Deloitte.

International Tax

World Tax Advisor

10 January 2014

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New decree and rules may ease effects of Mexican tax reform on maquiladora industry

The Mexican president issued a decree on 26 December 2013 (Presidential Decree) that grants maquiladoras several tax benefits relating to income tax, VAT and the use in Mexico of machinery and equipment (M&E) owned by nonresidents, in order to mitigate some of the effects of the 2013 tax reform. Subsequently, on 30 December and 1 January, the Mexican tax authorities (SAT) issued miscellaneous tax provisions that clarify some of the tax reform measures affecting maquiladoras. The Presidential Decree was issued following discussions between the maquiladora industry association (INDEX) and the SAT, during which INDEX requested that the government take steps to ease the impact of the new legislation on the industry. The tax reform – which generally is effective as from 1 January 2014 – tightens the requirements for a maquiladora to qualify for benefits and significantly limits some benefits that were granted in the past.

Presidential Decree

The decree, which applies as from 1 January 2014 (unless otherwise noted), includes the following measures:

Neutralization of the negative impact of nondeductible payroll expenses – Under the new Income Tax Law (ITL), 53% of payroll-related expenses that are considered tax-exempt for employees is deductible by the employer, provided the employer's contributions to such benefits are not less than the contributions made by the employer in the previous year. Otherwise, the deductible percentage is reduced to 47%. Since typically maquiladoras perform labor-intensive assembling operations, payroll represents one of their largest expenses; thus, this limitation would result in a significant increase in the maquiladoras' tax liability.

The Presidential Decree provides that companies that qualify as performing maquila operations, as defined in the new ITL, will be allowed to take an additional deduction on their tax return equal to 47% of nondeductible payroll expenses, thus partially offsetting the limit on the deduction for the provision of tax-exempt benefits to employees. The additional deduction will be available to maquiladoras using the "safe harbor" option or that opt to obtain an advance pricing

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agreement (APA) from the SAT to comply with their income tax obligations. Regardless of the option chosen, maquiladoras should maintain detailed accounting records that clearly segregate maquila operations from other activities and identify the tax-exempt payroll items.

The Presidential Decree also requires that maquiladoras file an information return describing the amount of the tax benefit and how it was calculated by March of the year following the tax year.

Although the additional deduction does not fully offset the limit on the deduction of employee benefits, it does grant a benefit that is not offered to other sectors in the Mexican economy.

Grandfather clause for maquiladoras operating on 31 December 2009 – Under the definition of maquila operations in the IMMEX Decree, any company operating as a maquiladora (i.e. a company with an IMMEX program (a company authorized to temporarily import goods and services that will be manufactured, transformed or repaired, and then re-exported without payment of taxes, etc.) that had complied with its transfer pricing obligations under the maquila provisions) before 31 December 2009 was not required to comply with the M&E ownership requirements in the decree (otherwise known as the "grandfather clause"). The ownership requirements were carried over to the new ITL.

Under the ownership requirements, at least 30% of the M&E used to carry out the transformation or repair process by the maquiladora must be provided by the nonresident that is a party to the maquila agreement, and the nonresident's M&E may not previously have been owned by the maquiladora or another Mexican related party. This rule was not changed in the 2014 reform and there were no grandfather provisions for maquiladoras that were below the 30% threshold – all maquiladoras were required to satisfy the 30% M&E requirement by the end of 2014 or risk losing PE protection.

The Presidential Decree temporarily reinstates the grandfather clause by granting foreign principals a two-year period, starting in 2014, to provide at least 30% of the M&E to the maquiladora. After the third year (i.e. as from 2016), a maquiladora will not be entitled to obtain PE protection and apply the safe harbor provisions or the terms of an APA if the 30% requirement is not met.

Elimination of partial income tax exemption – The Presidential Decree formally eliminates the partial income tax exemption that was granted to maquiladoras in a 2003 presidential decree. The abolition of the partial exemption was anticipated, since the laws referenced in the 2003 decree were abolished under the 2013 reform. As a result, as from 2014, maquiladoras will have to pay income tax at the normal corporate rate of 30%, rather than an effective tax rate of 17.5% (or less) that applied under the 2003 decree.

Immediate VAT credit on acquisition of goods from a nonresident – The 2013 reform eliminates the 0% VAT rate on goods temporarily imported into Mexico and requires a maquiladora to withhold 16% VAT on behalf of a nonresident for the acquisition of goods temporarily imported into Mexico. The reform provided that a maquiladora could fully credit the VAT so withheld in the month following the month in which the VAT was paid to the authorities. The Presidential Decree now allows maquiladoras to credit the VAT in the month in which it is paid, thus eliminating the financial burden of paying the VAT to the tax authorities. This benefit applies only to the acquisition of goods that form part of a supply chain of products destined for export, and only if the maquiladora has obtained a valid tax compliance certification issued by the SAT (see below).

Maquiladoras must produce inventory controls and accounting records that track in detail goods and materials destined for export and those destined for the Mexican market.

Miscellaneous tax provisions

The following provisions in the package of miscellaneous rules affect maquiladoras:

Definition of "productive activities" – One of the stated purposes of the tax reform is to limit the concept of maquila activity to the export of manufacturing services and to restrict the ability of a maquiladora to sell or distribute directly in Mexico the products it manufactures. The new ITL provides that, for a maquiladora to qualify for PE protection, all income from a maquiladora's productive activities must be derived exclusively from the export of maquila services. The miscellaneous rules clarify that income will be deemed to be derived exclusively from the export of maquila services when it is derived from the provision of maquila services (or activities related to such services) to foreign related parties.

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The rules also clarify that income from productive activities does not include income from the sale and distribution of finished products, including: (1) the products manufactured by the maquiladora; or (2) the maquiladora's manufactured goods acquired in Mexico or abroad, whether separately or together with other products that were not manufactured by the maquiladora.

This provision will apply as from 1 July 2014 to give maquiladoras with nonmaquila income from sales to the Mexican market time to restructure or separate their activities. Until then, a maquiladora can consider that all of its income qualifies as income derived exclusively from productive activities, as long as the maquiladora has accounting records that differentiate each type of income, as well as the costs and expenses associated with each type of income.

Clarification that an APA is a transfer pricing and PE option – The miscellaneous rules clarify that an APA can be used by a maquiladora to fulfill its transfer pricing obligations and obtain PE protection for its nonresident related party, provided the maquiladora meets all other requirements in the ITL and the methodology used takes into account all assets located in Mexico destined for the maquila operation, including assets that belong to the foreign resident that is a party to the maquila agreement. Maquiladoras electing for an APA must inform the SAT no later than 30 June 2014 that they intend to opt for an APA.

VAT certification for maquiladoras – As explained above, the 2013 reform eliminates the 0% VAT rate on temporary imports for maquiladoras, but allows a maquiladora to apply a credit in the month the VAT is paid if the maquiladora has been certified by the SAT. On 1 January 2014, the SAT published in the Miscellaneous Tax Rules for Foreign Trade the requirements to obtain certification and the benefits of such certification. A three-tier rating system (A, AA and AAA) will be used to assess maquiladoras' controls and overall tax and customs compliance. The requirements and benefits associated with each rating are as follows:

A rating*		AA rating		AAA rating	
Requirements	Benefits	Requirements	Benefits	Requirements	Benefits
Electronically file a certification request Have adequate inventory controls in place to track the imported goods and materials Obtain a positive tax compliance opinion issued by the Mexican tax authorities Never have been listed on the SAT website as a "noncompliant taxpayer" Have valid "digital seals" and no omissions in the previous 12 months Demonstrate that all personnel are	Be able to credit VAT on temporary imports Obtain a VAT refund within 20 business days after the request is filed Certification will be valid for one year and will be renewed automatically if the maquiladora files a notice 30 days before the certification expiration date and continues to be in compliance	Same as for an A rating, plus: At least 40% of the maquila's operations carried out in Mexico in the previous year are with suppliers that have a positive tax compliance opinion and are not listed on the SAT website as noncompliant taxpayers Either carried out maquila operations for at least five years, or had more than 1,000 employees registered with the Social Security Institute in the previous year, or the value of M&E exceeds MXP 50 million	Be able to credit VAT on temporary imports Obtain a VAT refund within 15 business days after a request Have 30 days to self-amend any omission in advance of an audit If any tax liability has been omitted, the customs authorities can send the maquiladora an "invitation letter" rather than initiate an automatic examination Certification will be valid for two years and will be renewed automatically if	Same as for an A rating, plus: At least 70% of the maquila's operations carried out in Mexico in the previous year were with suppliers that have a positive tax compliance opinion and are not listed on the SAT website as noncompliant taxpayers Either carried out maquila operations for at least seven years, or had more than 2,500 employees registered with the Social Security Institute in the previous year, or the value of M&E exceeds MXP 100 million	Be able to credit VAT on temporary imports Obtain a VAT refund within 10 business days after a request Have 60 days to self-amend any omission in advance of an audit If any tax liability has been omitted, the customs authorities can send the maquiladora an "invitation letter" rather than initiate an automatic examination Certification will be valid for three years and will be renewed automatically if the maquiladora

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A rating*		AA rating		AAA rating	
Requirements	Benefits	Requirements	Benefits	Requirements	Benefits
registered with the Social Security Institute and provide documents showing payment of social security Produce evidence of investment in Mexico Submit the name and address of clients and vendors abroad from the previous tax year Allow customs officials to carry out an initial inspection and any additional inspections, as needed With respect to the IMMEX program: (1) have a valid program; (2) have all addresses or establishments registered with the Mexican tax authorities; (3) possess the necessary infrastructure to carry out maquila operations; (4) demonstrate that during the previous 12 months, the value of merchandise transformed and returned represents at least 60% of the temporary imports and exports of the same period; (5) demonstrate that		A tax liability was not assessed in the month before the certification application is filed, or if it was assessed, monthly payments were agreed upon or the liability was paid in full A VAT refund request was not denied within the previous 12 months	the maquiladora files a notice before the expiration date and continues to be in compliance	A tax liability was not assessed in the month before the certification application is filed, or if it was assessed, monthly payments were negotiated or the tax liability was paid in full A VAT refund request was not denied within the previous 12 months	files a notice before the expiration date and continues to be in compliance Allowed to file monthly consolidated customs filings (*pedimentos*) The company will be deemed to be in compliance with the customs inventory control requirements The maquiladora will not be required to show the serial number of merchandise in customs procedures The maquiladora will be able to make exports from its tax address

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A rating*		AA rating		AAA rating	
Requirements	Benefits	Requirements	Benefits	Requirements	Benefits
the maquila has the legal use of the real property on which the maquila operations are carried out for at least one year after the certification request is submitted; and (6) provide a description of the maquila operations					
* Additional requirements will apply to certain sectors and bonded warehouses, among other taxpayers.					

If a certification is suspended, the taxpayer will have 10 days to produce evidence to clear the cause of the suspension. If a certification is cancelled, the taxpayer will not be able to obtain another certification for 24 months.

A certification request may be filed between 15 April and 22 October 2014, depending on the taxpayer's location. Certification will be renewed automatically, provided the maquiladora files a notice before the term expires and it continues to be in compliance.

Conclusion

The publication of the Presidential Decree and miscellaneous rules are last-minute responses to the many challenges confronting maquiladoras in 2014 as a result of the tax reform, and other issues remain unresolved. According to INDEX's reports, industry representatives are continuing negotiations with the tax authorities, so more clarifications are expected in the near future.

— Herminia Diaz (New York)
Partner
Deloitte Tax LLP
hediaz@deloitte.com

Ricardo González Orta (Mexico City)
Partner
Deloitte Mexico
rgonzalezorta@deloittemx.com

Eduardo Barron (Mexico City)
Partner
Deloitte Mexico
edbarron@deloittemx.com

Cesar Martinez (New York)
Senior Manager
Deloitte Tax LLP
cesmartinez@deloitte.com

France:
Constitutional Court rules on finance law

The French Constitutional Court issued a decision on 29 December 2013 in which it invalidated several provisions of the finance law adopted by the parliament earlier in December that were designed to strengthen the anti-tax evasion rules and transfer pricing documentation requirements and to impose greater penalties for noncompliance. (Under French law, a law approved by both chambers of parliament can be referred to the Constitutional Court for review.) Most notably, the court rejected the new definition of "abuse of law," the new rules regarding the transfer of functions and risks abroad for transfer pricing purposes, the requirement to disclose tax schemes and the penalty rates based on turnover.

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On the other hand, the Constitutional Court upheld the anti-hybrid provision and the temporary tax on high salaries. The anti-hybrid rule disallows an interest deduction on a loan granted by an affiliated company if the interest is not subject to a tax at the level of the lending company that is equal to at least 25% of the tax that would have been due under the normal French rules. The temporary tax on high salaries is levied at a rate of 50% on the portion of remuneration paid to employees and directors that exceeds EUR 1 million per year per individual. The tax applies to remuneration paid or attributed in 2013 and 2014 (on an annual basis), but is capped each year at 5% of the company's turnover in the relevant year. The tax on high salaries is intended to replace the tax that would have required wealthy individuals in France to pay a 75% effective income tax rate on professional income exceeding EUR 1 million, but that was invalidated by the Constitutional Court in 2012.

The French president signed the laws without the following invalidated measures, and the laws were published in the official gazette of 31 December 2013:

Abuse of law – The finance law for 2014 contained a provision that would have expanded the definition of "abuse of law." Current rules allow the French tax authorities to disregard an arrangement that is artificial and/or that aims to benefit from the tax law in a manner that circumvents the intent of the legislature where the *sole* purpose of the arrangement is to mitigate or avoid tax. The budget law would have replaced the word "sole" with "main," but without any further clarification as to scope of the term. In its decision, the Constitutional Court noted that, in addition to the reassessment of unpaid tax and the imposition of late payment interest, a severe penalty is imposed for abuse of law (a fine equal to 80% of the unpaid tax). Taking these penalties into account, the court found that the proposed definition of abuse of law was too broad, and it therefore invalidated the new definition.

Reporting of "tax optimization" schemes – The finance law for 2014 included a requirement that any person marketing, selling, developing or implementing a tax optimization scheme report the scheme to the French tax authorities, with significant penalties for failure to comply. The scope of a tax optimization scheme would have been defined broadly to include any combination of steps and/or procedures whose main purpose would be to reduce tax liability, defer the payment of tax or obtain a tax refund. As with the case of the definition of abuse of law, the Constitutional Court found that the provision was too general and vague and could restrict the freedom of enterprises, and that the penalties for noncompliance with the reporting requirement (5% of fees received for the marketer and 5% of tax savings achieved for the implementer) were too severe.

Transfers of functions and risks abroad – The finance law for 2014 included measures that would have affected business restructurings (i.e. transfers of functions or risks) between affiliated companies where such restructurings led to a reduction in the taxable base in France; the measure specifically targeted situations where there is a transfer of activities to a foreign country or changes to the functions undertaken by a French company. If a transfer of functions or risks to a related enterprise created a reduction of at least 20% of the gross operating profit of the transferring enterprise (as compared to the average gross operating profit of the three years before the transfer), the transferring company would have had to submit information – at the request of the French tax authorities – demonstrating that it received arm's length compensation for the transaction (i.e. an amount equal to what would have been received from unrelated parties in similar circumstances), both before and after the transfer. Failure to provide the information would have resulted in profits that should have been realized being assessed at the level of the transferring company. According to the Constitutional Court, this proposal did not sufficiently define the terms "functions" and "risks," meaning that it violated the constitutional rules of accessibility and intelligibility of the law. As a result, the entire measure was omitted from the finance law.

Penalties based on turnover – The finance law for 2014 increased penalties for failure to comply with transfer pricing documentation requirements, from 5% of the transfer pricing reassessment to 0.5% of the turnover per tax period under audit (with a minimum penalty of EUR 10,000 per tax period). The Constitutional Court held that that the criterion for calculating the fine, which was unrelated to the magnitude of the offense, violated the principle of proportionality in penalties and, therefore, invalidated the measure.

For the same reason, the Constitutional Court invalidated the 0.5% fine based on turnover for failure to provide analytical accounting/cost accounting statements, as well as the consolidated accounts, during control operations onsite for companies whose turnover exceeds certain thresholds. Further, the court invalidated the 0.5% fine based on turnover where a company fails to submit a standard audit file (SAF-T) in an electronic format to the tax auditor within two weeks of the commencement of an audit.

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This article has been prepared by professionals in Taj, French tax and legal firm, member of Deloitte Touche Tohmatsu Limited.

— Ambroise Bricet (Paris)
Partner
Taj
abricet@taj.fr

Marie-Pierre Hoo (Paris)
Director
Taj
mhoo@taj.fr

Italy:
2014 Budget Law enacted

The Italian parliament passed the 2014 Budget Law on 27 December 2013 (and the law was published in the official gazette on the same date), which includes some important changes in the tax rules applicable to multinational companies with activities in Italy. The new provisions apply as from 1 January 2014, unless otherwise noted.

The most relevant new provisions are as follows:

Notional interest deduction – A notional interest deduction has been available to Italian companies as from fiscal year (FY) 2011. The deduction is determined by applying a notional yield (fixed at 3% for the first three years) to the increase in the qualifying book net equity, as shown in the financial statements for the period ending on or after 31 December 2010. The 2014 Budget Law increased the notional yield to 4% for FY 2014, 4.5% for FY 2015 and 4.75% for FY 2016.

Step-up of basis of assets booked in 2012 financial statements – The budget law introduces an opportunity to step-up the basis of tangible and intangible assets and certain participations booked in stand-alone financial statements as of 31 December 2012 (a similar opportunity last applied in FY 2008). A taxpayer will be able to increase its basis in an asset to the fair market value by paying a "substitute tax" on amount of this increase. The substitute tax, which would have to be paid by 16 June 2014, is 16% for depreciable assets and 12% for nondepreciable assets.

The increase in tax basis will allow higher deductible depreciation as from 1 January 2016 and lower capital gains from a sale of the asset as from 1 January 2017 for calendar-year taxpayers. The step-up will require a revaluation reserve to be booked in a company's net equity; such a reserve will have a "tax suspension" status (i.e. a distribution would trigger the taxation of the amount distributed at the level of both the company and the shareholder, unless a specific 10% substitute tax is paid).

Tax step-up of basis of intangibles booked in consolidated financial statements – The optional tax step-up regime for goodwill, trademarks and other intellectual property booked in consolidated financial statements is made permanent (the regime previously applied only to acquisitions/restructurings taking place before 2012, and now is retroactively available for acquisitions/restructurings occurring as from 2012). The substitute tax is equal to 16% of the amount of the step-up in basis and must be paid by the deadline for paying the balance of corporate income tax due for the period during which the acquisition took place (e.g. 16 June of the following year for calendar year taxpayers). The increase in tax basis will allow higher deductible depreciation as from the second fiscal year following the payment of the substitute tax and lower capital gains from an asset sale as from the fourth fiscal year following the payment.

Tax step-up of basis of Italian shares owned by nonresidents – As from 1 January 2014, the 2014 Budget Law reopens the window of opportunity for stepping up the tax basis of unlisted participations (and land) owned by Italian individuals and nonresident entities as of 1 January 2014, provided: (i) a formal valuation of the assets by a qualified appraiser is obtained by 30 June 2014; and (ii) a specific substitute tax equal to 2% (for nonqualifying participations) or 4% (for qualifying participations and land), applied to the entire stepped-up value, is paid by the same date.

Relevance of transfer pricing rules for IRAP purposes – The 2014 Budget Law clarifies that Italian transfer pricing rules are relevant for IRAP (i.e. local income tax) purposes (their relevance had been unclear since the rules for the computation of the IRAP taxable basis changed in 2008). No penalties are applicable for transfer pricing adjustments assessed by the tax authorities in relation to past tax years (i.e. from 2008 to 2012).

"Web tax" – A controversial web tax will apply as from 1 July 2014, under which Italian taxpayers will be required to purchase online advertising services and sponsored web links only from entities that are VAT-registered in Italy, even if the

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purchase is made through media companies and/or third-party operators. The purpose of the web tax is to force online multinational entities that often sell advertising through intermediary companies (with lower tax rates) to register for tax purposes in Italy.

The purchase price for online advertising services and ancillary services will have to be paid exclusively by bank or postal wire transfer (which must show identification information for the beneficiary), or other traceable payment method.

Italian entities involved in sales of online advertising services and related auxiliary services will not be able to determine their income on a cost-plus remuneration basis unless a specific tax ruling is obtained from the tax authorities.

Because there are some doubts as to whether the web tax is compatible with EU law, the effective date was deferred to 1 July 2014 to allow the Italian government to verify compatibility with the European Commission.

New procedure to offset tax credits against tax liabilities – To offset income tax or VAT credits exceeding EUR 15,000 per year against tax or social security liabilities, a taxpayer must obtain a “conformity certification” with respect to the tax returns giving rise to the credits from a CPA or internal statutory auditors to support that the taxpayer’s accounting is consistent with the tax returns and supporting documentation. This rule is applicable beginning with the tax returns filed for 2013.

Changes to deductibility of finance lease costs – Regardless of the duration of the contract, financial lease costs now are deductible for corporate income tax purposes by the lessee over half the tax depreciation period. For immovable property, financial lease costs are deductible over a period no shorter than 12 years. The new rules are applicable for finance leasing agreements concluded after 31 December 2013. Specific rules continue to apply for the leasing of company cars.

IRAP deduction for newly hired employees – As from FY 2014, Italian employers that increase the number of employees with an open-ended (i.e. permanent) contract (compared to the previous year) will be able to deduct additional personnel costs of up to EUR 15,000 per employee per year (labor costs generally are nondeductible for IRAP purposes). The deduction is available for the year of hiring and the following two years and cannot exceed the increase in the overall labor costs. This benefit is allowed in addition to other deductions on employment provided for IRAP purposes, but the total amount of the deduction for each employee cannot exceed the maximum limit of the salary and other related costs incurred by the employer. The deduction for each employee is available as long as the individual employment relationship is not interrupted.

The increase in employment must be considered net of decreases that may have occurred in controlled/related companies. The IRAP tax deduction will be forfeited if the number of employees in the following years decreases or remains the same.

Conversion of IRAP deferred tax assets into tax credits – The 2014 Budget Law extends indefinitely, as from FY 2013, the option for Italian entities to convert deferred tax assets created by the limited depreciation of goodwill and other intangibles into a tax credit. This option now also is available for IRAP purposes (previously, it was available only for corporate income tax purposes).

If a tax loss is reported on the IRAP tax return, the IRAP deferred tax assets booked on the financial statements for goodwill and other intangibles can be converted into tax credits in the amount related to those negative components that contributed to the tax loss.

— Luca Bosco (Torino)
Partner
Deloitte Italy
lubosco@sts.deloitte.it

Francesca Muserra (Bologna)
Partner
Deloitte Italy
fmuserra@sts.deloitte.it

Stefano Schiavello (New York)
Client Service Executive
Deloitte Tax LLP
stschiavello@deloitte.com

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Japan:
Tax reform proposals announced

On 12 December 2013, the ruling parties of Japan (the Liberal Democratic Party and the New Komeito Party) released the outline of 2014 tax reform proposals that support the government's efforts to revitalize the Japanese economy through tax incentives aimed at encouraging investment and consumption by corporations. In addition, the proposed legislation would change the way permanent establishments (PEs) are taxed in Japan.

Several of the key proposals that may affect foreign companies doing business in Japan and individuals working in Japan are highlighted below, including an update on certain expected changes to the Japanese consumption tax reform. It is important to note that these tax proposals have not yet been enacted and could change before becoming law.

Corporate tax

Proposals that would affect corporate tax include the following:

- Special reconstruction corporation surtax – The 10% surtax imposed on the national corporate tax for the three fiscal years beginning on or after 1 April 2012 would be abolished one year early. This would result in a reduction in the Japanese effective tax rate (e.g. the effective corporate tax rate of a company with its headquarters in Tokyo would be reduced from approximately 38% to 35.64% for fiscal years beginning on or after 1 April 2014).
- Taxation of PEs – The attribution approach would be adopted for allocating profits to a PE of a foreign enterprise located in Japan, instead of the "force of attraction" approach that has been used in the past. This would move Japan closer to the preferred profit allocation method advocated by the OECD. The reform would be effective for tax years beginning on or after 1 April 2016 for corporate tax purposes and from 2017 for income tax paid by individuals. Key features of the attribution approach include the following:
  - A PE would be treated as a separate and independent enterprise for purposes of allocating profits and losses, including those resulting from intracompany transactions between the PE and its foreign head office;
  - Profits attributed to the PE would be considered Japan-source income;
  - A foreign tax credit system would be established to provide a credit for taxes paid by the PE on its foreign source income; and
  - Records and proper documentation of PE transactions would need to be maintained and available upon request by the tax authorities during an audit of the PE.
- National strategic special zones (NSSZs) – As part of the prime minister's growth strategy, the government would designate certain NSSZs to encourage domestic and foreign investment through deregulation and tax incentives, including the following:
  - Allowing qualifying companies in an NSSZ to elect a special 50% depreciation or 15% tax credit on the acquisition cost of certain assets (25% depreciation and 8% tax credit on buildings and structures) placed into service between 1 April 2014 (or the effective date of the NSSZ Act, whichever is later) and 31 March 2016; and
  - Allowing an immediate deduction equal to 100% of the acquisition cost of qualifying core business assets.
- Deductibility of entertainment expenses – Corporations would be allowed a tax deduction for up to 50% of meal expenses (excluding meals for employees/directors) for the two fiscal years beginning on or after 1 April 2014. Small and medium-sized enterprises, which currently can claim a tax deduction of up to JPY 8 million for meals and entertainment expenses, would be able to elect to apply the current rule or the 50% deductibility rule.
- Tax credit or special depreciation for certain production-improving assets – Qualifying corporate taxpayers would be able to elect to take a tax credit of up to 20% of their tax liability or to expense the cost of certain state-of-the-art assets acquired and placed into service between the effective date of the act introducing this proposal and 31 March 2016. A reduced tax credit or depreciation deduction of up to 50% of the cost of such state-of-the-art assets would be available for assets acquired and placed into service on or after 1 April 2016 up to 31 March 2017.
- Other proposals related to tax credits – These include the following:
  - The conditions would be relaxed for obtaining the tax credit relating to wage increases, and this incentive would be extended two years to tax years beginning on or before 31 March 2016.
  - The percentage of research and development (R&D) expenses allowable as a credit under the incremental R&D credit regime would increase to a maximum of 30% (currently 5%), depending on the amount of the

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increase in R&D expenses. This incentive would be extended three years to tax years beginning on or before 31 March 2017.
    - The tax credit for job creation would be extended two years to tax years beginning on or before 31 March 2016.
- Revisions to local inhabitants and enterprise taxes – There would be a rebalancing of the local inhabitants and enterprise taxes effective for tax years beginning on or after 1 October 2014, although these revisions should not impact a company's current effective tax rate.
- Investment loss reserve deductions – Deductions would be allowed for qualified investment loss reserves associated with a reduction in value of certain assets acquired in a business reorganization or with an investment in a venture business through an investment limited partnership.

Consumption tax

The government is considering reducing the consumption tax rates on daily necessities at the time the general consumption tax rate is proposed to increase to 10% (i.e. 1 October 2015). A final decision on whether Japan will increase the consumption tax rate from 8% to 10% is expected in August 2014, with details of a multi-rate system expected by December 2014.

Legislation expected to broaden the scope of the Japanese consumption tax to include the provision of services (including Internet transactions and digital content) from overseas has been postponed.

Individual tax

The employment income deduction (a statutory deduction to provide an allowance for the costs incurred in relation to holding employment that is based on total taxable salary) would be revised for individual income tax purposes. The gross employment income threshold for the deduction and the deduction limitation would be reduced beginning in tax year 2016 (2017 for individual inhabitant tax).

— Sunie Oue (Tokyo)
Partner
Deloitte Japan
sunie.oue@tohmatsu.co.jp

Jun Takahara (Tokyo)
Partner
Deloitte Japan
jun.takahara@tohmatsu.co.jp

Linda Ng (New York)
Director
Deloitte Tax LLP
ling@deloitte.com

Yukinori Fujii (New York)
Manager
Deloitte Tax LLP
yukfujii@deloitte.com

Kuwait: Tax regulations amended

Ministerial Order No. 875 of 2013, issued by the Kuwait tax authorities (KTA) on 12 December 2013, makes significant changes to Kuwait's tax rules that are effective for financial periods ended on or after 31 December 2013.

Changes include the following:

Tax declaration – An auditor is required to provide full details of any violations of the Kuwait tax rules and regulations in the auditor's report to be attached to the tax declaration. Failure of an auditor to comply with the new rules will result in disciplinary procedures.

Taxpayers must attach certain additional information to the tax declaration regarding income derived from contracts and contract costs incurred during the year, along with relevant comparative figures for the previous taxable period.

Taxable income – The rules on the treatment of certain deductible expenses are amended as follows:

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- "Pre-operating" expenses incurred after a contract or agreement is signed but before activities commence may be deducted in the period in which the expenses are incurred, i.e. during the initial period of the contract, rather than being capitalized and amortized over the term of the contract.
- Costs relating to imported materials and equipment (M&E) sold to a party with which the taxpayer has a contract are determined based on a fixed percentage of the relevant income, rather than a range. The deductible percentage varies from 85% to 95% of income, depending on whether M&E is imported from the head office, a related party or an unrelated party.
- Design and consulting expenses incurred abroad are determined based on a fixed percentage of the relevant income, rather than a range. The deductible percentage varies from 70% to 85% of income, depending on whether the expenses relate to design or consulting and whether the services are performed by the head office, a related party or an unrelated party.
- Work-in-progress (WIP) costs are more comprehensively defined as costs incurred for work not yet completed by the taxpayer, but that have been declared in the tax return where no corresponding revenue has been recognized during the taxable period. As a result, a taxpayer can either properly measure and declare the income corresponding to WIP costs to be reported during the year, or carry forward such costs to subsequent fiscal years if the relevant revenue cannot be properly measured or estimated.
- Losses resulting from any subcontracting of work are not deductible, regardless of whether the subcontractor is the taxpayer's agent or a third party, and certain written approvals are required to deduct subcontracting costs.
- If the taxpayer submits custom statements and documents relating to assets leased from a head office or related party, it may deduct the rent charged by the head office/related party, provided the amount does not exceed the depreciation on the assets for the period during which they are used in Kuwait and the head office/related party treats the lease payments as taxable income. If it is not possible to determine the value of assets with respect to which depreciation is calculated, leasing costs relating to such assets are disallowed in full.
- The KTA may estimate capital gains from a disposal of fixed assets only if the taxpayer fails to provide sufficient documentation supporting the profits or losses realized on the disposal.
- A deduction is allowed for labor insurance required under Kuwait law and M&E provided locally, but insurance costs incurred abroad are not deductible, except to the extent they relate to imported M&E (in which case they are considered part of the total cost of the imported M&E).
- Compensation may be taken into account only in the taxable period in which it was realized and is adjusted against the taxable profit accordingly (previously, compensation could be proportionally claimed based on the relevant income, regardless of whether the taxpayer's results were assessed on an actual or a deemed basis).

Exemptions – The deductible percentage of indirect expenses incurred inside Kuwait (general and administrative expenses) for companies that are exempt from tax under the provisions of an applicable tax treaty or that are permanently exempt under a special Kuwaiti law is a fixed percentage of 20%, rather than a range of 15% to 20%.

Tax collection, administration and procedure – The KTA can impose penalties on companies that do not declare income in their tax declarations where this income is discovered during a subsequent inspection or audit.

A number of rules are amended to reflect a change in the forms and information required to be submitted to the KTA. These changes affect the issuance of a tax residence certificate that can be used by the taxpayer to claim the benefits under an applicable tax treaty; tax refunds as a result of overwithholding under a treaty; the registration of investment funds, portfolio and direct investments on the Kuwait stock exchange and notification to the KTA of any changes to such investments or the ceasing of activities; and the requirements for fund managers, investment custodians and corporate bodies to withhold and transfer tax due on dividends to the KTA.

— Ihab Abbas (Kuwait City)
Partner
Deloitte Kuwait
iabbas@deloitte.com

Bassem Abul Khair (Kuwait City)
Senior Manager
Deloitte Kuwait
basabulkhair@deloitte.com

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Spain:
Fiscal year 2014 budget enacted

Spain's fiscal year 2014 budget, published in the official gazette on 26 December 2013, contains tax measures that usually are included in the annual budget laws and extends measures that were introduced in recent years to increase tax collection.

The main measures included in the new budget are the following:

Corporate income tax

- Effective retroactively from 1 January 2013, gains derived from the migration of an entity to another country or from the transfer of the assets of a permanent establishment to another EU member state will be deferred until the assets are transferred to a third party. A similar tax deferral has been introduced for reorganizations that fall within the scope of the special tax regime. These measures have been introduced as a result of the 25 April 2013 decision of the Court of Justice of the European Union that Spain's exit tax rules discriminated against nonresidents.
- The reduced corporate tax rate of 25% applicable to entities with turnover of less than EUR 5 million that have less than 25 employees but that maintain or create jobs has been extended for fiscal year 2014.
- The deduction for professional training activities regarding new technologies has been extended for fiscal year 2014.
- An annual update of the applicable monetary correction coefficients to calculate the taxable gain derived from the transfer of immovable property is included.

Withholding tax

For fiscal year 2014, the withholding tax rates on payments to foreign individuals or entities will continue to be 21% and 24.75%, depending on the nature of the payment.

Personal income tax

- The "complementary tax" to the general personal income tax that was approved for 2012 and 2013 has been extended to fiscal year 2014. The complementary tax is calculated on the general net personal income tax base (which includes salary and wage income, income from economic and professional activities and income from the leasing of real property). The complementary tax rates range from 0.75% for the first tax bracket for income below EUR 17,707.20 to 7% for income exceeding EUR 300,000.
- The complementary tax continues to apply to taxable savings income, which generally includes dividend and interest income and capital gains. The applicable rates range from 2% for income below EUR 6,000 to 6% for income over EUR 24,000.

Wealth tax

The elimination of the 100% exemption to the wealth tax, which originally was introduced in 2008, is extended for fiscal year 2014. However, the wealth tax is not applicable to most taxpayers, since a significant tax-free allowance of EUR 700,000 was granted in 2011.

— Brian Leonard (Madrid)
Partner
Deloitte Spain
bleonard@deloitte.es

Cristino Fayos (Madrid)
Partner
Deloitte Spain
cfayos@deloitte.es

Elena Blanque (Madrid)
Senior Associate
Deloitte Spain
elblanque@deloitte.es

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Vietnam:
Foreign currency restrictions tightened

The State Bank of Vietnam issued a circular on 26 December 2013 (Circular 32) that contains new restrictions to re-enforce guidance on the use of foreign currency in Vietnam. Under the circular, residents and nonresidents may not conduct transactions in foreign currency within Vietnam or use foreign currency in advertising, quotes, contract prices or similar uses within Vietnam unless specifically allowed under previous guidance (Decree 160/2006/ND-CP), which provides implementation guidance on the Ordinance on Foreign Currencies. The new rules will apply as from 10 February 2014.

Circumstances in which foreign currency may be used within Vietnam include the following:

- Banks and nonbanking credit institutions, branches of foreign banks and other organizations that are allowed to conduct business may provide foreign exchange services permitted by the State Bank of Vietnam.
- Under certain circumstances, domestic businesses or foreign contractors that qualify as tax residents are allowed to bid in foreign currency and to receive payment in foreign currency for remittance overseas.
- Foreign currency may be used to quote, set prices, list prices in contracts and make and receive payments in transactions between an export-processing enterprise (EPE) and another EPE, or where an EPE purchases domestic goods for export manufacturing.
- Resident enterprises engaged in the business of air transportation, hospitality or tourism are allowed to list and advertise prices of goods and services in Vietnam Dong (VND) and an equivalent foreign currency on websites and in specialized publications that are written only in foreign languages.
- Resident or nonresident organizations are allowed to pay salaries, bonuses and allowances in foreign currency, as agreed in labor contracts with foreign employees who work for the organization, regardless of the residence status of these employees.

Failure to comply with the rules in the circular may result in penalties of up to VND 500 million.

— Thomas McClelland (Ho Chi Minh City)
Partner
Deloitte Vietnam
tmcclelland@deloitte.com

Tuan Bui (Hanoi)
Partner
Deloitte Vietnam
tbui@deloitte.com

Vietnam:
2014 rate changes

The following chart summarizes some of the tax rate changes that are effective as of 1 January 2014 (unless otherwise noted):

Country	Type of tax		
	Corporate income tax	Withholding tax on dividends, interest and royalties paid to a nonresident	VAT
Cyprus			Standard rate is expected to increase from 18% to 19% and 8% reduced rate is expected to increase to 9% on 13 January 2014
Denmark	Reduced from 25% to 24.5%		
Estonia		Withholding tax on interest applies only where a nonresident investor derives interest income from an Estonian contractual fund or other pools of assets	
Finland	Reduced from 24.5% to 20%	Withholding tax rate on dividends and royalties reduced from 24.5% to 20%	

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Country	Type of tax		
	Corporate income tax	Withholding tax on dividends, interest and royalties paid to a nonresident	VAT
France	Temporary surtax increased from 5% to 10.7%		Standard rate increased from 19.6% to 20%
Japan			Consumption tax rate will increase from 5% to 8% in April 2014 and is expected to increase to 10% in October 2015
Israel	Increased from 25% to 26.5%		
Mexico	30% corporate income tax rate is unchanged, but the flat tax is abolished	A 10% withholding tax applies to dividends paid out of profits generated after 1 January 2014	
Norway	Reduced from 28% to 27%		
Thailand	Reduced from 30% to 20% for tax years 2013 and 2014		
Ukraine	Reduced from 19% to 18% (rather than the envisaged 16%)		Standard rate reduced from 20% to 17%
United Kingdom	Standard rate will reduce from 23% to 21% on 1 April 2014 and to 20% on 1 April 2015		
Vietnam	Reduced from 25% to 22% and will further reduce to 20% on 1 January 2016		

In brief

Canada – The province of Nova Scotia will reduce its harmonized sales tax rate from 15% to 14% on 1 July 2014 and to 13% on 1 July 2015.

Czech Republic – VAT returns must be submitted electronically as from 1 January 2014, although electronic filing is not mandatory for individuals whose an annual turnover is less than CZK 6 million.

Hong Kong – A bill gazetted on 27 December 2013 would reduce by half (from 16.5% to 8.25%) the profits tax on the offshore risk insurance business of captive insurers that are set up to underwrite risks of companies within the captive insurer's group. The proposed measure aims to attract more enterprises to establish their captive insurers in Hong Kong, which is in line with the initiative announced by the Financial Secretary in the 2013-2014 budget. The operation of captive insurance, its contribution to risk management and Hong Kong's regulatory framework for captive insurers will be discussed during an upcoming workshop held by the Financial Services and the Treasury Bureau and the Hong Kong Federation of Insurers. If the bill is passed, it will be effective from year of assessment 2013/2014.

Hungary – Changes to Hungary's participation exemption regime and the taxation of company migrations were approved by the parliament on 18 November 2013 and apply as from 1 January 2014. The new rules reduce the ownership threshold to benefit from the participation exemption for capital gains on the sale of shares in a company from 30% to 10% and

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extend the deadline for reporting the acquisition to the tax authorities from 60 days to 75 days. The one-year holding period is unchanged. Under the new company migration rules, nonresident entities that migrate their tax residence to Hungary by transferring management and control to Hungary will be entitled to a fair market value basis for tax depreciation purposes. The new rules allow companies migrating to Hungary to step up the tax value of their assets to market value, irrespective of the historic or current foreign tax value of those assets.

Indonesia – As from 1 January 2014, electronic invoices may be issued for VAT purposes. Printed invoices still are possible, although if a VAT entrepreneur is qualified to issue electronic invoices, it is not permitted to issue hard copy invoices unless certain conditions are satisfied.

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Australia
Government announces fate of outstanding tax measures
The Australian government has announced the outcome of the review on whether 64 unlegislated tax measures would proceed.
Issue date: 20 December 2013
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-australia-201213.pdf?id=us:em:na:wta:eng:tax:011014

Gibraltar
Royalty income to be subject to income tax
As from 1 January 2014, Gibraltar will tax royalty income.
Issue date: 24 December 2013
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-Gibraltar-241213.pdf?id=us:em:na:wta:eng:tax:011014

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