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Overview of requirements to obtain benefits under Croatia's tax treaties and EU directives

The withholding tax rates on certain types of Croatian-source income may be reduced if the recipient is resident in a treaty partner jurisdiction or if the income qualifies for an exemption under an EU directive. This article summarizes the requirements for EU (or Swiss) corporate recipients of Croatian-source income to obtain the benefits of certain EU directives.

Background

Nonresident companies receiving Croatian-source income may apply the provisions of a tax treaty or, if applicable, a relevant EU directive, to obtain an exemption or reduced withholding tax rate on dividends, interest and royalties received. Treaty provisions also may grant a withholding tax exemption for service fees (services are defined as market research, business advisory, audit and tax consulting). However, certain administrative formalities apply to obtain these benefits, and the formalities differ depending on whether the benefits of an EU directive may apply. Failure to comply with these requirements will result in the income being subject to withholding tax at Croatia's domestic rates (12% on dividends and 15% on interest, royalties and service fees).

To benefit from reduced withholding tax rates, the Croatian payer of the income must submit the nonresident recipient's certificate of residence or a treaty relief form to the Croatian tax authorities. Specifically, if the recipient is claiming an exemption from withholding tax under the relevant treaty, a certificate of residence is required (such a certificate is valid for one year from the date it is issued); if the recipient is claiming a reduced withholding tax rate, the Croatian payer generally must submit a treaty relief form for each payment (although if a payment is made on a recurring basis for the same type of service, the relief form may be submitted annually).

As an EU member state, Croatia has implemented the provisions of the EU parent-subsidiary and interest and royalties directives into its domestic law (additionally, under the EU agreement with Switzerland, measures similar to those of the directives apply to payments to Switzerland). According to the directives, payments generally must be exempt from tax at the time the payment is made (i.e. member states may not tax the payments and subsequently refund the tax to the taxpayer), but member states are permitted to require taxpayers to comply with administrative formalities to benefit from the relevant exemption. In Croatia, the following requirements must be met to benefit from the withholding tax exemptions for dividends, interest and royalties:

- **Parent-subsidiary directive:** To benefit from the 0% withholding tax on dividends and other profit distributions made by a Croatian company to an EU (or Swiss) parent company, the parent company must hold directly at least 10% (25% where the parent company is located in Switzerland) of the capital of the Croatian subsidiary for an uninterrupted period of two years. Additionally, the EU (or Swiss) recipient must have a legal form that is listed in the annex to the directive and be subject to corporate income tax under the relevant foreign tax law without the possibility of being exempt from tax.
- **Interest and royalties directive:** To benefit from the 0% withholding tax on interest and royalties paid by a Croatian company to an EU (or Swiss) company, the recipient must (1) be the beneficial owner of the income and be resident in another EU member state (or Switzerland), or be an associated company of the EU (or Swiss) company whose permanent establishment situated in another EU member state (or Switzerland) is treated as the beneficial owner; (2) be an associated company of the payer, meaning that the recipient must hold directly at least 25% of the capital of the payer company, or a third EU (or Swiss) company must hold directly at least 25% of the capital of both EU (or Swiss) companies; and (3) the participation must be held for an uninterrupted period of two years. Additionally, the EU (or Swiss) recipient must have a legal form that is listed in the annex to the interest and royalties directive and be subject to corporate income tax under the relevant foreign tax law without the possibility of being exempt from tax.

The holding period for purposes of both the parent-subsidiary and the interest and royalties directives is two years. Although certain EU member states allow the benefits of the directives to be granted even if the holding requirement is not met at the time of the payment, with tax subsequently collected if the holding period is not met, Croatia has not adopted this option and the Croatian tax authorities' position is unclear.

Requirements to obtain exemption

To obtain the withholding tax exemptions under the parent-subsidiary and interest and royalties directives, Croatia requires that certain documentation be submitted to the Croatian tax authorities. If the documentation is not provided, Croatia has the right to tax the payments.

For the withholding tax exemption on dividends, the following documentation must be submitted to the tax authorities within 15 days of the date the dividends are paid:

- Certificate of tax residence of the dividend recipient;
- Proof that the recipient meets the participation and holding period requirements (e.g. a trade registry excerpt of the payer/recipient);
- Proof that the recipient is subject to corporate income tax under the relevant foreign tax law (e.g. a statement provided by the foreign tax authorities); and
- Proof that the recipient company has one of the legal forms listed in the annex to the directive (e.g. a trade registry excerpt).

For the withholding tax exemption on interest and royalties, the following documentation must be submitted to the tax authorities before the relevant payment is made:

- Certificate of tax residence of the recipient;
- Proof that the recipient is the beneficial owner of the income (e.g. an official statement of the company);
- Proof that the recipient meets the participation and holding period requirements (e.g. a trade registry excerpt of the payer/recipient);
- Proof that the recipient is subject to corporate income tax under the relevant foreign tax law (e.g. a statement provided by the foreign tax authorities);
- Proof that the recipient has one of the legal forms listed in the annex to the directive (e.g. a trade registry excerpt of the recipient); and
- Information regarding the legal basis on which the interest or royalties payment was made (e.g. a loan agreement or licensing agreement).

Upon the submission of the required documentation, the tax authorities will issue an exemption certificate, under which the Croatian payer will have the right to make interest and royalties payments exempt from withholding tax. The payer may not apply an exemption for interest and royalty payments *before* receiving an exemption certificate issued by the tax authorities (Croatian tax law does not require such an approach for dividend payments).

Documents submitted to the Croatian tax authorities for purposes of securing an exemption certificate must be updated every 12 months from the date they are issued. The tax authorities will issue an official confirmation of the exemption within three months from the date the request is submitted, and the confirmation will be valid for one year.

A separate request for a withholding tax exemption must be submitted to the tax authorities for each payment made on a separate legal basis; for example, if interest payments are made under two loan agreements, an exemption request must be submitted for each agreement.

Comments

As described above, the benefits of the directives are available only if the relevant participation is held for at least two years and all other applicable requirements are met. The administrative procedure to apply the exemptions under the directives also require additional documentation that is not required when requests for reduced withholding tax rates are made under a treaty. Nevertheless, the application of the directives can be more beneficial for taxpayers if the withholding tax rates on dividends, interest and/or royalties prescribed by the relevant tax treaty exceed 0%.

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Chile:
New direct foreign investment regime proposed

The Chilean government submitted a bill to Congress on 30 January 2015 that would establish a new regime for direct foreign investment in the country and replace the existing foreign investment statute (Decree Law (DL) 600).

DL 600 has been the main route for foreign direct investment in Chile since 1974. The Foreign Investment Committee (FIC), the entity that administers DL 600, establishes the terms and conditions of the foreign investment. Under DL 600, foreign investors that bring capital, tangible assets or other forms of investment into the country may sign a foreign investment contract with the government. Such contracts offer foreign investors the following rights:

- The right to receive nondiscriminatory treatment;
- The right to participate in any form of investment;
- The right to acquire foreign currency at the most favorable exchange rate available on the formal foreign exchange market;
- The right to remit or reinvest earnings immediately and to remit capital after one year;
- The right to request under the investment contract that, during the investment period, the foreign investor will not be liable for changes in taxes on sales and services or for import tariffs on certain machinery and equipment, and that such goods will be exempt from VAT; and
- The possibility to request income tax or mining tax stability for a certain period of time.

The broad-based tax reform enacted in 2014 repealed DL 600 (effective 1 January 2016) and required that new foreign investment legislation be presented before 31 January 2015. The bill, which incorporates comments from a report issued by the Presidential Advisory Committee, is expected to be enacted, although it may undergo changes during the legislative process.

Overview and scope of proposed regime

Under the bill, the Chilean president would be responsible for setting the strategy for incentives and the promotion of direct foreign investment. A new committee of ministers would be formed to advise the president on these matters, and a new agency would be created to promote and attract the remittance of all types of capital and foreign investment. The agency would be the legal successor to the FIC.

A foreign investor would be defined as a nonresident individual or legal entity that transfers capital into Chile. A qualifying foreign investor would be able to request a certificate from the government that would allow it to apply the special regime contained in the bill.

Direct foreign investment would be defined as the transfer into Chile of foreign capital or assets owned or controlled by a foreign investor, in an amount equal to or greater than USD 5 million. The transfer could be in the form of tangible assets, technology, freely convertible foreign currency, the reinvestment of profits, loan capitalization or related party loans associated with the foreign investment.

Benefits of proposed regime

As under DL 600, the bill would guarantee a qualifying foreign investor access to Chile's formal foreign exchange market, both for incoming capital and for acquiring the currency to remit capital or profits. The foreign investor would be entitled to remit the capital and profits resulting from the investment abroad, provided all Chilean tax obligations have been met.

The bill provides that foreign investors would be subject to the general legal regime applicable to domestic investors and that there would be no discrimination against foreign investors.

The VAT exemption on certain imported capital assets also would be maintained.

However, the proposed regime does not contain a tax stability rule, such as the rule contained in DL 600.

Transition rules

Foreign investors that entered into contracts with the Chilean government under DL 600 would continue to be governed by the rules applicable to those agreements, provided the contracts are concluded by the later of 1 January 2016 or the date the bill becomes effective.

The bill also contains a transition regime, under which foreign investors would be able to apply for the benefits of DL 600 for a period of four years starting from the later of 1 January 2016 or the date the bill becomes effective. In this case, the foreign investors would be able to benefit from the tax stability regime (at a tax rate of 44.45%, as opposed to 42% under DL 600).

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Costa Rica: Draft income and sales tax reform bill released

On 10 March 2015, Costa Rica's Ministry of Finance released discussion drafts of a bill that would make substantial changes to the income tax and sales tax laws. The drafts are expected to be formally sent to congress in April for debate and approval.

The most important measures in the discussion drafts are as follows:

Income tax

- Introduction of a worldwide system of taxation (Costa Rica currently taxes on a territorial basis);
- Introduction of a general 15% tax on capital gains derived by Costa Rica residents (although securities issued by the National Financial System would be taxed at a rate of 8%) and an exemption for gains derived from the sale of a taxpayer's primary residence; a 3% withholding tax would be levied on gains derived by nonresidents from the sale of immovable assets, and a 15% rate in all other cases;
- Introduction of "BEPS"-type rules that would disallow a deduction for expenses paid to a resident of a tax haven jurisdiction;
- Introduction of formal transfer pricing rules based on the OECD guidelines;
- Taxation of foreign passive income when it is repatriated to Costa Rica, at a 15% rate;
- Introduction of new progressive income tax rates applicable to individuals (0%-25% for employees and 10%-25% for self-employed individuals); and
- Change of the tax period from the fiscal year to the calendar year.

Sales tax

The sales tax would be replaced by a value added tax (VAT), levied at a standard rate of 15% on the sale of most goods and services (services currently are not subject to sales tax). A reduced VAT rate of 5% would apply to certain supplies, such as raw materials used for the production of basic goods and services required for the production of agricultural goods. The following would be exempt from VAT: commissions and interest paid to regulated financial institutions, the transfer of movable and immovable property that is subject to transfer tax, private home leases and private health care.

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European Union:
Tax transparency package includes exchange of information on tax rulings

The European Commission published a tax transparency package on 18 March 2015 that contains proposals to combat tax avoidance by multinationals that threatens EU member states' tax revenues. A key component of the package is a proposal to introduce the automatic exchange of information between the tax authorities of EU member states on their tax rulings.

While tax rulings are granted to taxpayers primarily to provide legal certainty, rulings can result in tax base erosion where they are granted to offer selective tax advantages or to artificially shift profits to low or no-tax jurisdictions. The European Commission has already launched state aid investigations into specific tax rulings granted by several member states and has asked the targeted states to provide information on the rulings so the Commission can determine whether selective tax advantages are creating competitive distortions (for previous coverage, see *World Tax Advisor*, 9 January 2015).
URL: http://newsletters.usdbriefs.com/2015/Tax/WTA/150109_ib.html

Under the tax transparency package, the EU directive on administrative cooperation in the field of taxation, as amended by the European Council in 2014, would be amended to require full transparency regarding cross-border tax rulings granted by the EU member states' tax authorities. (The directive currently requires member states to automatically exchange a broad range of financial information with each other, in line with the new OECD/G20 global standard for automatic exchange of information between jurisdictions.)

The proposed tax transparency ruling measures would require the tax authorities of EU member states to automatically exchange information about the cross-border tax rulings they grant with the tax authorities of other EU member states on a quarterly basis. If another EU member state has any questions about a ruling, it would have the opportunity to request additional information from the member state that granted the ruling, and it then would be able to act against abusive situations as appropriate.

Other features of the tax transparency package, which are specifically aimed at information exchange, include the following:

- The code of conduct on business taxation would be revised. The code of conduct contains criteria to determine whether a domestic regime in an EU member state is "harmful," in that it may result in tax benefits for certain companies. However, since the current conditions for establishing when harmful tax competition arises fail to take account of the more intricate tax structures that may lead to tax avoidance, the European Commission is contemplating changes to the code of conduct that would make the provisions more effective in "ensuring fair and transparent tax competition" within the EU.
- The EU savings tax directive would be repealed. The savings tax directive contains less extensive provisions on the exchange of information than those in the EU directive on administrative cooperation.
- Certain proposals would be directed at increasing the transparency of multinationals, including the public disclosure of their tax information. However, the Commission

recognizes that this proposal requires careful consideration and a decision on this issue has, therefore, been postponed.

- The European Commission would cooperate with Eurostat and the member states to quantify the precise scale of tax fraud and evasion, to develop measures that are better targeted against these issues.

Comments

The tax transparency package represents another ambitious initiative in the EU's efforts to combat tax avoidance and evasion and to ensure greater transparency and cooperation between EU tax authorities. In addition to the 1997 code of conduct on business taxation, the 2012 action plan to combat fraud and the revision of the administrative cooperation directive, the European Commission has been negotiating with Switzerland about the automatic exchange of information. As from 2018, Switzerland will automatically exchange data with the tax authorities of EU member states about holders of Swiss bank accounts. The Commission aims to conclude similar agreements with Andorra, Monaco and San Marino; the EU and these countries currently have agreements in place that are substantially similar to the savings tax directive.

The proposals will now be submitted to the European Parliament for consultation and then to the Council for approval, with the goal of obtaining agreement on the measures before the end of 2015, so the new regulations would become effective on 1 January 2016. However, it is unclear whether all EU member states will agree to the measures.

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Greece:
New restrictions introduced on expense deductions

Greece's parliament approved a law on 20 March 2015 that introduces new restrictions on the deductibility of expenses for tax purposes.

Under the new rules, which apply as from 21 March (the date the law was published in the official gazette), any expense incurred for a payment to one of the following categories of persons (whether an individual or a legal person/entity) generally will be nondeductible:

- A person resident in a noncooperative state or a privileged tax regime jurisdiction (a country with a corporate tax rate of less than 13%);
- A "de facto" affiliated company that does not comply with Greece's transfer pricing documentation requirements *before* the relevant transaction is carried out; or
- A company or group of companies that lacks sufficient substance to conduct the particular business activity.

However, the expenses may be deductible if the taxpayer prepays a 26% tax on the total amount of the expenses. The tax paid will be refunded if the taxpayer can demonstrate within a three-month period (starting from the date the relevant invoice was issued) that the transaction took place on market terms.

For expenses incurred in transactions with companies described in the second and third bullets above to be fully deductible, the taxpayer will have to furnish "*conclusive evidence that the company does not fall under one of these categories*" before a regular tax audit takes place. If such evidence is produced, the taxpayer will not be required to pay the 26% tax.

The Ministry of Finance is expected to issue further clarifications of the new rules in the near future. Some business associations and the Scientific Committee of the Hellenic Parliament have criticized the measures on the grounds they may not be compliant with EU law and Greece's tax treaties.

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India:
Supreme Court rules success fees constitute fees for technical services

In a decision issued on 18 February 2015 (*GVK Industries Ltd.* (GVK)), India's Supreme Court held that a "success fee" paid to a nonresident financial advisor was subject to withholding tax as fees for technical services (FTS) under India's Income-tax Act 1961 (ITA), even though the advisor operated from offices outside India and provided the services outside India.

FTS are defined under Indian tax law as any consideration (including lump sum consideration) for the provision of managerial, technical or consultancy services (including the provision of services of technical or other personnel), but the definition does not include consideration for construction, assembly, mining or similar projects (which would be taxed as salary income of the recipient).

Section 9(1)(vii) of the ITA provides for source-based taxation of FTS paid to a nonresident by a payer located in India, unless it can be demonstrated that the services provided by the nonresident were used in the resident payer's business or profession carried on outside India, or that the fees were used to earn income from a source outside India. The source rule also provides that FTS received by a nonresident from an Indian payer are taxable in India, irrespective of whether the nonresident has a residence, a place of business or a "business connection" in India, or whether the nonresident has rendered services in India. (The concept of a business connection is used as a way to determine the Indian tax liability of nonresidents; the business income of a nonresident will be chargeable to tax in India to the extent the income accrues or arises through a business connection in India or from an asset or source of income located in India, and to the extent that income is attributable to operations carried out in India.)

Facts of the case

GVK, an Indian energy company, entered into an agreement with ABB Projects & Trade Finance International Ltd., Switzerland (ABB Switzerland) for consultancy services to assist GVK in raising funds both inside and outside of India to finance one of GVK's gas-based power projects. The consultancy services provided by ABB Switzerland included (i) developing a comprehensive financial model for the project; (ii) assisting in obtaining loan financing for the project on the most competitive terms, including the support of export credit agencies; (iii) assisting in loan negotiations and documentation; and (iv) closing the project financing in a coordinated and expeditious manner. For those services, GVK paid ABB Switzerland a fee equal to 0.75% of the total debt financing received by GVK. The fee was called a "success fee" because if ABB Switzerland failed to obtain the loan financing, the fee would not have applied.

GVK requested a "no objection certificate" from the Indian tax authorities that would enable it to remit the success fee to ABB Switzerland without the imposition of Indian withholding tax. GVK took the position that the success fee was not taxable in India for two reasons:

1. The fee did not arise or accrue, and was not deemed to arise or accrue, in India under the ITA because ABB Switzerland did not have a business connection in India and it provided all services from outside India; and
2. The success fee did not constitute FTS under the ITA because ABB Switzerland did not render any technical services. (GVK did not invoke the tax treaty between India and Switzerland because the payments were made before the 1994 treaty became effective.)

After the Indian tax authorities rejected GVK's application to remit the fee to ABB Switzerland without withholding Indian tax, GVK appealed to the Andhra Pradesh High Court. The High Court agreed with GVK's first argument that ABB Switzerland did not have a business connection in India, but disagreed with GVK on the source rule and held that success fee paid to ABB Switzerland was taxable in India as FTS. GVK appealed the decision to the Supreme Court.

Decision of the Supreme Court

The Supreme Court concurred with the Andhra Pradesh High Court's decision that ABB Switzerland did not have a business connection in India. With the issue of business connection settled, and because no relevant tax treaty applied, the Supreme Court was left to rule on whether the success fee was taxable as FTS under section 9(1)(vii) of the ITA.

According to the court, the main issue was whether the services provided by ABB Switzerland constituted "consultancy services." The Supreme Court observed that the term is not defined in the ITA, but it noted the general and common meanings of the word "consultancy" in judicial precedents and the dictionary, and concluded that the rendering of advice or opinions constitutes consultancy services. Since ABB Switzerland's financial advisors had specialized skills and knowledge (i.e. they prepared a model for the necessary financing and loans), the services provided constituted consultancy services. Accordingly, the success fee was sourced to India as FTS within the meaning of section 9(1)(vii), and was subject to Indian withholding tax at the applicable domestic rate.

This is the only Supreme Court decision that has explained the meaning of the term consultancy services. However, because a tax treaty did not apply in the case, the court did not address the meaning of FTS in the context of a treaty. Hence, while the decision is important, it will have a limited effect on similar cases in which an applicable tax treaty provides for a more restricted definition of FTS. (The Supreme Court decision actually was delivered 20 years after GVK requested the “no objection certificate” to remit the fee without withholding tax. Apparently, the primary reason for the delay was because a constitutional issue was raised, but ultimately was dropped).

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Indonesia:
Guidance on mutual agreement procedure updated

Indonesia’s Ministry of Finance issued a new regulation on 22 December 2014 (No. 240/PMK.03/2014 (PMK-240)) that updates the existing regulations in relation to the implementation of the mutual agreement procedure (MAP) provided for under Indonesia’s tax treaties. The new regulation is effective from 22 December 2014 and also applies to any ongoing MAP requests that were submitted before the issuance of the regulation but that have not yet been concluded. The salient updates are provided below.

Continuance of domestic dispute resolution during MAP process

PMK-240 reaffirms the provision from a prior regulation indicating that taxpayers have the option to apply for a MAP and to simultaneously continue to pursue domestic dispute resolution mechanisms (by applying for a tax objection, appealing to the Tax Court or requesting a reduction or cancellation of an incorrect tax assessment).

- Where the MAP results in a mutual agreement after the issuance of a tax assessment, but the taxpayer does not file an objection or apply for a reduction or cancellation of the tax assessment from the Director General of Taxation (DGT) (or seeks these remedies but the request is revoked or rejected due to failure to meet certain requirements), the DGT will amend the tax assessment letter.
- Where the MAP results in a mutual agreement and the taxpayer has filed an objection with the DGT, but the decision on the objection has not been issued, the DGT will take the mutual agreement into account in issuing the decision.
- Where the MAP results in a mutual agreement after the issuance of a DGT decision on an objection, but the taxpayer does not appeal the decision or revokes its appeal, the DGT will amend the decision.

- Where the MAP does not result in a mutual agreement, the DGT's assessments or decisions will remain in effect.

Request for MAP

PMK 240 specifies that a MAP request can be filed by (1) an Indonesian resident taxpayer, through the DGT; (2) the DGT itself; or (3) the tax authorities of a treaty partner country.

The regulation expressly states that documents submitted by taxpayers for the purpose of requesting a MAP will be treated as confidential, in accordance with the provisions of the law.

Under the regulation, a MAP request must be filed by the deadline specified in the relevant tax treaty; the period starts to run upon the first notification of an action resulting in taxation that is not in accordance with the treaty provisions. This may be: (a) the date of the tax assessment letter; (b) the date of the documentation supporting the withholding/collection of income tax; or (c) any other time specified by the DGT. A MAP request cannot be submitted after the final hearing on a dispute is concluded by the Tax Court under the domestic dispute resolution procedures.

MAP request filed by Indonesian taxpayer, through the DGT: A MAP request can be initiated by an Indonesian resident taxpayer when, among other reasons:

- An action by the tax authorities of a tax treaty partner country has resulted, or will result, in the imposition of double taxation on the Indonesian taxpayer in relation to a transfer pricing transaction with the foreign taxpayer;
- An action by the tax authorities of a treaty partner country in relation to an Indonesian taxpayer's permanent establishment (PE) in that country has resulted, or will result, in imposition of tax that is not in accordance with the relevant tax treaty;
- A dual residence issue exists; or
- Provisions are applied in relation to income sourced from the tax treaty partner country that are not in accordance with the relevant tax treaty, including where withholding tax is deducted by a tax resident of the tax treaty partner country.

The information needed for an Indonesian resident taxpayer to apply for a MAP includes the following (where applicable):

- The identity of the Indonesian taxpayer and its counterpart in the other country involved in a transfer pricing transaction;
- The fiscal year and/or the tax period with respect to the MAP request;
- An explanation of any adjustment made by the tax authorities of a treaty partner country, including the substance of the transaction, the amount and the basis for the adjustment; and
- The Indonesian taxpayer's opinion regarding any such adjustment.

The application and supporting documents must be submitted to the Director of Tax Regulation II; previously, a MAP request was submitted through the tax office where the taxpayer is registered.

The MAP request can be withdrawn at any time before the competent authorities reach a mutual agreement.

MAP request filed by the DGT: The DGT can file a request for a MAP if it deems this necessary, including in the following cases:

- A review of past mutual agreements indicates incorrect information;
- The DGT is requesting a corresponding adjustment from the tax authorities of a treaty partner country;
- The DGT is following up on a taxpayer's advance pricing agreement (APA) request; or
- There is an issue regarding the interpretation of certain provisions in the relevant tax treaty.

MAP request filed by the tax authorities of a treaty partner country: The tax authorities of a treaty partner country may request a MAP in the following cases, among others:

- The DGT issues a tax assessment to a tax resident of a tax treaty partner country that has a PE in Indonesia, or to an Indonesian resident taxpayer in relation to a transaction with a foreign taxpayer, that is considered not to be in accordance with the provisions of a relevant tax treaty (including a transfer pricing adjustment);
- The tax authorities are requesting a corresponding adjustment;
- There is a dual residence issue; or
- The tax authorities are following up on a foreign taxpayer's APA request.

PMK-240 has resolved an ambiguity from the previous MAP regulation by clearly indicating that the tax authorities of a treaty partner country may invoke a MAP (most likely due to the request of a taxpayer in that country) to provide relief from double taxation that has arisen due to a transfer pricing adjustment made by the DGT to a transaction with a related party in Indonesia. Accordingly, if an Indonesian taxpayer would like to request a MAP to dispute a tax assessment by the DGT, the request must come from its counterpart in the treaty partner country via the counterpart's competent authority. The DGT will then follow up on the request with the Indonesian taxpayer and request supporting documents and information from either the tax authorities in the treaty partner country or the Indonesian taxpayer.

As with a MAP request filed by an Indonesian taxpayer, a MAP request from the tax authorities of a treaty partner country must be submitted to the Director of Tax Regulation II, and the tax authorities can withdraw the MAP application before a mutual agreement is reached.

The regulation also provides a list of documents and information that the tax authorities of a treaty partner country should submit to file for a MAP. The information needed includes:

- The identity of the foreign taxpayer and its counterpart in Indonesia;
- The fiscal year and/or tax period with respect to the MAP request; and
- The actions taken by the Indonesian taxpayer or the DGT that are deemed to be not in accordance with the relevant tax treaty.

In a case where the MAP application relates to transfer pricing, the DGT will examine the availability of the corresponding adjustment provision in the relevant tax treaty in determining whether the MAP application can be processed.

MAP process

The regulation includes the following provisions on the MAP process:

- The process will be performed by the MAP implementation team, which is commissioned to examine the MAP application, request supporting documents and additional information, visit the taxpayer's site, prepare a position paper and perform other actions.
- The DGT will initiate a consultation with the tax authorities of the treaty partner country, which could be in the form of a direct meeting, an electronic communication or correspondence. Consultations should be conducted and completed within three years of the initial consultation, but could be extended through an agreement between the DGT and the tax authorities of the treaty partner country.
- After consultations, the DGT and the tax authorities of the treaty partner country will prepare a draft mutual agreement. The Indonesian taxpayer will then be asked to confirm the draft agreement. Once all parties have agreed to the draft, the DGT will issue a decision on the mutual agreement.
- The MAP process may be terminated before conclusion for certain reasons, including the following:
    - Incomplete documents;
    - Missing information;
    - A strong indication that a mutual agreement would not be obtained;
    - Withdrawal of the MAP application by the Indonesian taxpayer or foreign tax authorities;
    - Failure of parties to agree to the draft mutual agreement; or
    - Issuance of a tax court decision on an appeal, under domestic dispute resolution procedures, before a mutual agreement is reached.

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Italy:
Energy tax surcharge struck down

On 9 February 2015, Italy's Constitutional Court declared the energy tax surcharge (also known as the "Robin Hood" tax) unconstitutional and repealed the surcharge effective from 12 February 2015 (the day after the decision was published in the official gazette).

The surcharge was introduced in 2008, at the beginning of the global financial crisis, as a means to redistribute the excess profits earned by Italian entities (resident companies or permanent establishments of nonresident companies) operating in the energy sector. The surcharge consisted of a 6.5% increase (5.5% for FY 2008 and 10.5% for FYs 2011-2013) to the corporate income tax rate (IRES), and applied to companies exceeding certain revenue and income thresholds (for 2014, the thresholds were EUR 3 million of revenue and EUR 300,000 of taxable income) and operating in one the following sectors:

- Research and exploitation of hydrocarbons;
- Oil refining, production and trading of petrol, gasoline, natural gas and similar activities;
- Production and sale of electricity; or
- Transportation and distribution of natural gas.

The surcharge was extended to companies operating in the renewable energy sector in 2011.

An Italian company challenged the constitutionality of the surcharge in a lower tribunal, which referred the case to the Constitutional Court. The court concluded that the surcharge violated the general principles of equality and ability to pay set forth in the Italian constitution. The Constitutional Court based its decision on the following rationale:

- The surcharge was applied to overall taxable income, instead of only to "excess profits";
- Initially, the surcharge was justified by the financial crisis, but the conditions that existed at the time of its introduction no longer exist; and
- It was impossible to assess if the surcharge was being passed on to the final customers through an increase of retail prices (which specifically was prohibited by law).

The court's decision does not apply retroactively. Therefore, the surcharge still applies for 2014 (for calendar year taxpayers), and will have to be considered in the balance of the corporate tax payment that generally will be due by 16 June 2015.

Energy companies should consider the tax accounting impact of the change to the tax rate from 2015, and its potential effect on the 2014 financial statements.

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Korea:
Supreme Court rules on taxation of patents

Korea's Supreme Court issued a decision on 27 November 2014 concluding that payments made for the use of a patent registered outside Korea should not be considered Korea-source income for purposes of the Korea-US tax treaty, regardless of whether the patent was used in manufacturing or sales activities in Korea.

Background

Under article 93 of Korea's Corporate Income Tax Law (CITL), income for the use of intangible assets (including patents) in Korea, or income paid in Korea, will be treated as Korea-source income that is subject to withholding tax. The 20% domestic withholding tax (plus the 10% local income surtax) is reduced to 15% (16.5%, including the 10% local income surtax) under the Korea-US tax treaty. Under article 6(3) of the treaty, however, a payment for royalties will be treated as Korea-source income only if the payment is made for the use of, or the right to use, the property giving rise to the royalties within Korea.

In 2007, the Korean Supreme Court ruled that a patent is effective only in the jurisdiction(s) in which it is registered, in accordance with the territorial principle applicable to patents. Therefore, a payment for the use of a patent would be treated as Korea-source income only if the patent is registered in Korea; based on this interpretation, if a patent is registered only outside Korea, a payment for the use of the patent should not be considered Korea-source income.

Due to the conflict between the CITL and the language in Korea's tax treaties, the CITL was amended in 2008 to provide that where a patent is registered outside Korea, but it is used in manufacturing or sales activities in Korea, the patent will be deemed to be used in Korea and, hence, will give rise to Korea-source income.

Relying on the amended CITL, the Korean tax authorities have taken the position that withholding tax can be levied on royalties paid for the use of a patent in Korea, even if the patent is not registered in Korea.

Supreme Court decision

The Supreme Court held in its November 2014 decision that a payment for the use of a patent that is registered only in the US, and not in Korea, does not constitute a Korean-source royalty payment, regardless of whether the patent is used in manufacturing or sales activities in Korea. The Supreme Court based its conclusion on the following rationale:

- Even though the CITL was amended to provide that a patent that is not registered in Korea, but is used for manufacturing or sales in Korea, is deemed to be used in Korea, the Korea-US tax treaty takes precedence over domestic legislation (as confirmed by Korea's International Tax Coordination Law);
- Under the court's interpretation of the Korea-US tax treaty, a payment made for the use of a patent may be deemed to be Korea-source income only if the patent is registered and used in Korea; and
- Thus, if a patent is registered only in the US, it is irrelevant for purposes of the treaty whether the patent is used in manufacturing or sales activities in Korea.

Comments

This is the first Supreme Court decision rendered on this issue after the CITL was amended, and it clearly states that a tax treaty takes precedence over domestic tax law. Thus, whether a patent that is not registered in Korea actually is used in Korea is irrelevant in determining whether the payment constitutes Korea-source income under article 6(3) of the Korea-US treaty. The Supreme Court seems to have interpreted the place of use of a patent for purposes of article 6(3) of the treaty to be the place where the patent is registered. However, it is not entirely clear whether this interpretation also would apply where a Korean company manufactures products using a patent that is not registered in Korea, but sells the manufactured products in Korea (in contrast, in the case before the Supreme Court, the Korean company sold the manufactured products in the US market).

According to Korean tax law, a taxpayer can file an amended tax return to claim a refund of inappropriately paid withholding tax within three years after the original due date for filing the return. It is expected that a number of amended tax returns will be filed to claim a refund of withholding tax based on the Supreme Court decision.

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Ukraine:
Currency control restrictions extended and tightened

The National Bank of Ukraine (NBU) recently published new regulations aimed at ensuring the stability of the Ukrainian national currency (UAH), by limiting the flow of foreign currency outside the country. These regulations extend currency control measures introduced in 2014 (for previous coverage, see *World Tax Advisor*, 12 December 2014), and introduce additional restrictions.
URL: http://newsletters.usdbriefs.com/2014/Tax/WTA/141212_10.html

The regulations, which apply as from 4 March 2015, prohibit the granting of loans in UAH that are secured by property rights for foreign currency funds deposited with Ukrainian banks and place limits on the amount of foreign exchange that can be purchased. For example, resident entities may not purchase foreign currency if the foreign currency in their bank accounts exceeds USD 10,000 and a Ukraine bank may not transfer funds in UAH from investment accounts belonging to foreign investors in order to purchase Ukrainian state bonds. Foreign investors may not remit dividends abroad, nor may they make any remittance of funds abroad arising from a reduction in authorized share capital of a Ukraine company or that allows the investor to exit from a Ukraine company. To purchase or transfer foreign currency abroad, a certification must be obtained from the Ukraine tax authorities evidencing that the transferor does not have any Ukraine tax debt.

The NBU also raised the benchmark interest rate from 19.5% to 30%.

The new restrictions apply until 3 June 2015.

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In brief

European Union: The European Court of Justice (CJEU) issued a decision on 5 March 2015, concluding that France and Luxembourg cannot apply reduced VAT rates to electronically supplied books. Since 2012, France and Luxembourg have applied reduced VAT rates (5.5% and 3%, respectively) to books that are downloaded or streamed from a website. Hard copies of books also are taxed at the reduced rates. Both countries have taken the position that, since there effectively is no difference between digital and printed formats, no distinction should be made in the VAT treatment. The CJEU held that e-books should be subject to the standard rate of VAT, on the grounds that such books are electronically supplied services.

Greece: The government has issued guidance that sets out the documentation a Greek enterprise must submit to support a withholding tax exemption on dividends, interest and royalties paid to qualifying EU enterprises under the relevant EU directives as incorporated in the Greek Income Tax Code. Documents supporting a withholding tax exemption must be filed for each payment before the deadline for filing a nil return; alternatively, the taxpayer can furnish a tax residence certificate issued by the competent foreign authority. A transitional rule allows a Greek entity to submit the required documentation relating to dividends, interest and royalties paid between 1 January 2014 and 26 January 2015 up to 30 April 2015 without the assessment of penalties.

Hong Kong: The Inland Revenue (Amendment) Bill 2015, published in the official gazette on 20 March 2015, seeks to amend the existing provisions of the Revenue (Profits Tax Exemption for Offshore Funds) Ordinance 2006 to extend the profits tax exemption to nonresident private equity funds. The exemption, announced in the 2015-16 Hong Kong budget, is designed to increase the competitiveness of Hong Kong's asset management businesses.

Hungary: The European Commission has opened an in-depth investigation into whether Hungary's advertisement tax, introduced in June 2014, complies with EU state aid rules. Under the Advertisement Tax Act, companies are taxed at a rate depending on their advertisement turnover and companies with a higher advertisement turnover are subject to a significantly higher tax rate. At this stage, the Commission considers that this progressivity of the tax rates, ranging from 0% to 50%, selectively favors certain media companies, in breach of EU state aid rules. The Commission also has issued a separate decision prohibiting Hungary from applying the progressive rates until the Commission has finished its assessment (a "suspension injunction"). Following the investigation, the Commission will decide whether the advertisement tax gives rise to state aid to certain companies and, if there is aid, whether it complies with EU rules.

Tax treaty round up

At the end of each month, *World Tax Advisor* provides an update on recent tax treaty developments, with a focus on items that directly affect the withholding tax rates of the key jurisdictions covered by the Deloitte International Tax Source (DITS). Additional coverage may include stated negotiating priorities and other important tax treaty trends.
URL: http://www.dits.deloitte.com?id=us:em:na:wta:eng:tax

Unless otherwise noted, the developments discussed below are not yet in force.

Belgium-Bahrain: The 2007 treaty and 2009 amending protocol entered into force on 11 December 2014 and apply as from 1 January 2015. Dividends are exempt from taxation if paid to a resident of the other contracting state that, at the time of payment of the dividends, has held shares representing at least 10% of the capital of the payer company for an uninterrupted period of at least 12 months; otherwise, the rate is 10%. A 0% rate applies to interest on commercial debt claims resulting from deferred payments for goods, merchandise or services; interest on debt claims or loans (not represented by bearer instruments) paid to banking enterprises; and interest paid on bank deposits; otherwise, the rate is 5%. Royalties are taxable only in the state of residence of the recipient.

Croatia: See article in this issue.
URL: http://newsletters.usdbriefs.com/2015/Tax/WTA/150327_1.html

Cyprus-Bahrain: When in effect, the treaty signed on 9 March 2015 provides that dividends, interest and royalties will be taxable only in the state of residence of the recipient.

France-Tajikistan: The treaty between France and the former USSR has been terminated and ceased to apply as from 31 December 2014.

Hungary: The multilateral Convention on Mutual Administrative Assistance in Tax Matters, as amended, entered into force in Hungary on 1 March 2015 and generally applies from that date.

Malaysia: The Inland Revenue Board (IRB) released draft guidance on 15 March 2015 on the compliance requirements for Malaysia-based financial institutions and other persons to meet their due diligence and reporting obligations under the US Foreign Account Tax Compliance Act (FATCA). The guidance addresses the following: (1) key implementation milestones; (2) financial institutions that are required to report; (3) financial accounts to be reported; (4) exempt financial institutions, account holders and financial accounts; (5) procedures for identification of US reportable accounts; (6) information to be reported; and (7) timeline for reporting and how to submit the information. Malaysia reached an agreement on a Model 1 intergovernmental agreement (IGA) with the US to implement FATCA on 30 June 2014, and has been included in the US Treasury's list of jurisdictions that are treated as having an IGA in effect with the US. Under the IGA, reporting financial institutions will provide the IRB with the required account information for US persons, and the IRB then will exchange that information with the US Internal Revenue Service.

Portugal: The amending protocol to the multilateral Convention on Mutual Administrative Assistance in Tax Matters entered into force in Portugal on 1 March 2015 and generally applies from that date.

Singapore: On 17 March 2015, the Inland Revenue Authority of Singapore (IRAS) issued an e-Tax Guide to provide guidance to businesses, entities and persons affected by Singapore's intergovernmental agreement (IGA) with the US for implementation of the Foreign Account Tax Compliance Act (FATCA). The e-Tax Guide addresses the main aspects of due diligence and reporting requirements under the IGA, including the following: (1) key implementation steps; (2) financial institutions that are required to report; (3) financial accounts to be reported; (4) exempt financial institutions, account holders and financial accounts; (5) due diligence procedures required to be performed by reporting Singapore financial institutions to identify US reportable accounts; (7) information to be reported; and (8) timeline for reporting and how to submit the information. The IGA was concluded in substance on 6 May 2014 and signed on 9 December 2014.

South Africa-Cameroon: When in effect, the treaty signed on 19 February 2015 provides for a 10% withholding tax rate on dividends paid to a company that holds at least 25% of the capital of the payer company; otherwise, the rate will be 15%. The rate on interest and royalties will be 10%.

Spain: The Ministry of Finance published an order on 12 March 2015 that extends the deadline for financial institutions to submit the annual information declaration for financial accounts of certain US persons for purposes of the US Foreign Account Tax Compliance Act (FATCA). The deadline for 2014 has been extended to 1 June 2015 from 31 March 2015.

Turkey-Vietnam: When in effect, the treaty signed on 8 July 2014 provides for a 5% withholding tax rate where dividends are paid to a company (other than a partnership) that holds directly at least 50% of the capital of the distributing company or has invested more than USD 10 million (or its equivalent in Turkish or Vietnamese currency) in the capital of the distributing company; a 10% rate will apply where dividends are paid to a company that holds, directly or indirectly, at least 25% but less than 50% of the capital of the distributing company; otherwise, the rate will be 15%. The rate on interest and royalties will be 10%.

United Kingdom-Senegal: When in effect, the treaty signed on 26 February 2015 provides for a 5% withholding tax rate where dividends are paid to a company that holds directly at least 25% of the capital of the payer company; an 8% rate will apply where dividends are paid to a pension scheme; a 15% rate will apply where dividends are paid out of income (including gains) derived directly or indirectly from certain immovable property by an investment vehicle that distributes most of this income annually and whose income from such property is exempt from tax; otherwise, the rate will be 10%. The rate on interest will be 10%. A 10% rate will apply to royalties paid for the use of, or the right to use, a copyright of literary, artistic or scientific work (including cinematograph films), a patent, trademark, design or model, plan, secret formula or process or for information concerning industrial, commercial or scientific experience; a 10% rate also will apply to payments for the use of, or the right to use, industrial, commercial or scientific equipment, but the tax will be levied on 60% of the gross amount.

United States: Intergovernmental agreements to improve international tax compliance and to implement the Foreign Account Tax Compliance Act (FATCA) were signed between the US and Kosovo (on 26 February 2015), Belarus (on 18 March 2015) and Croatia (on 20 March 2015).

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Australia
New draft legislation on investment manager regime
The Australian government has released a fourth version of the investment manager regime that encourages particular kinds of investment made into or through Australia by certain non-Australian residents that have wide membership or that use Australian fund managers.
Issue date: 13 March 2015
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-australia-tax-alert-13-march-2015.pdf

United Kingdom
Budget 2015 announced
The UK chancellor announced his final budget of this parliament on 18 March 2015. The chancellor confirmed that the diverted profits tax legislation published in December 2014 has been revised and that the new law will come into force on 1 April 2015. Legislation also will be introduced, under which there will be an increase to the bank levy for short-term chargeable liabilities, as well as an increase in respect of chargeable equity and long-term chargeable liabilities. No new announcements were made with regard to BEPS other than to confirm that authority will be given to introduce country-by-country reporting in Finance Act 2015, and there was no update in relation to the introduction of legislation in respect of hybrid mismatches, with the commencement date for the new legislation still expected to be 1 January 2017.
Issue date: 18 March 2015
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-unitedkingdom-18-march-2015.pdf

United States
Progress on competent authority cases results in IRS acceptance of APA prefiling conferences for bilateral US-India APAs
The US IRS announced on 11 March 2015 that the Advance Pricing and Mutual Agreement program will begin accepting requests for prefiling conferences for bilateral APAs between India and the US.
Issue date: 12 March 2015
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-transfer-pricing-alert-15-005-12-March-2015.pdf

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