for investment

Where a taxpayer being a company invests any amount in the purchase of plant and machinery, for the purposes of extension, expansion, balancing, modernisation and replacement of the plant and machinery already installed therein, in an industrial undertaking set up in Pakistan and owned by it, credit equal to ten per cent of the amount so invested is allowed against the tax payable, including on account of minimum tax and final income taxes payable.

However, the above tax credit will apply if the plant and machinery is purchased and installed at any time between 1 July 2010 and 30 June, 2015. It is very much expected that the 30 June 2015 deadline will be extended to

encourage investments.

Ease of doing business - A foreign investor can set-up its business in Pakistan in less than 15 calendar days. Registrations with the Securities and Exchange Commission of Pakistan (SECP) and Federal Board of Revenue (FBR) are swift. Foreign currency inflows are welcome without any restrictions. Dividends and unsecured foreign currency loans by Group companies can be repatriated back with ease. Agreements for avoidance of double taxation are there and have an overriding effect.

I quote the words of a top finance executive of the largest business house of Pakistan, Nishat Group, one of our firm's largest clients: "in Pakistan you can setup/run a business with Government's money". I hope you agree.

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Romania

Increase in tax incentives for investment

Law no. 571/2003 of the Fiscal Code has been amended and supplemented by the publication of Government Emergency Ordinance no. 19 dated 23 April 2014, in connection to the profit tax exemption for reinvested profits.

This Ordinance abolishes article 19² of Law no. 571/2003 of the Fiscal Code.

The provisions include:

- the profit tax exemption for profits invested in new technological equipment (machinery, tools and working plant), as included in subgroup 2.1 of the Catalogue regarding the classification and the useful life of fixed assets, provided that the equipment is used for business purposes, has been reintroduced
- the tax exempt invested profit is represented by the gross accounting profit cumulated as from the beginning of the year when the commissioning of the equipment was performed
- the tax incentive applies for the profit reinvested in technological equipment manufactured and/or acquired as of 1 July 2014 and commissioned by 31 December 2016 inclusively
- for investments in technological equipment manufactured and/or acquired and commissioned during the period 1 July – 31 December 2014, the incentive is applied by taking into consideration only the gross accounting profit recorded as of 1 July 2014
- taxpayers subject to microenterprise tax which become profit tax payers during the fiscal year benefit from this incentive for technological equipment commissioned as

- of the quarter in which they became profit tax payers, according to the law
- the amount of profit for which this incentive is applied should be distributed at the end of the financial year, primarily for the setting up of reserves, but not before setting up the legal reserve. The reserves become taxable upon their utilisation and in the event of restructuring operations, if not re-built at the beneficiary level
- the tax incentive is also granted for investments performed over a period of several consecutive years, based on partial work reports
- in order to benefit from this tax exemption, taxpayers have to keep the equipment in their patrimony for at least half of the useful life, but for no longer than five years. Otherwise, the profit tax is recalculated and additional tax liabilities assessed, with the taxpayer being required to submit a rectifying tax return. The following equipment does not fall under the above-mentioned provisions:
 - transferred during restructuring operations
 - alienated during bankruptcy/liquidation procedures
 - destroyed, lost or stolen, provided the taxpayer has enough documentary evidence
- equipment subject to this incentive cannot be depreciated by using the accelerated depreciation method.

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Singapore Tax haven or just misunderstood ?

Much of the world, especially the more advanced nations, is in the grip of a raging debate about whether countries are collecting their fair share of taxes. Amidst the many on-going probes into high net worth individuals and multinational corporations sheltering their wealth and profits in exotic locations, tiny Singapore too has not been spared the onslaught. Why is that so? For one thing, Singapore does admittedly offer a low headline tax rate at 17%, particularly in comparison with the rest of the region where corporate tax rates are closer to rates like 25% in China or 30% in the Philippines. Only Hong Kong at 16.5% offers a lower rate. The low rates are mirrored on the personal tax front as well, with Singapore's top marginal rate of 20% being the second-lowest in the region after Hong Kong's 17%.

But low tax rates are just part of the story. At the core of the Singapore tax system is a generous and wide ranging array of tax incentives that were designed decades ago to promote and sustain the high levels of economic growth that the city state has enjoyed for years. These tax incentives, while designed to encourage high value added activities ranging from shipping to fund management, have also created a more implicit "shadow" tax system that at times contributes to the perception that Singapore is luring international companies at the expense of their home countries. Even the more generic non-industry oriented tax exemptions such as

the Start-Up Tax Exemption Scheme and Partial Tax Exemption Scheme can by some standards be viewed as being quite generous. The other aspect that adds to this perception, while not necessarily tax related, is possibly the ease with which a company can be incorporated in Singapore. While this undoubtedly underscores the business friendly environment that Singapore promotes, it also sits uncomfortably with those who feel that this encourages companies and individuals intending to shelter their profits or ill-gotten gains to make a beeline for the city state.

That brings us to the pertinent question of whether Singapore is indeed a tax haven. At first glance, a number of observations may indeed support this thesis. The high concentration of millionaires (one in ten according to one study) and a continuous influx of high net worth individuals which seem to be growing year by year are indicative of the lure of Singapore to the rich and wealthy. It is now very much a playground for the super-rich with its casinos, luxury residential enclaves, marinas and super yachts. But that is not all – Singapore, being a key business hub in the region, attracts the biggest global multinational corporations to set up shop on the island and in doing so, has unwittingly found itself at the centre of some tax sheltering controversies. Apple, for instance, was reported by Reuters last year to have booked revenues in its Singapore subsidiary in excess of the \$10.7 billion that it recorded in the rest of the Asia-Pacific region. The Singapore subsidiary's post-tax profits of \$186 million with an effective tax rate of 6% drew scrutiny from a U.S. Senate report detailing how global companies structured their operations to book the majority of their foreign profits in low tax jurisdictions. Aside from this, it is also Singapore's central position in the wealth management and private banking sectors that marks it out. At the heart of it are the banking secrecy rules that Singapore has always had. This potentially could have been the factor that has contributed most to Singapore's possible reputation as a tax haven.

However, the undeniable fact is that Singapore is a small and open economy that is heavily reliant on foreign capital. Its headline tax rate of 17% is low, but not excessively so by international standards. Its tax incentive regime has been crafted judiciously and is targeted specifically at companies in industries that Singapore wants to attract from shipping and commodity trading to fund management and biotechnology. It is a key business hub in the region requiring extensive treasury, cash management and other financial services which in turn require robust banking rules and regulations. All of this provides substantive counter-arguments against the notion that Singapore is a tax haven. Added to this is the fact that Singapore has signed an extensive network of double taxation treaties which is not typical of tax haven jurisdictions. It has also since 2008 voluntarily signed a number of information exchange agreements with various tax authorities ranging from Japan to Australia and Britain and allowed its tax authorities to obtain bank and trust information from financial institutions without having to seek a court order. While it is not a member of the OECD, Singapore has demonstrated in no uncertain terms its support for the Base Erosion and Profit Shifting Report published in July 2013. To cap things off,

Singapore has also concluded discussions on an Inter-Governmental Agreement with the United States to better enable financial institutions in Singapore to comply with the Foreign Account Tax Compliance Act, a US law requiring all financial institutions outside the US to report on accounts held by US persons.

The jury may still be out in certain quarters as to whether Singapore is a tax haven but taken together, these measures collectively make it an outlier by almost any criteria that a tax haven is defined by. As the tax competition heats up, Singapore can ill afford to sit on its laurels with global policymakers casting an ever watchful eye on those who continue to eagerly join this race to the bottom.

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Spain Spanish tax reform

The Spanish Government has approved on 31 July 2014 the Tax Reform. The changes relate mainly to personal income tax (PIT), non-residents income tax (NRIT) and company income tax (CIT); and the reform also includes measures to enhance tax compliance (like the publication of the list of tax defaulters and the strengthening of the tax audit process). The reform is expected to be passed by the Parliament within a few months.

Personal Income Tax (PIT)

Amendments to PIT Law will enter into force on 1 January 2015:

- starting in 2015, and being fully implemented in 2016, the number of tax brackets is reduced from seven to five,



all marginal income tax rates are reduced. Highest rate (57%) is also reduced (see Table 1 below)

- a new tax benefit is introduced for families with members with disability and other special social circumstances
- currently income from severance payments as defined by Labour Law is tax exempt. Exempt income from severance payments will be capped at EUR180,000. Payments in excess of this amount will be taxed on the excess with the possibility of a reduction of 30% of the taxed amount
- exemption on the first EUR1,500 of dividends disappears
- currently, only capital gains from the transfer of any asset with a period of generation of at least one year are taxed at the savings tax rate (up to a maximum tax rate of 27%). Upon tax reform, all capital gains from the transfer of

Taxable income <i>Up to EUR</i>		Tax due <i>EUR</i>	Remaining taxable income <i>Up to EUR</i>	Marginal tax rate % (*)
2015	0.00	0.00	12,450.00	20.00
	12,450.00	2,490.00	7,750.00	25.00
	20,200.00	4,427.50	13,800.00	31.00
	34,000.00	8,705.50	26,000.00	39.00
	60,000.00	18,845.50	Onwards	47.00
2016	0.00	0.00	12,450.00	19.00
	12,450.00	2,365.00	7,750.00	24.00
	20,200.00	4,225.50	15,000.00	30.00
	35,200.00	8,725.50	24,800.00	37.00
	60,000.00	17,901.50	Onwards	45.00

Table 1

(*) Please note that marginal rates may vary depending on the Autonomous Region of residence.

Taxable income <i>Up to EUR</i>		Tax due <i>EUR</i>	Remaining taxable income <i>Up to EUR</i>	State marginal tax rate % (*)
2015	0.00	0.00	6,000.00	20.00
	6,000.00	1,200.00	44,000.00	22.00
	50,000.00	10,800.00	Onwards	24.00
2016	0.00	0.00	6,000.00	19.00
	6,000.00	1,140.00	44,00.00	21.00
	50,000.00	10,380.00	Onwards	23.00

Table 2

assets will be subject to the savings tax rate, irrespective of its period of generation

- the tax rate on savings (interest, dividends, capital gains) is reduced from the current maximum rate of 27% as shown in Table 2
- the taxation of Stock Options Plans and Free Stock Plans is substantially changed:
Currently, a yearly EUR12,000 allowance on stock options and free stocks granted does exist in certain circumstances. Upon tax reform, such an allowance will disappear
- the reduction for income generated over two years or obtained on a non-regular basis is reduced from 40% to 30%
- currently the distribution of a share premium up to the acquisition cost of the participation is tax free. Upon the reform, the distribution of a share premium by non listed entities will be taxed as a dividend
- capital gains obtained by individuals older than 65 years will be exempt if the total consideration received in the transaction concerned (up to EUR240,000) is reinvested into pension annuities. (Currently an exemption only exists on gains from the transfer of dwellings.)
- from 1 January 2015, pension plans, assured savings plans, company savings plans and insurance contracts with mutual insurance companies would be redeemable after a 10-year period elapses from the date the contributions were made
- the minimum term for an individual systematic savings plan is reduced from five to ten years
- CFC rules are reinforced:
CFC rules will not be applicable to tainted income obtained by an EU resident entity only if the taxpayer proves that incorporation and operation of the EU resident entity has a valid economic reason, and the EU resident entity performs a business activity
- exit tax: unrealised capital gains on relevant entities will be subject to taxation if the taxpayer changes his tax residence and any of the following requirements are met:
 - market value of the portfolio is higher than EUR 4,000,000, or the participation held in the subsidiary is at least 25% and its market value exceeds EUR1,000,000.

Special taxation deferral rules are applicable if:

- the change of residence is due to a labour assignment to a country not included in the tax haven blacklist.
- the new country of residence is an EU member and an effective exchange of tax information exists.

- these taxation deferral rules may lead to non-taxation if the portfolio is not sold

- inward expatriates regime:
currently this regime could not be applied if foreseen yearly labour income exceeded EUR600,000. Such a limitation disappears, but the beneficial tax rate will not apply to income exceeding this amount: Accordingly only Spanish source income will be taxed, at the following tax rates in Table 3 (current tax rate is 24.75%):

Taxable income <i>EUR</i>		Marginal tax rate %
2015	6,000.00	24.00
	600,001 and onwards	47.00
2016	6,000.00	24.00
	600,001 and onwards	45.00

Table 3

Non residents income tax

Amendments to the NRIT Law will enter into force on 1 January 2015:

- deductible expenses for either non-resident individuals or entities without a PE will be defined by the PIT Law and the CIT Law respectively
- NRIT individual taxpayers resident in another EU member state may be taxed according to PIT rules. This measure is focused to enable low income taxpayers to benefit from PIT allowances
- NRIT rates will be reduced:
taxpayers without a PE, from 24.75% to 24%;
taxpayers resident in another EU member state from 24.75% to 19%. PEs will be taxed at the same CIT rates applicable to resident entities (the general tax rate will be 25%)
- currently the distribution of a share premium up to the acquisition cost of the participation is tax free. Upon the reform, the distribution of share premium by non quoted entities will be taxed as a dividend at a 21% rate
- anti-abuse clauses related to EU parent-subsidiary dividends and EU associated companies royalties are reinforced
- following the new definition of article 7 of the OECD Model Tax Convention, if contained in the relevant Treaty, whenever deemed expenses of internal operations within the headquarters or within any of its foreign PEs are attributed to a Spanish PE, the following rules will be

applicable:

- royalties, interest or commissions paid by the Spanish PE either to headquarters or foreign PEs in exchange of technical assistance services or the use of rights and goods will be considered non-deductible. This is not applicable to interest paid by a PE of a foreign bank derived from its activity
- deemed income allocated to either headquarters or foreign PEs will be taxed in Spain according to rules applicable to income not obtained through a PE.

Corporate income tax

The new CIT Law is expected to enter into force on 1 January 2016. Nevertheless some measures will be applicable in 2015:

- tax rate
The general tax rate will be reduced from 30% to 28% in 2015 and to 25% on 2016.
Banking entities will continue to be taxed at 30%.
New entities will be taxed at 15% in the first FY of obtaining profits and the following FY
- the intra-group financing tax regime will be the same as for participative loans (hybrid financing)
- Gifts to clients will be deductible only up to 1% of entity turnover
- deductibility of financial expenses:
a new limitation is introduced on interest derived from the acquisition of a participation in an entity if the subsidiary is further included into a tax group or suffers a restructuring operation.
- losses carry forward:
offsetting of carry forward losses will be subject to no time limitation (current limitation is 18 years).
Nevertheless the amount to be offset will be limited to 60% of taxable income before the reduction of the tax base resulting from the application of the proposed new special tax-free reserve with a minimum amount of EUR 1,000,000. Stronger measures to avoid offsetting losses of dormant companies are introduced.
Carry forward losses or tax credit amounts will not benefit from the statute of limitations. Tax authorities will be able to review these even if the statute of limitations (four years) has elapsed
- double taxation relief for participation in both resident and no-resident entities will be the same
- participation exemption
A participation exemption will be applicable to both qualifying resident and non-resident subsidiaries (QFS).
The participation exemption for a non-resident QFS will require the non-resident QFS to be subject to foreign corporate taxation at a minimum 10% nominal rate.
If such requirement is not met the following rules will be applicable:
 - income derived from non-distributed reserves corresponding to FYs in which the minimum taxation rule was met will be exempt.
 - income derived from profits other than non-distributed reserves will be understood to have being obtained on a linear basis. Income allocated proportionally to FYs in which the minimum taxation rule was met will be exempt

- transfer pricing
Simplified documentation obligations are introduced for entities or a group of entities whose turnover is below EUR45,000,000
The hierarchy on valuation methods (CUP, C+, RMM, GMM and TNMM) disappears and new valuation methods are secondarily permitted provided free competition is respected.
The penalties regime is softened
- tax credits
The tax credit for reinvestment of profits disappears and is replaced by a capitalization reserve (amounts applied to the reserve will not be subject to taxation irrespective of whether they are reinvested)
- R&D
Companies allocating more than 10% of their revenues to R&D activities will be allowed to monetize the R&D tax credit up to EUR5 million, when the option for the monetisation of the credit is applicable
- special regimes
Tax groups
Indirect participated resident subsidiaries owned through non resident companies will qualify for the tax consolidation regime.
Tax neutral restructuring regime
It will not be an optional regime but the general one applicable to such operations.
Goodwill arising from a merger will no longer be deductible.
SME tax regime
SMEs may carry back five FYs future losses against current profits. If no losses are generated in the 5 FYs period the reserve created will be taxed at the end of such a period (taxation is deferred five years).
- SOCIMs (Spanish REITs)
No withholding will be practised on dividends distributed by SOCIMs to a resident entity.
Capital gains on disposal of SOCIMs' shares obtained by non-resident shareholders will not be subject to taxation provided their participation does not exceed 5%.

Assessment

Tax experts share the view that the tax reform is electorally motivated and it does not transform the Spanish fiscal system either in the direction or in the depth that it is most needed.

Despite the fact that back in March 2014 the ad-hoc Government-nominated Panel of Tax Experts submitted its report on tax reform the Government has now failed to include the main recommendations proposed.

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Switzerland Overview of tax changes in 2014

The tax landscape is subject to constant change. We are pleased to provide the following tax-relevant information regarding changes in legislation for the tax period 2013 and already in effect as at 1 January 2014, as well as additional interesting tax aspects.

Public access to tax registers

Any taxpayer may have access to his/her own tax records within certain time constraints and under certain substantive preconditions (eg presenting a final tax assessment).

However, some cantons provide information regarding tax factors to third parties as well. The disclosure of such information to third parties is governed at the cantonal level. For instance, the tax laws of Canton Berne stipulate that the tax register is publicly accessible. In Canton Zurich, information regarding tax factors can be obtained by third parties for a fee.

Taxpayers who object to third-party access to their tax files should contact the relevant tax authority and block access to their own records by third parties, which may incur some costs.

Household goods or taxable assets?

This differentiation appears to be quite simple at first glance. However, closer consideration of this question reveals the finer points.

Based on a court ruling by Canton Zurich, a picture that significantly increases in value over the years can suddenly be regarded as a taxable asset. The precise dividing line between non-taxable household goods and taxable assets must be assessed on an individual case-by-case basis. The grounds for acquisition, intended purpose and utilisation are non-relevant for making such an assessment.

When objects such as jewellery or paintings are insured separately, the articles may no longer be regarded as normal household furnishings and considered as taxable assets, according to court opinion.

In view of this tightening interpretation of taxable assets, taxpayers are advised to review their objects of value as to whether the relevant declaration has been properly submitted to date.

Commuter deduction from 2016

In connection with the “FABI” (Financing and Upgrading Switzerland’s Rail Infrastructure) bill, the Swiss Parliament has decided to limit the so-called commuter deduction from federal direct tax to CHF3,000. The commuter deduction is not part of the FABI bill. According to the Parliament, however, the limit will only come into force if FABI passes. The law that governs the commuter deduction will not be publicly disclosed until after the FABI vote.

Analyses of various tax administrations have revealed that limiting the commuter deduction in the cantons affects an average of between 20% and 25% of taxpayers, especially long-distance commuters that travel by car and holders of first-class general rail passes, in particular.

The federal government is banking on additional annual revenues of roughly CHF200 million through this measure. Cantons should still retain the decision-making ability for how they want to structure the commuting cost deduction.

Limited tax amnesty

The “limited tax amnesty” came into force on 1 January 2010. Persons subject to tax are therefore granted the possibility of subsequently declaring any previously undisclosed assets and income, in the form of voluntary self-disclosure and without the consequences of penalty tax.

The prerequisites for non-punitive voluntary self-disclosure are as follows:

- persons subject to tax must file a voluntary disclosure
- the amnesty applies to the first instance of self-disclosure of tax evasion
- the tax evasion has not been reported to any tax authorities
- tax authorities are to be provided with unconditional support in determining the amount of back taxes
- persons subject to tax must seriously endeavour to effect payment of the back taxes due.

Many more persons have taken advantage of the amnesty offer to date than the tax authorities had anticipated.

Maximum contributions to pillar 3a as well as additional social insurance

The following maximum pension contributions may be deducted in 2014:

With contributions to pillar 2	CHF 6,739
Without contributions to pillar 2	CHF 33,696

You will find details regarding additional social insurance information on our homepage at www.abt.ch.

Value-added tax (VAT) and use for private purposes

Changes in practice regarding leasing of residential property went into effect starting from 1 January 2014. Utilisation for private purposes has been limited. The new definition in this context is restricted to use for purposes of residency: ie only utilisation of the property as residence and for weekly stays qualifies as exempt from taxes. Consequently, the possibilities of opting for services that are exempt from taxes have been extended.

Renting of holiday apartments constitutes accommodation services subject to a special tax rate and not tax-exempt leasing, since the property is not used for purposes of residency.

New value-added tax numbers from 1 January 2014

All Swiss enterprises have been assigned a so-called Business Identification Number (BIN) in recent years, comprising three letters and nine digits. Only the new VAT number is valid for VAT-compliant documentation starting from 1 January 2014, which consists of the company's BIN number as well as supplemental VAT, TVA or IVA. The multi-year transition deadline from the old six-digit number to the new BIN number is definitively expired.

The VAT numbers are structured as follows:

CHE-123.456.789 MWST

CHE-123.456.789 TVA

CHE-123.456.789 IVA

The following VAT number is invalid: CHE-123.456.789 VAT.

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USA

Report of Foreign Bank and Financial Accounts (FBAR): US persons investing overseas - are you required to file?

With an increase in globalisation, more and more U.S. individuals are investing in and holding accounts overseas. Foreign account owners need to be aware of the various U.S. reporting requirements that come with having accounts abroad, specifically the requirement to file the Report of Foreign Bank and Financial Accounts (FBAR).

Under the Bank Secrecy Act, U.S. persons who have a financial interest in or signature authority over financial accounts in a foreign country with an aggregate value exceeding \$10,000 at any time during the calendar year

must electronically file the FBAR Form 114 (formerly TD F 90-22.1) on the Financial Crimes Enforcement Network (FinCEN). Filing of the form is required even if the account generated zero taxable income and/or if the account was opened or closed during the calendar year.

See: <http://www.fincen.gov/forms/files/FBAR%20Line%20Item%20Filing%20Instructions.pdf>.

For purposes of FBAR reporting, a U.S. person is generally defined as a U.S. citizen, U.S. resident, entities created or organized in the United States (corporations, partnerships, or LLCs), or trusts or estates formed under the laws of the United States.

See: <http://www.fincen.gov/forms/files/FBAR%20Line%20Item%20Filing%20Instructions.pdf>.

Financial accounts include, but are not limited to, bank and securities accounts, insurance and annuity accounts with cash value, commodity futures and options accounts, and mutual fund accounts. Accounts of a foreign financial institution held at a U.S. branch are also reportable on the FBAR form. Financial accounts of a U.S. financial institution held at a foreign branch are not reportable. See: <http://www.fincen.gov/forms/files/FBAR%20Line%20Item%20Filing%20Instructions.pdf>.

Generally, a U.S. person has a financial interest in a foreign financial account if he/she is "the owner of record or holder of legal title of the account, regardless of whether the account is maintained for the benefit of the U.S. person or for the benefit of another person." The owner of record or holder of legal title can also be an "agent, nominee, attorney, or a person acting in some other capacity on behalf of the U.S. person with respect to the account." If a U.S. person owns more than 50% in another entity, including a trust, he or she is deemed to have a "financial interest" in that entity's bank accounts. In this regard, a U.S. parent company needs to consider whether it has an FBAR filing requirement with respect to any accounts owned by its foreign subsidiaries. See: <http://www.fincen.gov/forms/files/FBAR%20Line%20Item%20Filing%20Instructions.pdf>.

An individual has signature authority if he or she has the power (exclusively or in conjunction with other individuals) to "control the disposition of assets in a financial account by direct communication with the person maintaining the account." If an account has two or more cosigners, each cosigner is deemed to have signature authority over the account. See <http://www.fincen.gov/forms/files/FBAR%20Line%20Item%20Filing%20Instructions.pdf>.

The FBAR report must be filed on or before June 30th of the year following the calendar year being reported. Effective 1 July 2013, the FBAR forms, including delinquent FBARs, must have been filed electronically through FinCEN's BSA E-Filing System. It is not filed with the Federal income tax return; hence, a filing extension granted by the IRS for the Federal income tax return does not extend the time to file the FBAR. There are no provisions to request an extension for the FBAR. See: <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Report-of-Foreign-Bank-and-Financial-Accounts-FBAR>.

The existence of foreign accounts also needs to be disclosed on Schedule B, Part III of the individual's U.S. Federal income tax return, whether or not there was an FBAR filing requirement. Spouses can file joint FBAR returns if all accounts are owned jointly and the FBAR report is filed timely on Form 114. Delinquent FBARs must be filed separately for each spouse even if all accounts were owned jointly. See: <http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Report-of-Foreign-Bank-and-Financial-Accounts-FBAR>.

The penalty for a willful violation of the FBAR requirements is equal to the greater of (a) USD100,000 or (b) 50% of the balance in the account at the time of each violation. The penalty for a non-willful violation is USD10,000. Penalties can be avoided if the violation was due to reasonable cause and the income from the account(s) was properly reported on the relevant tax return(s). The taxpayer can follow the "Delinquent FBAR Submission Procedures" for submitting delinquent FBARs. This is only relevant if the taxpayer is not under investigation by the IRS, has no unreported income, and has not been contacted by the IRS about delinquent FBARs. Taxpayers, if eligible, also have an option to go through the Offshore Voluntary Disclosure Program (OVDP) or the Streamlined Filing Compliance Procedures to file delinquent FBARs and amended Federal income tax returns. In addition, they would report and pay any additional tax and penalties, which are lower when going through the two programs. The IRS does not consider a "quiet disclosure" where the taxpayer merely amends returns to be an appropriate form of remediation. See: <http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Report-of-Foreign-Bank-and-Financial-Accounts-FBAR>.

U.S. Taxpayers that hold foreign financial accounts may also be required to file Form 8938 Statement of Specified Foreign Financial Assets, which is filed with the Federal income tax return. Form 8938 must be filed if the total value of assets held was USD50,000 on the last day of the tax year or USD75,000 at any time during the tax year (higher threshold amounts apply to married individuals filing jointly and individuals living abroad). The IRS provides a chart that compares Form 8938 and the FBAR filing requirements – it is a great tool to use to determine whether there is a filing requirement for either form. See: <http://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements>.

According to an IRS report, as of June 2014, more than 45,000 disclosures have emerged from the offshore programs, bringing in revenues of over USD6.5 billion from taxes and penalties. The IRS clearly has an incentive to go after U.S. persons with offshore accounts, and it appears that they will keep conducting audits and investigations. For how long? We don't know. Since taxpayers are at risk for civil penalties and even criminal charges, it is important that they reexamine the tax requirements related to FBAR filings. If you are unsure of whether or not you need to file an FBAR, you should consult with a tax accountant and/or a tax attorney who has experience with FBARs.

* Information was compiled from the FinCEN website, various IRS websites, BNA Portfolio 947 and filing instructions.

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USA

A practical approach to compliance with the foreign account tax compliance for non-financial companies

The Foreign Account Tax Compliance Act (FATCA) was enacted in 2010 by the U.S. Congress to combat tax evasion by U.S. taxpayers using foreign accounts. FATCA requires foreign financial institutions (FFIs) to enter into disclosure compliance agreements with the IRS which include the performance of due diligence to discover and report financial accounts held by U.S. taxpayers, or by foreign entities in which U.S. taxpayers hold a substantial ownership interest, as well as to withhold on payments to accounts of persons who refuse to provide the requested information. FATCA enforces this requirement by imposing a 30% withholding on certain payments, such as U.S. source dividends, interest, rents, royalties, proceeds from sale of property that generates interest or dividends, etc ("withholdable payments"), made to noncompliant FFIs.

Pursuant to FATCA, the IRS has released detailed regulations on the due diligence, reporting, and withholding obligations of persons or entities making and/or receiving withholdable payments. Additionally, 42 countries have entered into intergovernmental agreements (IGAs) with the U.S. as of 6 September 2014. Under the IGA framework, many FFIs may report to their local tax authorities who will share the information with the IRS.

The IRS announced in Notice 2014-33 that 2014 and 2015 will be considered transition years for IRS enforcement of due diligence, reporting, and withholding requirements under FATCA. During the transition period, the IRS will consider the extent to which an entity has made a good faith effort to comply with FATCA requirements. Entities which make a good faith effort to comply will be afforded transition relief from mandatory withholding during this period.

Although much of the focus and press coverage of FATCA has related to its impact on financial institutions, it will also have implications for non-financial companies that make and/or receive withholdable payments.

The following outline represents a proposed practical FATCA compliance implementation plan for non-financial multi-national groups that if undertaken should evidence their good faith effort to comply with the regulations.

Step 1: Identify and Register Foreign Financial Institutions within the Group

Companies should review the functions and financial information of non-U.S. group entities and identify any entities that may be considered foreign financial institutions (FFIs) under the regulations or a relevant inter-governmental agreement (IGA). Entities which are identified as FFIs must be registered with the IRS. Entities which are determined not to be FFIs must have their FATCA status documented.

Step 2: Identify and classify all Entities within the Group for FATCA Purposes

Next, companies should identify the appropriate FATCA classifications of all group entities based on a review of the functions and financial information of each entity.

Step 3: Complete Forms W-8BEN-E, W-8IMY, and W-9 for all Group Entities

Based on the FATCA classifications determined in steps 1 and 2, companies should complete updated W-8BEN-E, W-8IMY, and W-9 forms for each group entity. These forms should be kept on file and supplied to payers of US-source income. It should be noted that there is a transition period until 31 December 2014 for obtaining the new series of W-8 forms from payees who may have previously provided "old W-8" forms to payers.

Step 4: Identify all Withholdable Payments made by group entities

Concurrent with the classification of group entities for FATCA purposes, companies should conduct a review with their accounts payable department to identify all potential withholdable payments.

Step 5: Document FATCA status of all payment recipients
Companies should review the documentation of FATCA status provided by recipients of withholdable payments identified in step 4. Companies should update all missing, expired, or incomplete documentation.

Step 6: Identify all withholdable payments received by group entities

Companies should review payments received with their accounts receivable department to identify all withholdable payments. Companies should then review the documentation provided to payers of such withholdable payments and provide updated documentation as required.

Step 7: Document FATCA Compliance Process and Procedures

Finally, companies should keep record of the FATCA implementation plan conducted and procedures undertaken to ensure FATCA compliance on an ongoing basis.

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Notes



Notes



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