Morison KSi

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Global Tax Insights

Editorial

Sachin Vasudeva, Partner, S.C. Vasudeva & Co., India

The first Morison KSi international conference was held 10–13 November 2016 in Bangkok, a city known for its ornate shrines and vibrant street life, and was attended by over 150 delegates from across the world. On the final day, the tax group met to share the latest developments in their respective jurisdictions and examples of how clients have benefited from their advice.

On the international tax front, over 100 nations have recently concluded negotiations on a multilateral instrument that will swiftly implement a series of tax treaty measures in the area of base erosion and profit shifting (BEPS). The multilateral instrument has been developed under Action 15 of the Organisation for Economic Co-operation and Development (OECD)'s BEPS project and will transpose BEPS recommendations into over 2,000 tax treaties worldwide. The OECD's aim is to enable implementation of minimum standards to counter treaty abuse and to improve dispute resolution mechanisms while providing flexibility to accommodate specific tax treaty policies.

The long-awaited tax reform in indirect taxes in India inches closer to reality. The Indian Parliament approved the amendment to the Constitution paving the way for an Integrated Goods & Services Tax to replace the existing Value Added Tax on goods and Service Tax on services. Under the proposed law, there would be a four-tier tax structure. The rates approved by the GST council are 5%, 12%, 18% and 28%.

This edition includes two international tax cases: one from Israel, which deals with a very interesting concept of taxation of scholarships; the other from India, dealing with the interpretation of the India–UAE tax treaty.

I express my gratitude to all member firms that have contributed to this edition of the newsletter. I sincerely hope that the contents are useful to members and their clients. Feedback and suggestions are always welcome. You may email your suggestions to sachin@scvasudeva.com.

Wishing all readers a blessed 2017!

Sachin Vasudeva

Country Focus

Australia

Contributed by Andrew Lam,
Tax Director, Hill Rogers

E: andrew.lam@hillrogers.com.au

Australian GST changes to cross-border supplies

The Australian Government has recently enacted the Tax and Superannuation Laws Amendment (2016 Measures No. 1) Act 2016 ('the Act').

Broadly, the Act removes certain cross-border business-to-business (B2B) transactions from the goods and services tax (GST) net, from 1 October 2016. This will relieve non-resident suppliers from the obligation to account for GST on certain supplies.

These changes will generally simplify the GST treatment of B2B cross-border transactions. These measures broadly exclude supplies of goods or real property and effectively apply to supply of services and intangibles.

The changes provide certainty of GST treatment to cross-border transactions. Businesses involved in Australian cross-border trade should review their transactions to determine their correct GST treatment. Below is only a broad high-level outline of the changes.

What do these changes mean?

New PE rules for GST purposes

Supplies made by non-residents through a permanent establishment in the indirect tax zone (ITZ) will continue to be caught in the GST net. Broadly, ITZ means all land territories of Australia and the coastal seas but excluding external territories. The test of when an enterprise is carried in in the ITZ will be more closely aligned with Australia's modern treaty practice in relation to permanent establishments (PEs).

Under the new rules, generally a non-resident's enterprise will need to be based in Australia for more than 183 days in a 12-month period, and have a GST turnover of at least Au$75,000, to be required to register for GST. This could result in some entities being able to cancel their GST registration.

No GST on Australian businesses making supplies offshore

Under the previous rules, certain GST-free supplies made to non-residents lose their GST-free status because the supply is provided to another entity in the ITZ.

Under the new rules, supplies made in these scenarios will be GST free provided the recipient in the ITZ is a GST-registered entity and the supply is not of a private or domestic nature. The new rules remove the burden of overseas businesses having to register for GST for the purpose of claiming input tax credits.

An example of a supply that may now be GST free is when an Australian business makes a supply of training services to an overseas company, but provides those services to one of the company's employees in Australia.

Supplies of warranty services to non-residents but provided to Australian warranty holders to be GST free

A non-resident supplier of goods to Australian consumers may engage an Australian repairer to provide the repair services under the non-resident's warranty obligations.

Under the old rules, the local repairer must charge GST on the supply of repair services and on any goods used in the repairs even though the local repairer charges the non-resident supplier.

Under the new rules, the supply of repair services to a non-resident in relation to warranty obligation on goods will be GST free.

Easier calculation methodology for imported goods

GST-registered importers can calculate the value of taxable importation for GST purposes without identifying the exact amount paid for:

- International transport
- Insurance
- Loading or handling
- Service costs for the transport.

Instead, the importer may now opt to use an uplift factor (currently 10%) of the customs value of the imported goods. This will ease administration.

Supplies of goods installed or assembled in Australia

Under the old rules, a supply of goods into the ITZ is connected with the ITZ if the supplier either imports the goods into the ITZ or installs or assembles the goods in the ITZ.

Under the new rules, a supply of goods into the ITZ is only connected with the ITZ if the supplier imports the goods. If the supply of the goods that are brought into the ITZ involves the supplier installing or assembling the goods in the ITZ, the part of the supply that involves the installation or assembly of the goods is treated as a separate supply and an apportionment may be necessary.

Relief for non-resident entities making inbound B2B supplies to Australia

Under the previous rules, supplies made by non-resident entities are subject to GST if the supply is done in the ITZ or the supply is made through an enterprise carried on in the ITZ.

Under the new provisions, the 'connected with the ITZ' rules have a much more limited application where the recipient of the supply is a GST-registered business. Generally, this means that a larger range of supplies will be caught by the compulsory reverse charge provisions.

What other GST changes are there?

Separately, the Act also contains measures to extend the GST net to business to consumer (B2C) transactions involving the supply of intangibles, such as digital products, from 1 July 2017.

Accordingly, supplies of digital products, such as streaming or downloading of movies, music, apps, games and e-books, as well as other services such as consultancy and professional services, receive similar GST treatment whether they are supplied by a local or foreign supplier.

These types of supplies have largely escaped GST under the previous law.

Under these new rules, overseas suppliers will need to register and charge GST if they meet the Au$75,000 turnover threshold (Au$150,000 for non-profit entities).

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Country Focus

Germany

Contributed by Dr Christoph Schneider, Morison Frankfurt GmbH

E: cschneider@wubwp.de

Federal Fiscal Court doubts RETT intra-group exemption to comply with EU Law requirements on state aids

The European Union (EU)'s restrictions on state aids pursuant to Articles 107 and 108 of the Treaty on the Functioning of the European Union (TFEU) have recently gained considerable significance. The European Commission (EC)'s decision of 30 August 2016, forcing Apple to repay €13 billion arising from illegal tax benefits in Ireland, is just the latest example of its strict application of the state aid limitations.

The EU's state aid regime focuses on provisions in national tax acts. In this regard, the EC found that Section 8c, para. 1a of the German Corporation Income Tax Act *(Körperschaftsteuergesetz)* – the 'restructuring clause' *(Sanierungsklausel)*, which mitigates the limitations on offsetting of losses for restructuring purposes – would not be compatible with the internal market.

Recently, the Federal Fiscal Court (FFC) raised the issue of whether Section 6a of the German Real Estate Transfer Tax (RETT) Act *(Grunderwerbsteuergesetz)* could constitute an inadmissible subsidy within the meaning of Article 107 of the TFEU (see Court Order from 25 November 2015, file no. II R 62/14). The German Ministry of Finance has now been invited to provide its view on that question.

German RETT is very likely to turn out to be a (share/asset) deal breaker: even if RETT rates are relatively low (ranging from 3.5% to 6.5% among the German countries), its assessment basis can climb to seven-digit amounts. Therefore, tax exemptions are very important for taxation for RETT purposes. Section 6a of the RETT Act allows RETT-neutral intra-group restructurings under certain conditions. According to this exemption, the transfer of real estate – as well as the means to circumvent such a transfer, e.g. by selling shares in the PropCos instead – are exempt from RETT if they form part of a restructuring process within the meaning of Section 1, para. 1, nos. 1–3 of the German Reorganization Act *(Umwandlungsgesetz)*. Such restructurings include mergers, demergers, spinoffs, hive-downs, and so on.

Section 6a of the RETT Act could qualify as inadmissible state aid within the meaning of Article 107 of the TFEU if this provision distorts or threatens to distort competition between the member states. The regular proceedings to determine whether the criteria for incompatibility with the internal market are fulfilled are normally initiated by the member state itself that plans to establish a subsidy. In accordance with Article 108, para. 3 of the TFEU, the member state must inform the EC in sufficient time of any plans to grant or alter aid, to enable it to submit its comments. If it considers any such plan to be incompatible with the internal market according to Article 107, it is obliged to initiate the procedure provided for in Article 108, para. 2 of the TFEU.

If the member state has failed to notify its state aid before the latter is granted for the first time, this subsidy will be considered as formally illegal. Under the condition that it is not compatible with the internal market, the EC will treat this state aid as materially illegal. Only subsidies being materially illegal cause the EC to require the respective member state to recover the granted state aid from its beneficiaries.

This reclaim can have serious consequences for the beneficiaries. They must pay interest on the granted amount and repay the subsidy, even if the limitation period according to national tax law has already passed or the state aid notice has become final. German authorities must enforce this reclaim, even if a confirmative advanced ruling *(verbindliche Auskunft)* by the competent tax authority has been issued to the beneficiary in question.

Therefore, we advise the beneficiaries of the RETT intra-group exemption pursuant to Section 6a of the RETT Act to carefully analyse whether the requirements of Article 107 of the TFEU might have been fulfilled. In this respect, the EC's guidance on the question of whether public spending falls within and outside the scope of EU state aid control, published on 19 May 2016, could be helpful. If necessary, the respective beneficiary could create accruals *(Rückstellungen)* in order to be hedged against the recovery case.

Country Focus

Germany

Contributed by Carsten Deecke, Auditor/Tax Advisor, Partner, Dr Florian Gehrke, Lawyer/ Expert Lawyer for Commercial and Corporate Law, Partner and Dr Simone Wick, Tax Advisor, Dierkes Partner

E: cdeecke@dierkes-partner.de,

E: fgehrke@dierkes-partner.de

E: swick@dierkes-partner.de

Carsten Deecke

Dr Florian Gehrke

Dr Simone Wick

Risks of Brexit from a continental European – especially German – perspective

One of the most hotly discussed topics over the past few months has been 'Brexit'. Numerous articles, comments and recommendations have already been published, despite the remarkable fact that so far nothing has changed: the UK is still a member of the EU! All regulations, rules, agreements, etc. remain unchanged and are still valid. So far, the issues of when Great Britain will leave the EU, and how the EU and its members will proceed to cooperate with the UK, remain ambiguous. However, recent developments in UK politics and statements from Prime Minister Theresa May suggest that the withdrawal is gaining momentum, with leading national newspapers reporting that the UK government plans to trigger Article 50 of the Lisbon Treaty, thus executing Brexit, by the end of March 2017. In addition, unsettled by increasingly radical views expressed in support of a 'hard BREXIT', economic operators are now starting to leave the UK. Russia's VTB Bank, for example, is seeking to relocate its European headquarters.

Thus, it is important to understand possible developments and the impacts of Brexit on daily business. The main issues are explored below from our respective points of view as lawyer, auditor and tax advisor.

Lawyer's perspective

Corporate law will be one of the topics that will have a huge impact for companies. Within the EU, companies can decide if they want to move their place of management to another country without losing their legal identity. Therefore, several corporations were founded as limited liability partnerships (LLPs) or limited companies within recent years. Right now, it is unclear what will happen to such UK companies in other EU jurisdictions. Under current legislation, those LLPs and limited companies will not keep their status as corporation but will be transformed compulsorily into a limited partnership, resulting in the shareholders becoming personally liable. Furthermore, cross-border mergers and similar actions will be much more complex with parties from a non-EU country, as the UK will be after Brexit.

It is worth checking existing contracts for any references to 'EU countries', as such contracts will need modification if UK companies are to be included after Brexit.

Global companies share many data, benefiting within the EU from the harmonised data protection rules. After leaving the EU, the UK will be seen as a non-member country and companies will need to obey stricter data protection regulations.

Pre-referendum debates revealed that some voters resented the influx of too many foreigners into the UK. Within the EU, the principle of freedom of movement applies. When the UK leaves the EU, foreign nationals living in the UK may need to deal with visa issues, work permits, and so on – just as UK nationals will need to do in continental Europe. At the moment, employers and employees can rely on EU labour laws and social security regulations. After Brexit, each case will be dealt with individually. Where possible, requests will need to be filed (e.g. for social security issues) and some employees may even have to terminate their work abroad. For British nationals working overseas, Brexit will mean that they will no longer benefit from any EU regulation or law.

Auditor's perspective

The currency risk has always been a topic for companies having subsidiaries or business connections with the UK. Auditors will need to bear increased volatility in mind, and should carefully check the values of participations, loans, etc. connected to British companies. So far, Brexit's effect on worldwide and especially EU markets is unpredictable.

Within the EU, the bookkeeping can be done by a company of another member country after applying for it. This will not be possible with the UK after leaving the EU.

Tax advisor's perspective

One of the main tax issues relating to daily business will be VAT and customs. Within the EU, companies and customers can benefit from harmonised VAT regulations. After Brexit, the UK government can set the VAT percentages freely without considering the minimum percentage of 15% for EU member countries. Furthermore, the UK government and British companies need not worry that the national regulations will be checked and eventually be abandoned with regard to EU laws on state aid. At the same time, the special regulations for EU member countries can no longer be used.

Especially for multinational groups, the loss of the parent–subsidiary directive will have a noticeable impact: within the EU, dividends can be paid tax free if certain conditions are met. Non-EU companies cannot benefit from this regulation, and the subsidiaries must withhold taxes for any dividend (in Germany, 25% plus solidarity surcharge). In case of a double tax treaty, the rate of the withholding tax might be reduced. The same aspects will need checking with regard to interests and license fees (interest and royalties directive).

In connection with corporate law also, tax advisors must bear in mind that UK corporations (limited companies and LLPs) will no longer be automatically accepted as corporations in Germany. As mentioned above, those companies will compulsorily be switched into a partnership and the shareholders will become taxable in Germany – in the absence of a grandfather rule or any other agreement. Furthermore, transformations relating to British companies will cause tax payments because they can no longer profit from tax reliefs given to EU companies.

EU companies can avoid an additional taxation at the German parent company on the basis of the provisions of the Foreign Transactions Tax Act if they can prove an actual economic activity. After leaving the EU, income from British subsidiaries might have to be taxed in Germany, if the tax rates stay as low as they are at the moment.

For individuals, it is important to be aware that after Brexit they will no longer profit from tax incentives for EU citizens, such as married-couple splitting.

While the UK seems to be starting Brexit earlier than expected, so far what happens next is unclear. Since some articles suggest that initial steps will be taken in March 2017, it is reasonable to start evaluating possible ways to proceed for clients having any business relations (holding company, subsidiaries, business etc.) with the UK.

Country Focus

Israel

Contributed by Ariel Zitnitski, CPA & ADV, Zitnitski Weinstein & Co.

E: az@zw-co.com

USA–Israel FATCA

The US and Israeli governments signed an agreement on 30 June 2014 to improve international tax enforcement and implementation of the provisions of the legislation of the FATCA (Foreign Accounts, Tax Compliance Act). The agreement regulates the transfer of information to the US Internal Revenue Service (IRS) through the Israel Tax Authority (ITA), which will receive the information from the Israeli financial institution.

In light of the petition submitted to and rejected by the High Court of Justice, and in light of the volume of inquiries to the ITA due to the short time remaining for the transfer of all reports, the ITA – having addressed this issue with the IRS and coordinated it with the USA – has extended the date for transferring the information required to 30 November 2016.

In accordance with the regulations, Israeli financial institutions must provide digital information to the ITA. This information will include data about accounts owned by US residents/citizens, as identified by financial institutions for the years 2014–2015.

Country Focus

Luxembourg

Contributed by Alhard von Ketelhodt, Fiduciaire Eurolux SA

E: avk@eurolux.lu

Changes in Capital Gains Tax

As the first step of a major tax reform, Luxembourg has changed its tax rate applicable on capital gains realised on the sale of real estate located in Luxembourg.

The tax rate is a quarter of the normal tax rate to be applied to individuals, resulting in a maximum rate of 10%.

This rate will be applicable for a limited period of time, from 1 July 2016 to 31 December 2017.

Country Focus

Malta

Contributed by Benjamin Griscti, Manager, Tax Services, KSi Malta

E: bgriscti@ksimalta.com

Malta: An ever-present non-domicile alternative

The lack of changes to its non-domicile fiscal legislation over the last few years has made Malta a highly attractive jurisdiction for individuals and companies wishing to obtain this status in an EU member state. Recent changes in other jurisdictions' legislation have intensified interest in Malta's non-domicile regime.

Consistently ranked among the best countries to live in by various international surveys, Malta's numerous territorial and fiscal traits have long attracted expatriates – including those of high-net worth – to take up residence there and adopt the non-domicile regime. Without any complications, minimum thresholds or charges, Malta's non-domicile status (for individuals or companies) allows for 'any foreign income and capital gains other than income earned during the year to be received into Malta without any tax charges'.

Although an individual could obtain residency, but not domicile status, in Malta through the normal operation of tax law (particularly by substantiating the fact that Malta becomes part of one's regular order of life), Malta offers a number of other formal residence non-domicile schemes. Below is a summary of the main residence non-domicile scheme options available.

- **The Residence or Global Residence Programme** (for both EU and non-EU nationals): Beneficiaries are subject to a beneficial flat tax rate of 15% on foreign income earned during the year and remitted to Malta, with a minimum tax liability of €15,000 p.a.
- **Malta Retirement Programme:** Beneficiaries are subject to a flat tax rate of 15% on foreign income earned during the year and remitted to Malta, with a minimum tax liability of €7,500 and an additional €500 for any dependent/special carer.
- **Highly Qualified Persons Programme** (for senior professionals in the financial services, gaming and aviation industries, both EU and non-EU): Eligible applicants enjoy a beneficial 15% tax on their employment income, and pay no income tax on any earnings exceeding €5 million.
- **United Nations Pensions Programme** (for both EU and non-EU nationals): Exempts beneficiaries who are in receipt of a pension or a widow(er)'s benefit from the United Nations, and offers a beneficial flat tax rate of 15% on any other foreign income earned during the year and remitted to Malta.

In addition, to date Malta continues offering the only EU endorsed Citizenship Programme enabling successful applicants to enjoy full EU citizenship together with all the rights associated with EU citizenship.

Country Focus

Peru

Contributed by Evelin Suarez R., Quantum Consultores

E: esuarez@quantumconsultores.com;

Madeira no longer a tax haven under tax laws in Peru

Madeira is a Portuguese archipelago situated in the North Atlantic Ocean, which is considered a tax haven under Peruvian tax laws and regulations; accordingly, most expenses incurred in that jurisdiction are not considered as income tax deductibles in Peru under the aforementioned laws.

With effect from fiscal 2015, Peru has signed a Double Taxation Avoidance Agreement (DTAA) with Portugal that is also intended to prevent tax evasion.[1]

According to Peruvian income tax legislation established since 2013, whenever Peru signs a DTAA with any jurisdiction considered as a tax haven that includes provisions for the exchange of information, that previously considered tax haven jurisdiction would no longer qualify as a tax haven from the effective date of the aforementioned DTAA. Article 25 of the DTA signed with Portugal includes a provision for exchange of information.

Consequently, under Peruvian income tax legislation, Madeira is no longer a tax haven (despite its 5% income tax rate) from the date the above-mentioned DTAA was signed between Peru and Portugal.

In this context, investments in and/or transactions between these two countries have become more attractive (that is, for transactions with economic substance rather than only form) – especially given that Portugal is a member of the OECD and EU; is not listed in any international blacklist; has an extensive network of DTAAs currently in force; and, most notably, its advantageous income tax regime (5% income tax).

Footnotes

1. 'El convenio entre la República del Perú y la República Portuguesa para evitar la doble tributacion y prevenir la evasión fiscal en relación con los impuestos a la renta y su protocolo' – CDI.

Country Focus

UK

Contributed by Andrew Constable and Graham Morgan, Kingston Smith LLP

E: aconstable@kingstonsmith.co.uk

E: gmorgan@kingstonsmith.co.uk

Andrew Constable

Graham Morgan

Country-by-country reporting

In October 2015, the OECD published its final guidance on the implementation of country-by-country (CbC) reporting.

The UK government has long been committed to the OECD's project on base erosion and profit shifting (BEPS) and included provisions in Finance Act 2015 to allow the Treasury to make regulations on the implementation of CbC reports for UK entities.

The relevant regulations came into force on 18 March 2016 and bring in reporting obligations for accounting periods beginning on/after 1 January 2016.

The rules will apply to multinational enterprise (MNE) groups that have consolidated group revenue in excess of €750 million.

UK entities that are the ultimate parent entities of MNE groups must file CbC reports within 12 months from the end of the accounting period to which the report relates.

In addition, UK constituent entities of MNE groups, and constituent entities with a UK PE, might be required to file a CbC report to the UK tax authorities; this could be the case if the ultimate parent entity has not filed a report in its country of residence, or if it has done so but there are no exchange arrangements between that country and the UK.

Exchange arrangements are only loosely defined in the regulations, but these will be deemed to be in place between signatories of the OECD's Multilateral Competent Authority Agreement (MCAA) on the exchange of CbC reports.

As of 21 October 2016, a total of 49 countries had signed up to the CbC MCAA for the exchange of information.

Where a UK entity that is not an ultimate parent entity is required to file a CbC report, it will only need to do so in respect of its subgroup.

Complications may arise in the first years of CbC reporting due to differences in the implementation dates in various jurisdictions.

For example, the USA will introduce reporting for accounting periods beginning on/after 30 June 2016; a US-headed group will not be required to prepare a CbC report in the US for year ended 31 December 2016, but a UK subsidiary of the group may well need to submit a report to the UK tax authorities for that year.

In addition, complications may arise as a result of foreign currency fluctuations. The USA has set the CbC turnover limited at US$850 million, and Australia at Au$1 billion, and exchange rate movements may therefore mean that a CbC report is required in the UK even though it is not required in the jurisdiction of the ultimate parent entity.

The requirements in each jurisdiction requiring a CbC report will need to be carefully reviewed following each accounting period.

The content of reports due in the UK is currently based on the OECD minimum standard, under which, for each jurisdiction in which the group (or subgroup) operates, the following will need to be provided:

- Total revenues, split between related and unrelated parties
- Profit before tax
- Tax paid and tax accrued for the year
- Stated capital
- Accumulated earnings
- Number of employees
- Total tangible assets other than cash
- Details of each entity operating in that jurisdiction and its principal activities.

These regulations add a further compliance burden to large businesses operating worldwide, which will need to ensure that sufficient resources are allocated to deal with these requirements.

Late filing in the UK will result in an initial penalty of £300, plus daily penalties which can rise as high as £1,000 per day. Additionally, penalties of up to £3,000 may be levied for inaccurate reports.

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International Tax Headlines

Contributed by Saurabh Jain, Tax Adviser, S.C. Vasudeva & Co.

E: saurabh.jain@scvasudeva.com

Australian government releases diverted profits tax exposure draft

On 29 November 2016, the Australian government released draft legislation for implementation of the Diverted Profits Tax (DPT), which shall give increased powers to the Australian Taxation Office (ATO) to address multinational tax avoidance. The DPT shall apply where it is reasonable to conclude that the principal purpose of a scheme involving a related-party cross-border transaction is to obtain an Australian tax benefit. The proposed legislation (DPT) shall broaden the ATO's scope to identify large multinationals seeking to avoid tax by shifting profits out of Australia, enabling the Commissioner to impose a penalty tax rate of 40% on arrangements made in breach of the rules.

Brazil issues proposed CbC reporting rules

On 4 November 2016, the Brazilian Federal Revenue Agency *(RFB; Receita Federal do Brasil)* has issued a proposed normative instruction (the proposed NI; an administrative legislation) to introduce country-by-country reporting (CbCR) rules in Brazil. The introduction of CbCR is one of the key steps taken towards Brazil's participation in the OECD BEPS project.

OECD releases multilateral convention to implement tax treaty–related measures to prevent BEPS

On 24 November 2016, the OECD released the text of the multilateral convention to implement tax treaty–related measures to prevent BEPS under Action 15 (the multilateral instrument). The text and the related explanatory statement have been formally adopted by some 100 countries to implement a series of tax treaty measures to update international tax rules and lessen the opportunity for tax avoidance by multinational enterprises.

India signs four new unilateral APAs

India's Central Board of Direct Taxes (CBDT) has entered into four unilateral advance pricing agreements (APAs). These were signed on 22–23 November 2016, with Indian taxpayers operating in various sectors, including pharmaceuticals, information technology and construction. The international transactions covered in these agreements include software development services, information technology–enabled services, engineering design services, contract research and development services and marketing support services. CBDT has so far entered into 115 APAs (108 unilateral, 7 bilateral).

Singapore increases disclosure requirements under transfer pricing

Recently, the Inland Revenue Authority of Singapore (IRAS) introduced new disclosure requirements for reporting of related-party transactions (RPTs). The given disclosure requirement (RPT form) shall be applicable from financial year 2017 (i.e. assessment year 2018) onwards, whereby taxpayers shall be required to file the RPT form along with their yearly income tax return (Form C). The new disclosure requirements shall be applicable to companies that have aggregate related party transactions above SGD 15 million in a financial year.

Amendments to the Poland Corporate Income Tax Act

On 22 September 2016, the President signed the Act dated 5 September 2016 to amend the Personal Income Tax Act and the Corporate Income Tax (CIT) Act. The amended provisions, apart from certain exceptions, will enter into force with effect from 1 January

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2017. The major changes brought to corporate income tax are as follows:

- The Amendment introduces a condition for application of exemption from withholding tax (WHT) of interest and royalties paid to associated companies from the EU. To qualify for the WHT exemption, the Polish payer must obtain a written statement confirming that the recipient company or PE is the beneficial owner of the payment.
- The Amendment introduces definition of income earned within the territory of Poland for purposes of determining the limited tax liability of non-Polish residents.
- The Amendment introduces reduced rate of 15% (instead of 19%) of CIT for small taxpayers, and for taxpayers who are in their first year of business activity.

Spain to hike CIT burden

On 2 December 2016, the Spanish government announced a revenue-raising Budget. This will increase the tax burden on corporations by restricting corporate tax deductions. The Budget imposes new limits on loss carry-backs and restrictions on the use of losses linked to shareholdings in companies located in tax havens or in territories that do not have an appropriate level of tax.

South Korea's 2017 Budget to hike top personal income tax rate

South Korea's government and parliamentary lawmakers have agreed to introduce an increased top rate of individual income tax in the 2017 Budget, to part-fund a childcare support programme. Individuals with annual taxable earnings of more than KRW 500 million (US$428,500) will be subject to a 40% income tax rate. The previous top rate was 38% for those with taxable earnings of over KRW 150 million.

Switzerland and South Africa sign declaration on AEOI

On 24 November 2016, Switzerland and South Africa signed a joint declaration on the automatic exchange of information (AEOI). They intend to begin collecting data in 2018, with the first exchanges to take place in 2019. Implementation will be based on the Multilateral Competent Authority Agreement (MCAA) on the automatic exchange of financial account information.

Switzerland and India sign declaration on AEOI

On 22 November 2016, Switzerland and India signed a joint declaration on AEOI. They intend to begin collecting data in 2018, with the first exchanges to take place in 2019. Implementation will be based on the MCAA on the automatic exchange of financial account information.

India and Japan amend their Double Tax Avoidance Agreement

An update to India and Japan's DTAA entered into force on 29 October 2016. The agreement has been amended to add internationally accepted standards for the exchange of information in tax matters. It provides that information received from Japan in respect of a resident of India can be shared with other law enforcement agencies with authorisation from the competent authority of Japan, and vice versa. The Protocol also inserts a new Article on assistance in the collection of taxes, and will exempt tax income from interest in the source country with respect to debt claims insured by government-owned financial institutions.

International Tax Cases

Prof. Kretzmer, Prof. Schremer, Prof. Beer v. Jerusalem Income Tax Assessor [Income Tax Appeals no. 4690-10-14/51481-01-15/49971-01-15 (5 October 2016)

Contributed by Ariel Zitnitski, CPA & ADV, Zitnitski Weinstein & Co.

E: az@zw-co.com

Facts of the case

The appellants, Prof. David Kretzmer, Prof. Yishai Beer and Prof. Adiel Schremer, were invited by the University of New York to spend the academic year as researchers at the newly opened research institute (Straus Institute and Tikvah Institute; hereafter, 'the Institute'). In return, the appellants received payments from New York University (NYU) in the amounts of US$75,000–100,000 for a 10-month stay (i.e., US$ 7,500–10,000 per month). The appellants reported the income as tax free.

Amendment 175 of Israel's Income Tax Ordinance determines that that fellowship income is tax exempt, subject to several conditions. The main condition for tax exemption is that the student/researcher must have been given their fellowship/scholarship without any commitment to provide any consideration or service in return.

The Jerusalem tax assessor issued the appellants' tax assessments for this income as taxable income from employment/occupation, not as a tax-exempt scholarship.

Contention of the taxpayer

- The appellants argued that they have received payment from NYU for the purpose of individual professional development, as a scholarship without any consideration given or service provided to NYU. Even if NYU had any expectations that the research would lead to academic publication, it is only expectation and not a legal liability on the part of the appellants.

- Two of the appellants, Prof. Beer and Prof. Schremer, argued that the study selected by them was not within the area of their professional specialisation. Thus, Prof. Schremer argued that he is a historian, not a law expert; and Prof. Berg argued that he is an expert in tax law, not in the law of war. Therefore, the tax assessor cannot describe this as professional income.

Contentions of the tax assessor

- The tax assessor claimed that the appellants in return gave services to the research institutes, and therefore all the funds given are taxable as income. Appellants were invited to NYU to carry out investigations in the research centre, and the Institute sought to promote their areas of expertise, as described in the invitation letters to Prof. Schremer and Prof. Beer: 'all fellows will share a research interest in the study of law and justice. This does not mean that each fellow will necessarily be a professor of law – we expect a robust disciplinary mix'.

- According to the tax assessor, the consideration given by the appellants to the research institutes is reflected by their commitment not to work elsewhere during their stay in New York, their commitment to research a topic that is in the interests of NYU and the Institute, and in anticipation of NYU and the Institute of a tangible product, such as an article, at the end of the period, as described in the invitation letter to Prof. Beer: 'We do expect something tangible such as an article, a completed book manuscript, etc. to show – and if appropriate to post on the Center's website – at the end of the fellowship or shortly afterwards'.

Decision of District Court

- Appeal denied.

- The court accepted the position of the tax assessor, which stated that the income from academic research in question is income from the appellants' occupation and is taxable under the tax laws.

International Tax Cases

M/s FZ- LLC v. Income Tax Officer (International Transactions), Ward – 1(1), Bangalore [2016] 75 taxmann.com 83 (Bangalore – Trib.)

Contributed by Ashish Gupta,
Tax Adviser, S.C. Vasudeva & Co.

E: ashish.gupta@scvasudeva.com

Facts of the case

The appellant (M/s ABB-FZ LLC) is a foreign company incorporated in the United Arab Emirates (UAE). During Assessment Year 2012–13, the appellant entered into a service agreement with ABB India Ltd (an Indian company) for rendering certain services, and received fees in consideration. These were in the nature of technical services, and the fees received were taxable in India at 10% as 'fees for technical services' (FTS) under Section 115A read with Section 9(1)(vii) of the Income Tax Act 1961 ('the Act'). The appellant did not offer to tax this income, on the grounds that the provisions of the DTAA between India and UAE included no clause for taxability of FTS and in the absence of any specific Article in the DTAA, the said income would not be taxable in India. During the assessment proceedings, the assessing officer held that in the absence of an FTS clause in the DTAA between India and UAE, the fees would be taxable as per the provisions of Section 9(1)(vii) of the Act, and accordingly passed the draft assessment order which was confirmed by the Dispute Resolution Panel.

Contention of appellant

- The FTS received by the appellant were taxable in India as per the Act, but the India–UAE DTAA did not contain any Article for taxability of FTS; therefore, the FTS would not be taxable as per the DTAA. Since the DTAA was more beneficial to the appellant, its provisions would apply; accordingly, the FTS would not be taxable in India.

- In the absence of any FTS clause in the India–UAE DTAA, the FTS could be either treated as business income (covered in Article 7 of the DTAA) or other income (covered in Article 22 of DTAA). Taxability in both cases is as discussed below.

  - **Business income (Article 7 of India–UAE DTAA):** If the FTS is treated as business income of the appellant, then it is not taxable in India in view of Article 7 of the India–UAE DTAA, since the appellant had no PE in India.

  - **Other income (Article 22 of India–UAE DTAA):** If the FTS is treated neither as FTS nor as business income of the appellant, then it falls under the residuary Article 22 of the India–UAE DTAA ('Other Income'), which mentions that such income is taxable in the country of residence of the recipient or payee only – which in the appellant's case is UAE; i.e., the FTS is not taxable in India.

- Given that the DTAA does not confer any right to tax any particular income, then the provisions of domestic law cannot be invoked to tax it.

- The absence of a relevant provision in the DTAA is not an omission, but a deliberate mutual agreement between the contracting states not to recognise/classify any income as FTS for the purposes of taxation. Therefore, the intention for not incorporating any provision in the DTAA is not to tax an income under the category of FTS; accordingly, the FTS cannot be brought to tax by applying the provisions of the Act.

Contention of assessing officer

- If the DTAA is silent regarding the taxability of a particular income, then the provisions of the Act should be considered and applied in respect of the FTS.

- Where there is no conflict between the Act and DTAA regarding FTS, then in the absence of any such provision in the DTAA, the provisions of the Act would apply to tax the FTS.

Appeal to Income Tax Appellate Tribunal (ITAT)

While filing appeal to ITAT, the appellant raised the following grounds:

- Whether in the absence of any specific article for taxability of a particular income in the DTAA, the provisions of the Act would be applicable to determine the taxability of such income?

- Whether FTS received by the appellant would be taxable in India regardless of whether that DTAA contains a specific article for the taxability of such income?

Decision of the ITAT

The Tribunal held that in the absence of an FTS clause in the India–UAE DTAA, the FTS would be taxed as per Article 7 of the DTAA – that is, it would be considered as business profit, since the assessee provided the services in the normal course of business; and as the appellant has no PE in India, the FTS is not chargeable to tax in India in view of Article 7 of the India–UAE DTAA.

Editorial Comments:

The following issues are covered in the above judgement:

In the absence of any specific article in the DTAA with regard to the income in question, it is not immediately apparent that the FTS is not taxable. It is therefore governed by other specific articles of the DTAA; and if the FTS does not fall under any specific article, then it is governed by the residuary article of the DTAA.

The article of the DTAA dealing with 'elimination of double taxation' states that in cases of conflict between the provisions of the DTAA and the Income Tax Act, the provisions of the Act will prevail. The said article should be restricted to the elimination of double taxation and cannot be extended to determine the taxability of a particular income; that is, it cannot be said that in the absence of any specific article in the DTAA, the income is taxable as per the provisions of the Act.

Morison KSi

The Next Step

Contact Morison KSi to discuss your needs

E: info@morisonksi.com
T: +44 (0)20 7638 4005

www.morisonksi.com

Morison KSi
6th Floor
2 Kingdom Street
Paddington
London, W2 6BD
United Kingdom