Briefing

International briefing for March

Speed read

In the UK the main focus this month has been the Budget where we saw the 'business tax roadmap' published with details of the UK's plans for implementation of the OECD BEPS proposals. The EU also published a roadmap for BEPS and launched a public consultation on double taxation dispute resolution mechanisms. The final UK country by country reporting regulations were published last month just before ECOFIN reached political agreement on the EC's CbC proposals. The OECD released a discussion draft on treaty residence of pension funds. Overseas there was a Budget in India, Luxembourg announced a decrease in its corporate tax rate and the Australian government announced measures to incorporate tax compliance requirements into foreign investment applications.

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The big news this month was the chancellor's Budget Speech on 16 March which contained a number of announcements on international tax matters. The *Business tax road map* – the sequel to the *Corporate tax road map* published in 2010 – was eagerly anticipated but a little disappointing as it offered little more than a summary of the Budget. In terms of actual content, the government reiterated its commitment to the OECD's proposed actions on base erosion and profit shifting (BEPS), confirming expectations that it will implement the recommendations on hybrid mismatches from 1 January 2017 and interest deductions from 1 April 2017. In relation to the latter, the UK's existing 'debt cap' legislation will be replaced with a restriction on interest deductions to 30% of EBITDA, subject to a £2m de minimis rule and a group ratio rule that will allow additional relief where the worldwide group as a whole is more highly geared. Financial services groups, typically exempt from the existing debt cap rules, are again likely to require a distinct regime, but there is no indication as to the potential form of this, which is still subject to discussions at the OECD.

As well as implementing the BEPS proposals, the government hopes to tackle weaknesses in the current regime for cross-border royalty payments by an extension in the UK's domestic withholding tax charge together with a new domestic law treaty abuse rule. Overseas property developers are also targeted, with the announcement of protocols to the existing tax treaties with Jersey, Guernsey and the Isle of Man intended to ensure that non-resident developers remain subject to UK tax on the profits of UK property development.

Also of note are plans to review the operation of the substantial shareholding exemption and the double taxation treaty passport scheme. Few details are given, but it is understood that these schemes will be reviewed against the backdrop of their original policy objectives. The significance of these regimes means that many groups will be watching closely to see precisely what this entails. Although not strictly international tax measures, the greater than expected reduction in the corporation tax rate to 17% in 2020 will increase the attractiveness of the UK but this will be counteracted by the new restriction on loss carry forwards which could be very costly for large groups.

The next stage of the tax policy cycle will be the publication of Finance Bill 2016 on 24 March, just before the Easter break, where we will see the legislation for the hybrids and royalty measures mentioned above, as well as the updated clauses to bring in the expected changes to the UK patent box.

EU update

EU roadmap on BEPS

On 19 February the Netherlands Presidency issued the final version of its roadmap, setting out its plans for work in the Council during the coming months, in the field of BEPS.

In the short term, the presidency aims to reach agreement on, amongst others, the possible inclusion of a minimum effective taxation test in the Interest and Royalties Directive; guidance and explanatory notes on hybrid permanent establishment (PE) mismatches in cases involving third countries; and the possible implementation of measures against tax treaty abuse. The Anti-Tax Avoidance Directive and country by country reporting will also be given a high priority (see more on progress on the latter below).

The medium term priorities include measures on transfer pricing, proposed EU guidance on the disclosure of aggressive tax planning and development of a set of guidelines on the conditions and rules for the issuance of tax rulings by member states.

Country by Country (CbC) reporting update

The final version of the UK's CbC regulations (The Taxes (Base Erosion and Profit Shifting) (Country-by-Country) Reporting Regulations, SI 2016/237) were published last month with several amendments since the draft regulations that were published in October 2015.

> A secondary reporting requirement will be introduced [for] UK tax resident constituent entities of foreign-parented groups

The most fundamental being that a secondary reporting requirement will be introduced such that UK tax resident constituent entities of foreign-parented groups will be required to file a 'UK CbC' report for the UK sub-group if the foreign parent is not required to file a report in its own territory, or if there are no / inadequate exchange arrangements in place such that HMRC will not receive the global CbC report from the parent tax authority. The UK regime applies for accounting periods starting on or after 1 January 2016 for multi nationals with revenues above the sterling equivalent of €750m in the previous period.

Then, on 8 March, the Council of the EU (ECOFIN)

reached political agreement on the European Commission's (EC's) CbC reporting proposals, which will also apply from 2016 to groups with revenues exceeding €750m. The main open issue had concerned the mandatory nature of the secondary reporting requirement for EU subsidiaries of non-EU parents because secondary reporting is optional under the OECD recommendations. Following a proposal by the German minister of finance, all member states agreed to make this reporting obligation mandatory from 2017 onwards, however it remains an option for member states to bring this requirement into their local legislation for 2016. Given the updated UK regulations came into force on 18 March 2016, unless there is a change, non UK headquartered groups in countries that have not yet introduced CbC requirements or have a delayed start date, for example the US, will have an obligation to file a UK CbC report for 2016.

Public consultation on double taxation dispute resolution mechanisms

On 16 February, the EC launched a public consultation to help identify ways to facilitate dispute resolution for businesses experiencing problems with double taxation in the EU. The consultation is part of the implementation of the EC's *Action Plan for Fair and Efficient Corporate Taxation*, launched in June 2015. The current mechanisms (Mutual Agreement Procedure and Arbitration) provided by bilateral tax treaties entered into by member states and by the EU multilateral Arbitration Convention can end up being very lengthy procedures. The general objective of this latest initiative is to create a more attractive investment and business environment and to achieve greater legal certainty at a time when recent significant changes to increase tax transparency, combat tax fraud and tax evasion may contribute to an exponential increase in disputes. The consultation will close on 10 May and then proposals for improvements to the current mechanisms are expected to follow in the summer.

Global update

OECD releases discussion draft on the treaty residence of pension funds

The final report on Action 6 of the BEPS Action Plan (*Preventing the granting of treaty benefits in inappropriate circumstances*) implied that additional work be needed to ensure that a pension fund is considered to be resident in the state in which it is constituted for the purposes of tax treaties regardless of whether it benefits from a limited or complete exemption from taxation in that state. Subsequently, on 29 February, the OECD released a discussion draft with proposed changes to articles 3 and 4 of the OECD Model Tax Convention, and to the Commentary on these articles, to effect the desired outcome. Comments are invited and should be sent by 1 April 2016 at the latest.

India: 2016 Budget

The Indian Budget Speech, on 29 February, contained proposals for a new 'equalisation levy' to tax the e-commerce transactions of non-residents. This new levy is expected to be charged at 6% of the amount of consideration for 'specified services' received or receivable by a non-resident payee not having a PE in India, and it will be paid by the Indian resident payer (or a non-resident payer having a PE in India). Specified services will include, amongst others, online advertisement, provisions for digital advertising space or any other facility or service for the purpose of online advertisement.

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It was also announced that implementation of the new company residence test based on place of effective management (POEM) will be deferred for a year until finance year 2016/17 and royalty income in respect of patents developed and registered in India by an Indian resident will be taxed at the rate of 10% on a gross basis (plus surcharge/cess). Also, there is confirmation that the government will deliver on its September 2015 commitment to legislate to put beyond doubt the fact that the minimum alternative tax (MAT) does not apply to foreign companies unless they have a PE in India; this is to be back-dated to 1 April 2001.

Luxembourg: 2017 tax reform

On 29 February the Luxembourg government released an outline of proposals for tax reform in 2017. Of most significance is a planned phased reduction in the corporate income tax rate from the current rate of 21% to 19% in 2017, and then to 18% in 2018. This would result in a global tax rate of 27.08% in 2017 and 26.01% in 2018 for companies in Luxembourg City. Limitations on the carry forward of losses are also to be introduced but there are few details at this stage. It is expected that tax losses generated in 2017 onwards will only be available to offset up to a maximum of 80% of the taxable profits of each year and for a limited period of time (expected to be set at ten years).

Australia: foreign investment applications and tax compliance

In an interesting development illustrating the increased emphasis being placed on good tax governance around the globe, the Australian government has announced that new tax compliance requirements are being imposed on foreign investment applications in order for such applications to be considered to not be against the 'national interest'. The new requirements include a broad condition that investors 'must comply with Australia's taxation laws' (as well as some specific conditions) in relation to the proposed investment and related transactions, operations or assets. The obligation on the investor is not limited to its own compliance, but also extends to investors ensuring that their 'associates' comply if it is within their powers to do so, or otherwise using their best endeavours to do so. Additional conditions may also be imposed on a case by case basis where a significant tax risk is identified. A failure to meet any of the conditions may result in prosecution, fines and/or ultimately an order for divestment of the Australian assets. ■

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- Budget 2016: The big picture (Chris Sanger, 18.3.16)
- Budget 2016: The impact on MNCs (Dominic Robertson, 18.3.16)
- 30 questions on BEPS (Jill Gatehouse & Susanna Brain, 29.10.15)