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In this issue:

Russia’s “de-offshoring” policy may affect foreign and domestic businesses

Russia’s national strategy for counteracting tax abuse, referred to as “de-offshoring of the economy,” is a critical topic on the agenda of businesses operating in Russia today. This strategy, which was initiated by the president at the end of 2013 and has been refined through negotiations and discussions between the government and business representatives, likely will have a significant impact on both domestic and foreign groups of companies.

The government intends to take a multi-pronged approach to tax avoidance and evasion and to ensuring that the ownership structures of Russian companies are more transparent. To this end, in February 2014, the government announced a detailed plan to counteract the off-shoring of the Russian economy, and announced legislative measures and deadlines to adopt the necessary laws. A series of draft laws related to de-offshoring are expected to be submitted to the State Duma before the end of 2014. The first draft law, which would amend the tax code, was presented by the Ministry of Finance and published on its website on 18 March 2014. This first wave of proposed measures includes the introduction of a new corporate residence rule, a controlled foreign company (CFC) regime and new rules on the indirect disposal of Russian real estate-rich companies. The draft law is expected to take effect as from 2015.

Although initially aimed at preventing owners of Russian businesses from earning profits in Russia while keeping their tax base offshore, de-offshoring may affect the Russian investment climate for foreign business groups as well. If adopted, the proposed legislation would provide the Russian tax authorities with a number of mechanisms to tax cross-border structures and would amplify their ability to obtain information on such structures.

Russia’s initiatives in many respects parallel the OECD’s base erosion and profit shifting (BEPS) project. Russia is an active participant in international discussions on BEPS and has voiced its support for a number of OECD initiatives related to combatting abuse of the tax system that results from discrepancies between domestic tax rules and those of other jurisdictions. Russia also has announced its full political support to the OECD’s 15-point action plan on BEPS.

This article looks at some of the proposed de-offshoring measures and other developments that tie into the de-offshoring initiative.

Definition of residence

One of the provisions in the draft law issued in March would amend the definition of residence of companies for tax purposes. The concept of residence currently is based on the place of incorporation (i.e. registration), meaning that a company is considered a Russian tax resident if it is incorporated in Russia. Foreign legal entities are taxed in Russia only if their activities constitute a permanent establishment or if they derive Russian-source income.

The draft proposal would introduce an additional criterion to determine the place of corporate residence: the place of effective management and control of the legal entity. As a result, the following legal entities would be deemed to be tax resident in Russia:

- Russian legal entities;
- Foreign legal entities that are considered Russian tax resident based on an applicable tax treaty; and
- Foreign legal entities that have their place of effective management in Russia.

The place of effective management of a foreign legal entity would be considered located in Russia if at least one of the following conditions is satisfied:

- Meetings of the board of directors (or another governing body of the entity) are held in Russia;
- Executive management is carried out in Russia;
- Key managers perform their duties in Russia;
- Accounting books and records are kept in Russia; or
- The entity's archive records are stored in Russia (e.g. archive of accounts, minutes of board meetings).

Under the proposed rule, a legal entity incorporated abroad but managed and controlled from Russia would be subject to unlimited tax liability in Russia (i.e. it would be subject to tax on its worldwide income), since it would be considered a Russian tax resident.

The relatively broad definition of tax residence potentially could create dual residence issues when a company may be subject to unlimited tax liability in two jurisdictions. In accordance with the OECD model treaty, issues involving dual residence generally should be resolved in favor of the jurisdiction where the company's place of effective management is located, although the language of a particular tax treaty could provide otherwise.

CFC rules

A CFC regime would be introduced for the first time, under which a Russian (corporate or individual) taxpayer would be taxed currently on the undistributed profits of controlled companies and structures.
The proposed rules would include:

- A definition of a CFC and controlling persons;
- A definition of control;
- A procedure for determining the profits of a CFC;
- The tax rates applicable to the profits of a CFC;
- Reporting requirements; and
- Tax offenses and penalties.

The CFC rules would apply to Russian resident individuals and legal entities that control foreign companies. Foreign companies for these purposes would include, *inter alia*, companies located in jurisdictions on Russia's blacklist. Control would exist where, due to its participation, a Russian individual/company can, or has the ability to, exercise a decisive influence over the decisions taken by a CFC with respect to the distribution of profits or where, due to participation in a contract, a decisive influence can be exercised over the person who manages the company. The relevant participation threshold would be set at 10% (whether direct or indirect), and the threshold would take into account any interest jointly owned with a spouse, minor children and other persons.

The current version of the draft law issued in March is designed to provide an incentive for companies to distribute dividends to their Russian tax resident shareholders, as opposed to accumulating profits offshore. If profits of a CFC are not distributed, Russian resident individuals would be subject to a 13% tax (rather than the standard 9% personal income tax rate on dividends), and for corporate shareholders, the tax rate would be 20% (rather than the standard 9% tax rate on dividends).

The draft law contains a number of provisions that will require further discussion between the government and the business community:

- A participation threshold of 10% would be used when defining control over foreign companies, which is not in line with the commonly-accepted interpretation of control over the activities of a foreign subsidiary/affiliate. In this regard, CFC legislation in most foreign jurisdictions provides for a participation threshold *exceeding* 10% (with the exception of Kazakhstan and a few other jurisdictions).
- The procedure for determining the profits of a CFC is unclear, as these profits would have to be calculated in accordance with Russian tax accounting rules, but confirmed by the financial statements of the foreign company, which could lead to discrepancies.
- In many foreign jurisdictions, the profits of a CFC subject to taxation typically are limited to passive income. However, the draft Russian law would extend the CFC rules to *any* income received by a company in a low-tax jurisdiction, including income derived from an active commercial activity.
- It was expected that a company in a low-tax jurisdiction that is a subsidiary of a company located in a "reputable" tax jurisdiction would not be recognized as a CFC; however, this provision is not included in the draft law.
- There is not a clear understanding of the list of jurisdictions that provide for "a preferential profits tax regime" that would be targeted by the CFC rules. The draft law refers to a list of countries and territories granting a favorable profits tax regime, approved by the Ministry of Finance, but does not specifically state that the list will be the same as the "blacklist" already approved by the Ministry. Therefore, debates on the possible introduction of a special "extended" list or "grey" list of countries and territories in which companies that are tax residents may be covered by the CFC rules (potentially including certain jurisdictions that typically are not considered tax havens), remain possible.

Taxation of indirect sales of real estate

The March draft law would make significant changes to the taxation of gains on the sale of Russian real estate-rich companies.

Under current rules, capital gains derived by nonresidents are subject to Russian tax only if they sell shares in Russian "real estate-rich" companies (i.e. companies where more than 50% of the assets consist of real property in Russia). The draft law would expand this rule to include capital gains derived by a nonresident from the indirect sale of a domestic or foreign company considered rich in Russian real estate (i.e. cases where a nonresident indirectly owns Russian real estate through one or more entities, and the entity that holds the Russian real estate is sold), except for sales of publicly traded shares. The draft law does not provide a mechanism for withholding of tax on an indirect sale between nonresidents (i.e. the party responsible for reporting taxable transactions or for withholding/remitting tax, etc.), nor does it specify how to determine the value of assets for purposes of the 50% threshold.

Over the last few years, Russia has been actively renegotiating tax treaties that provide protection from the taxation of direct and indirect real estate sales in Russia, and currently there are very few treaties that protect these sales from Russian tax (e.g. some treaties with EU member states, such as Austria, Germany, Hungary and the Netherlands, still offer this protection). The treaties that have been updated to remove this protection give Russia the right to tax income derived from direct or indirect sales of Russian real-estate rich companies (usually either by explicitly including indirect sales or by not explicitly excluding them). It is worth noting that the provisions of the amended treaties that allow the taxation of indirect sales in Russia may not apply until the relevant provisions of domestic legislation have entered into force.

Concept of "beneficial ownership"

Russian tax law currently does not have a formal definition of "beneficial ownership," although this is an area that has been under discussion for some time, and there have been several (unsuccessful) attempts to introduce a draft law on the concept. According to the legislative initiatives announced as a part of the government's action plan related to de-offshoring, it intends to introduce such a definition, along with criteria for applying the provisions of tax treaties.

The tax authorities have become more active in using an interpretation of beneficial ownership in determining whether foreign companies are eligible for reduced rates of withholding tax and other benefits under Russia's tax treaties. Additionally, the Ministry of Finance has issued several clarification letters expressing its own interpretation of "beneficial owner," which generally is in line with the OECD approach:

- Treaty relief should not be granted merely because income was received by an entity with the legal right to that income and the entity is located in a country with which Russia has concluded a tax treaty;
- For purposes of applying tax treaties, the recipient should be the direct beneficiary of the income and should not act as an agent or conduit for another entity that actually benefits from the income; and
- The beneficial owner of the income is the entity with the right to decide what will be done with the income received (the "economic owner," rather than the legal owner).

Unless the recipient of income is recognized as the beneficial owner of the income, reduced withholding tax rates under a treaty would not be granted in Russia.

Based on international practice and on the most recent letter issued by the Ministry of Finance (in April 2014), we assume that the tax authorities may consider the following factors as reasons to challenge the application of tax treaty benefits:

- The foreign company has a contractual obligation, or other legal obligation, to distribute or pay all or most of the income received to a resident of a third country;
- The foreign company has little or no right to control or dispose of the income received;
- The directors of the foreign company have limited powers; and
- The foreign company does not bear economic risks corresponding to its functions.

Deductibility of interest

Although the government's detailed de-offshoring plan does not mention changes to Russia's thin capitalization rules, the deductibility of interest expense in Russia has been an area fraught with controversy in the past few years. There have been several court decisions that have had the effect of expanding the scope of the rules, and the tax authorities are taking a more rigorous approach to the application of the thin cap rules. As a result, the thin cap rules are being tightened, in line with the international trend of imposing and increasing limitations on interest deductions through various anti-abuse mechanisms.

The thin capitalization rules apply to interest paid on a loan obtained from a Russian taxpayer's direct or indirect foreign shareholder that holds 20% or more of the share capital of the taxpayer, a loan obtained from a Russian entity affiliated with the foreign entity or a loan guaranteed by, or for which other security is provided by, such a foreign entity or affiliate. An interest deduction is disallowed if the amount of "controlled debt" of a Russian borrower exceeds a debt-to-equity ratio of 3:1 (or 12.5:1 for banks and leasing companies). In such cases, the excess interest is recharacterized as a dividend subject to a 15% withholding tax (unless the rate is reduced under an applicable tax treaty).

A literal interpretation of the Russian tax code suggests that loans obtained from foreign affiliates should not formally be considered as "controlled" debt for purposes of Russia's thin capitalization rules. However, the Russian tax authorities recently have been applying the rules to such debt. For example, the tax authorities have questioned whether, taken together, the evidence points to the parent company as being the actual lender, with the foreign affiliate being used as a mere conduit to avoid the application of the thin capitalization rules. Structures involving, for example, newly-established special purpose entities lacking local management/business substance and that simultaneously utilize back-to-back financing, may be susceptible to challenges.

In addition to challenges by the tax authorities, there is an emerging trend from the Russian courts on a couple of issues relating to the thin cap rules:

- The possible application of the rules where a loan is granted by a foreign "sister" company and there is evidence that the loan was financed and/or controlled by the parent company (or even with lack of such evidence); and
- The possible application of the rules, even where a relevant tax treaty includes a nondiscrimination provision and specific provisions on unlimited interest deductibility.

Apart from the general deductibility criteria and the thin capitalization rules, the current tax rules provide special limitations applicable to interest expense on debt. If the interest rate deviates by more than 20% from the average interest rate on comparable debt, the interest deductibility is capped at specific levels (depending on the loan currency). Simultaneously, transfer pricing rules also apply to controlled transactions between related parties (and parties deemed to be related). The interaction between these rules is not explicitly provided for by the law. Starting in 2015, interest on nonbanking debt may be deducted without limitation, except for transactions deemed to be controlled for transfer pricing purposes. Therefore, the current limits on the deductibility of interest that are based on the average level of interest on comparable debt no longer will apply.

Transfer pricing

Similar to the OECD action plan, the Russian de-offshoring initiative involves changes to the country's transfer pricing rules. In particular, it is planned that all transactions with parties from "blacklisted" jurisdictions would be considered controlled transactions, regardless of their value. The existing threshold limiting the definition of controlled transactions with unrelated blacklisted parties to transactions with a value exceeding RUB 60 million would be eliminated. Affected taxpayers would be required to prepare and file transfer pricing documentation and submit notifications of the controlled transactions to the tax authorities.

Disclosure of information

The global trend clearly is to expand rules requiring that businesses disclose information and promoting the development of information exchange between jurisdictions. Step 12 of the OECD BEPS action plan proposes the development of recommendations regarding the design of mandatory disclosure rules for transactions, arrangements or structures that are deemed to be aggressive.

Following this trend, Russia is considering improving the transparency regarding the ownership of legal entities and other establishments by requiring businesses to disclose their actual owners in Russia. A draft law published by the Ministry of Finance in April 2013 would require Russian and foreign businesses operating in Russia to disclose their entire chain of beneficiaries (down to the individual level), as well as certain other information. A register of beneficial owners is expected to be introduced, to which the Russian tax authorities would have access. Moreover, the tax authorities are likely to be granted access to information and documents received or formulated by auditors during audits and that are treated as "audit secrets," according to the law.

There also are plans to enhance cooperation and the exchange of tax information with foreign tax authorities. In particular, the OECD Convention on Mutual Administrative Assistance in Tax Matters is expected to be ratified in 2014 (having been signed by Russia in 2011). The convention includes mechanisms for the exchange of information, including simultaneous tax audits and participation in tax audits abroad.

Russia also is likely to apply the new OECD standard for the automatic exchange of information, once it has been developed. In addition, a model intergovernmental tax information exchange agreement is under development, and once approved, will require participating countries to conclude bilateral agreements with blacklisted jurisdictions in order to counteract tax evasion.

Comments

As discussed above, numerous changes to Russian tax law are likely to occur related to the country's de-offshoring policy. These changes have the potential to affect both foreign and domestic business groups. Taxpayers operating in Russia should carefully monitor developments to determine how their businesses may be impacted, and whether any actions to minimize the tax consequences may be appropriate.

— Estella Dzhantukhanova (New York)
Client Service Executive
Deloitte Tax LLP
esdzhantukhanova@deloitte.com

Elena Solovyova (Moscow)
Partner
Deloitte Russia
esolovyova@deloitte.ru

Alexander Krylov (Moscow)
Director
Deloitte Russia
akrylov@deloitte.ru

Kateryna Grynova (Moscow)
Senior Consultant
Deloitte Russia
kgrynova@deloitte.ru

European Union: Netherlands requested to end discriminatory taxation of dividend distributions to insurance companies

The European Commission has requested that the Netherlands end the discriminatory taxation of dividends received on shares held by insurance companies established in another EU member state or in an EEA country (Iceland, Lichtenstein or Norway). The Commission announced on 16 April 2014 that it sent the Netherlands a reasoned opinion (i.e. the second stage of the infringement procedure under the Treaty on the Functioning of the European Union (TFEU)) on the issue.

Dutch law

Under Dutch law, dividends distributed by Dutch resident companies to Dutch resident insurance companies on shares held within the framework of unit-linked insurance effectively are untaxed at the level of the insurance company. The Dutch insurance company must include the dividends received in its tax base, but it is allowed to deduct the increase in the obligation to pay dividends on to its policyholders, and any dividend withholding tax paid is credited against the corporate tax liability. This effectively reduces the corporate tax base for the dividend income to the insurance company to zero.

In contrast, when the insurance company receiving Dutch dividends on shares held within the framework of unit-linked insurance is resident abroad, the gross amount of dividends it receives is taxed. Since the foreign insurance company cannot credit any obligation to pay dividends on to its policyholders against the dividend withholding tax, the foreign insurance company effectively is taxed at a higher rate than a domestic insurance company.

According to the European Commission, the different treatment of domestic and foreign insurance companies constitutes an infringement of the free movement of capital principle in article 63 of the TFEU and article 40 of the EEA agreement, and is not in line with recent case law of the Court of Justice of the European Union (CJEU). Therefore, the Commission has formally asked the Netherlands to amend the legislation so that EU/EEA companies are not treated less favorably than domestic companies.

Comments

The Netherlands has two months to respond to the European Commission’s request; otherwise, the Commission can refer the case to the CJEU.

This is a new dividend taxation issue in an EU context. Although many cases on inbound or outbound dividends already have been referred to the CJEU (either under a preliminary ruling request or as a result of an infringement procedure) and obvious restrictions have been removed from the domestic tax law of various EU member states, the current pending infringement procedure involves a somewhat less obvious form of discrimination. The different treatment of foreign insurance companies in this case mainly is a result of the fact that the Netherlands does not have any right to levy corporate income tax on foreign insurance companies and, therefore, such companies cannot benefit from a deduction. The CJEU, however, has tended to take the position that the taxation of dividends in any cross-border situation cannot be higher than the taxation of dividends in a comparable domestic situation.

— Peter Kavelaars (Rotterdam)
Partner
Deloitte Netherlands
pkavelaars@deloitte.nl

Jasper Korving (Rotterdam)
Manager
Deloitte Netherlands
jkorving@deloitte.nl

France:
Measures announced to promote investment

The French government recently announced that it intends to take steps to attract foreign and domestic investment and to promote France as a strategic investment location. To this end, a series of measures (both tax and nontax) has been identified that should enhance the economic attractiveness of the country, including the following:

- Foreign companies will be able to confirm their tax obligations relating to an investment with the French tax authorities. A foreign investment department will be set up during 2014 to issue guarantees to foreign companies on the tax treatment of their investments.
- To help foreign start-ups set up in France, such companies will have a single entry point of contact with the tax authorities, and foreign subsidiaries of large groups that set up in France will be eligible for loans from the French public investment bank.
- The VAT regime applicable to import companies will be simplified. As from January 2015, companies will be able to defer the payment of the VAT due on imported goods on their VAT return. This option will be available to operators having a centralized customs clearance in place (which allows centralization of the payment of taxes and duties at one place for all imports/exports).
- Import and export customs procedures will be phased out.

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

— Michel Guichard (Paris)
Partner
Taj
mguichard@taj.fr

Odile Courjon (Paris)
Partner
Taj
ocourjon@taj.fr

Bertrand Jeannin (Paris)
Partner
Taj
bjeannin@taj.fr

William Stemmer (Paris)
Partner
Taj
wstemmer@taj.fr

Germany:
New treaty signed with China

China and Germany signed a new tax treaty on 28 March 2014 to replace the current treaty dating from 1985. The new treaty includes significant clarifications and some lower withholding tax rates, and should help facilitate cross-border investment between the two countries. The most notable features of the new treaty are as follows:

- A new 5% withholding tax rate (reduced from 10%) will apply on dividends paid to a corporation that holds directly at least 25% of the shares in the distributing company. A 15% rate will apply on dividends paid to listed REIT companies. The rate in all other cases will be 10%.
- The withholding tax on interest will remain at 10%.
- A 10% withholding tax rate will apply to royalties paid for the use of, or the right to use, a copyright of literary, artistic or scientific work (including film and television royalties); a patent, trademark, design or secret formula; or for information concerning industrial, commercial or scientific experience. The effective withholding tax rate on royalties paid for the use of industrial, commercial or scientific equipment will be 6% (a 10% rate levied on 60% of the gross amount of the royalties), instead of the current 7% rate. The rate in all other cases will be 10%.
- Changes are made to the tax treatment of capital gains from the sale of shares. The current treaty allows such gains to be taxed by the source country, but the new treaty allocates taxing rights to the country where the seller is resident, except in the following cases:
    - Where the capital gains result from the transfer of shares in a real estate-rich entity (i.e. where more than 50% of the assets of the company in which the shares are held directly or indirectly consist of real estate), the capital gains can be taxed by the country where the real estate is located; and

- The source country will have taxing rights on capital gains where the seller directly or indirectly held at least 25% of the shares in the relevant entity during the 12-month period before the transfer. This rule will not apply, however, where gains arise from the transfer of shares in a listed company if the shares transferred by the taxpayer during a tax year do not exceed 3% of the traded shares in the listed company.

- The new treaty includes a welcome clarification of the definition of a services permanent establishment (PE). Under the current treaty, a six-month minimum presence is required to create a services PE, but the new treaty changes this period to 183 days. The six-month rule has resulted in some uncertainty due to different interpretations of the six-month period. The new rule should provide more clarity.
- The duration for a construction site or construction, assembly and connected supervisory activities to create a PE will be extended from six months to 12 months.
- Places where natural resources are extracted will be able to qualify as a PE.
- China will continue to use the credit method for the elimination of double taxation, while Germany will use a modified credit and exemption method. The fictitious 15% withholding tax credit for interest and royalty payments described in the current treaty will be eliminated.
- A new anti-abuse provision is included in the treaty, under which treaty benefits will be denied if certain transactions/arrangements are undertaken to obtain a more favorable tax position and such treatment would be contrary to the object and purpose of relevant clauses of the treaty.

The new treaty will enter into force 30 days after the countries exchange instruments of ratification and will apply as from 1 January of the year following the year the treaty enters into force.

— Andreas Maywald (New York)
Client Service Executive
Deloitte Tax LLP
anmaywald@deloitte.com

Saudi Arabia: Tax bylaws retroactively amended

Saudi Arabia's Minister of Finance has issued a resolution (Minister Resolution No. MR 1776) amending several articles of the tax bylaws. The changes are effective from 19 March 2014 and apply retroactively to cases under appeal or that have not received a final assessment, as well as to all open years under the statute of limitations as of that date.

The amendments include the following measures:

- Payments to nonresident related parties for technical or consultancy services or services for international telephone calls are subject to a 15% withholding tax, rather than a 5% tax. Previously, the application of the higher withholding tax rate had been successfully challenged at the Higher Appeal Committee, but the Department of Zakat and Income Tax (DZIT) had appealed the decision to the Board of Grievance. Rather than waiting for the final decision, the Ministry of Finance amended the law retroactively, and the 15% rate now applies to all open years or years that are under appeal (it is unclear whether the 5% rate applies for closed years).
- Interest paid on loans by branches of foreign banks in Saudi Arabia to their head office abroad is now a tax-deductible expense.
- The DZIT will introduce transfer pricing rules that will specify the criteria for transactions between related parties to be considered carried out at fair value or at an arm's length basis, in accordance with international standards. The transfer pricing rules are expected to be in line with the OECD guidelines.
- New definitions have been added to clarify the calculation of the tax base of branches of airlines, land transportation companies and sea freight companies (5% of the total revenue realized from operations in Saudi Arabia), and to remove potential contradictions between the tax law and the bylaws.
- The deemed profit rate for small entities with limited income that are not required to maintain accounting records has been changed and now may vary from 10% to 80%, based on the nature of the activity (previously, the deemed profit rate was 15%).
- When shares in a company are sold, the buyer and seller are equally responsible for reporting the sale to the DZIT and settling the capital gains tax due within 60 days of the sale (previously, the company, buyer and seller were

jointly liable). The buyer may be held liable for any unsettled capital gains tax if the sale transaction is not reported within the 60-day limit. The seller no longer is required to settle the tax on profits for the period before the sale.

- Interest on interbank deposits is exempt from tax if the deposits remain with a local borrower bank for no more than 90 days and the borrower bank submits an annual statement that meets certain specified requirements. Clarification is needed as to whether this relief applies to branches of foreign banks in Saudi Arabia and whether it is available to other financial institutions.
- The DZIT's rights to obtain information from taxpayers and nontaxpayers with respect to the application of Saudi tax law and/or an applicable tax treaty are increased. Such persons must provide the DZIT with basic details of contracts for services, etc.
- The DZIT's powers to require individual and corporate taxpayers to cooperate and submit requested information during a field inspection have been increased. Penalties apply for failure to comply.

— Nauman Ahmed (Al Khobar)
Senior Director
Deloitte Saudi Arabia
nahmed@deloitte.com

Osama Nobani (Riyadh)
Senior Director
Deloitte Saudi Arabia
onobani@deloitte.com

Farhan Farouk (Jeddah)
Senior Director
Deloitte Saudi Arabia
ffarouk@deloitte.com

United Kingdom:
New policies affect PAYE reporting for employees on short-term business visits to the UK

In view of stricter HM Revenue & Customs (HMRC) compliance requirements, employers in the UK that currently do not have a valid Short-Term Business Visitor Agreement (STBVA) with HMRC may wish to consider the benefits of applying for one by 31 May 2014.

Generally, an STBVA is available only for individuals meeting the following requirements:

- Coming to work in the UK for a UK company or the UK branch of an overseas company;
- Expected to stay in the UK for 183 days or less in any 12-month period;
- Who either have not become UK resident for tax purposes or who, if UK resident, are also considered resident in a treaty partner country under the applicable treaty;
- Subject to a tax treaty with the UK under which the dependent personal services/income from employment article is likely to apply; and
- It can be shown that the UK company or branch will not ultimately bear the remuneration specified for the individual.

All employers with employees who visit the UK on short-term business may wish to review their procedures for the 2013/14 tax year and subsequent years, in view of HMRC's updated approach, described below.

Changes to HMRC policies

HMRC has confirmed that, with effect from 6 April 2013, where a UK business has a Pay As You Earn (PAYE) reporting and withholding obligation in relation to a Short-Term Business Visitor (STBV) to the UK that can be discharged through a valid claim under a tax treaty, the UK business is required to operate PAYE from day one of the visit to the UK, unless the business has a valid STBVA in place.

Previously, HMRC allowed employers to determine on a unilateral basis whether a STBV was exempt from UK tax under the terms of the relevant tax treaty, and to operate PAYE only where an exemption would not apply to discharge that liability – provided the employers accepted that, in the event of any intervention from HMRC, they would need to produce this evidence. While HMRC has confirmed that this previous practice may apply up to and including 5 April 2013, this approach has been withdrawn for the 2013/14 UK tax year (6 April 2013 – 5 April 2014) and thereafter.

HMRC has indicated that, as from the 2013/14 tax year, where it discovers that UK employers have adopted a unilateral approach, it will seek to recover PAYE deductions unless the employers provide complete self-assessment tax returns for each employee, containing valid treaty claims for each of the STBVs.

Considerations for employers

Employers that do not have an STBVA in place for the 2013/14 tax year have until 31 May 2014 to apply for an agreement and submit a full report for this tax year, in accordance with the terms of the STBVA. In other words, for the 2013/14 tax year only, the application and the required report can be submitted at the same time. For all future years, any new application for an STBVA must be made by the end of the relevant tax year, and the required report submitted by 31 May following the end of the relevant tax year.

As part of obtaining an STBVA, HMRC will require that the employer put in place some form of internal reporting system to keep as accurate as possible a record of the employees visiting the UK on business that are covered by the agreement. It is expected that this system will have the following minimum requirements:

- Employees would be required to periodically report days spent in the UK on business to the UK business's central point controlling this arrangement; and
- Employees should not spend more than 30 days intermittently in the UK in any 12-month period without reporting to that central point.

These expected requirements would aim to support the submission of the year-end report of employees for whom any PAYE reporting obligation has been relaxed. This report would detail the additional information required for each employee, which would depend upon the period of their visit to the UK (1 to 30 days, 31 to 60 days, 61-90 days, 91-150 days, 151-183 days, etc.).

An STBVA will not be available in situations in which an employee's remuneration ultimately is borne by the UK company. That said, the OECD commentary to the model treaty provides examples of situations where the UK company would not be regarded as the "economic employer," and a treaty exemption therefore may still apply. In such cases, a separate claim under the treaty should be made.

Comments

As a result of HMRC's revised approach, STBVs now present a potential increased PAYE risk to businesses in the UK. This approach has direct implications for the obligations placed on UK businesses and, potentially, for the obligations on individuals covered under the Senior Accounting Officer (SAO) regime. Under this regime, the SAO is required to establish and maintain appropriate tax accounting arrangements, and to certify that such arrangements have been in place throughout the company's financial year. HMRC may expect that tax accounting arrangements should include those arrangements in place for tracking STBVs and ensuring that the company meets its PAYE obligations in relation to such individuals.

Employers that do not have a STBVA for the 2013/14 tax year may wish to apply for one by 31 May 2014. In this case, steps should be taken to ensure that the required reports also can be submitted by this date.

With the proposed withdrawal of personal allowances for certain UK nonresidents from April 2015, these changes may mean that the cost to employers of compliance errors is likely to rise.

— Matt Ellis (London)
Partner
Deloitte United Kingdom
maellis@deloitte.co.uk

James Macpherson (London)
Partner
Deloitte United Kingdom
jmacpherson@deloitte.co.uk

In brief

European Union – The Court of Justice of the European Union has ruled on the difference in tax treatment in Poland between dividends paid to resident and nonresident investment funds, concluding that an EU member state cannot exclude dividends paid to an investment fund in a nonmember state from a tax exemption where a resident fund would have been exempt.

European Union – The European Commission has issued explanatory notes to help businesses prepare for the new VAT rules that apply as from 1 January 2015. As from that date, supplies of telecommunications, broadcasting and electronically supplied services (e-services) made by EU suppliers to private individuals and nonbusiness customers will be taxable in the EU member state of the customer. The Commission's notes are not legally binding and only provide practical and informal guidance about how EU law should be understood and applied. The notes should be read in conjunction with the Commission's guide to the VAT "one stop shop."

Greece – Effective 7 April 2014, the 1% capital tax levied upon the incorporation of an entity (e.g. corporation, partnership, joint venture, etc.) is abolished, but capital tax continues to apply to an increase in share capital.

Italy – It has been confirmed that the 8.5% surcharge to the corporate income tax that applies to companies and organizations operating in the banking and insurance sectors does not apply to "industrial holding" companies (i.e. companies that exclusively or primarily carry out activities such as the holding of participations in companies engaged in businesses other than banking and financing and that draft their financial statements in accordance with the Italian Civil Code), even if such companies are engaged in financing activities with respect to other companies in the group.

OECD – The OECD has published the final text of the common reporting standard for multilateral information exchange, with 41 jurisdictions having committed to its early implementation. The commentary to the standard still is under discussion at the OECD. The new standard draws extensively on earlier work of the OECD in the area of automatic exchange of information. It incorporates progress made within the EU, as well as global anti-money laundering standards. The standard would require jurisdictions to obtain information from their financial institutions and automatically exchange that information with other jurisdictions on an annual basis. It sets out the financial account information to be exchanged, the financial institutions that need to report and the different types of accounts and taxpayers covered, as well as common due diligence procedures to be followed by financial institutions. The standard has been developed jointly by the OECD and G20 countries.
URL: http://www.oecd.org/ctp/exchange-of-tax-information/automatic-exchange-of-financial-account-information.htm

Poland – The Ministry of Finance published a document on its website on 27 February 2014 entitled "Business restructuring between related parties," which sets out the ministry's interpretation of the business restructuring provisions in the transfer pricing rules that became effective in July 2013. The document explains how the ministry views key elements of the business restructuring regulations, indicates areas that will be of particular interest and provides the methodology the tax authorities should apply in analyzing business restructuring cases.

United Kingdom – HM Treasury has issued a consultation on charging UK capital gains tax on the disposal of UK residential property by nonresidents. One aspect will affect UK residents, namely, a proposal to abolish the election allowing a taxpayer to choose which of two (or more) residences is the principal residence and, therefore, exempt from capital gains tax. Instead, a facts-based test may be introduced. The "absence rules" (which, for example, provide relief where individuals need to be away from their main home for work or other reasons) would be unaffected. Any change would take effect from April 2015.

Tax treaty round up

At the end of each month, the *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-United Kingdom – A second protocol to the treaty was signed on 13 March 2014. The protocol clarifies that the amendments to the 1987 treaty by the 2010 protocol apply not only to federal taxes, but also to those taxes applied by the Belgian regions (Brussels-Capital, Flemish and Walloon regions) and the communities (Flemish, French and Germanspeaking). The protocol further confirms that the regional and communal Finance Ministers are recognized as "competent authorities."

Canada-Hong Kong – The 2012 tax agreement entered into force on 29 October 2013 and applies as from 1 April 2014 in Hong Kong and from 1 January 2014 in Canada. The 5% rate applies where dividends are paid to a company (other than a partnership) that controls, directly or indirectly, at least 10% of the capital of the distributing company; otherwise, the rate is 15%. The rate on interest and royalties is 10%.

China-Germany – See article in this issue.
URL: http://newsletters.usdbriefs.com/2014/Tax/WTA/140425_4.html

Denmark-Ghana – When in effect, the treaty signed on 20 March 2014 provides for a 5% rate where dividends are paid to a company (other than a partnership) that holds directly at least 10% of the capital of the distributing company or where the beneficial owner is the other contracting state or the central bank of that other state, or any national agency or any other agency (including a financial institution) owned or controlled by the government of that other state; otherwise, the rate will be 15%. The rate on interest will be 8%, with exemptions for interest paid to a pension fund or other similar institution providing pension schemes in which individuals may participate in order to secure retirement benefits, where such pension fund or other similar institution is established and recognized for tax purposes in accordance with the laws of the other contracting state; or interest paid in connection with the sale of any merchandise or equipment on credit. The treaty provides for an 8% rate on royalties.

Germany-United Kingdom – A protocol to the treaty was signed on 17 March 2014 that brings in the application and interpretation of the new article 7 (business profits) to the OECD model treaty and harmonizes the taxation rights under the government service and diplomatic missions articles with article 14 of the Consular Convention of 30 July 1956 between Germany and the UK. The protocol will enter into force once both countries have completed their legislative procedures.

Hong Kong-Guernsey – The 2013 treaty entered into force on 5 December 2013 and applies as from 1 April 2014 in Hong Kong and as from 1 January 2014 in Guernsey. Dividends and interest are taxable only in the state of residence of the recipient. A 4% withholding tax rate applies to royalties.

Hong Kong-Kuwait – The 2010 treaty entered into force on 24 July 2013 and applies as from 1 April 2014. The rate on dividends, interest and royalties is 5%.

Hong Kong-Mexico – The 2012 treaty entered into force on 7 March 2013 and applies as from 1 April 2014 for Hong Kong and 1 January 2014 for Mexico. Dividends are taxed only in the state of residence of the recipient. The 4.9% rate applies to interest paid to a bank; otherwise, the rate is 10%. The rate on royalties is 10%.

Hong Kong-Qatar – The 2013 treaty between Hong Kong and Qatar entered into force on 5 December 2013 and applies as from 1 April 2014 in Hong Kong and as from 1 January 2014 in Qatar. Dividends and interest are exempt from withholding tax, and a 5% rate applies to royalties.

India-Albania – The 2013 treaty entered into force on 4 December 2013 and applies as from 1 April 2014 in India and as from 1 January 2014 in Albania. The treaty provides for a 10% withholding tax on dividends, interest and royalties.

India-Latvia – The 2013 treaty entered into force on 28 December 2013 and applies in India as from 1 April 2014 and in Latvia as from 1 January 2014. A 10% withholding tax rate applies to dividends, interest and royalties.

India-Malta – The 2013 treaty and protocol entered into force on 7 February 2014 and apply in India as from 1 April 2014 and in Malta as from 1 January 2015. The treaty provides that where dividends are paid by a Malta company to an Indian company, the Maltese tax on the dividends may not exceed the amount chargeable on the profits out of which the dividends are paid. The rate is 10% for dividends paid by an Indian company. The rate on interest and royalties also is 10%.

India-Romania – The 2013 treaty to replace the treaty dating from 1987 entered into force on 16 December 2013 and applies as from 1 April 2014 in India and as from 1 January 2014 in Romania. The treaty provides for a 10% withholding tax rate on dividends, interest and royalties (as well as technical service fees).

India-Sri Lanka – The 2013 treaty to replace the treaty dating from 1982 entered into force on 22 October 2013 and applies as from 1 April 2014. The treaty provides for a 7.5% withholding tax on dividends and a 10% rate on interest and royalties (as well as technical service fees).

India-Uruguay – The 2011 treaty entered into force on 21 June 2013 and applies in India as from 1 April 2014 and in Uruguay as from 1 January 2014. The treaty provides for a 5% withholding tax on dividends and a 10% rate on interest and royalties.

Luxembourg-Sri Lanka – The 2013 treaty entered into force on 11 April 2014 and will apply as from 1 January 2015. When in effect, the treaty provides for a 7.5% withholding tax on dividends paid to a company (other than a partnership) that holds directly at least 25% of the capital of the payer company; otherwise, the rate will be 10%. The rate on interest and royalties will be 10%.

Malta-Moldova – When in effect, the treaty signed on 10 April 2014 provides that where dividends are paid by a Malta company to a Moldova company, the Maltese tax on the dividends may not exceed the amount chargeable on the profits out of which the dividends are paid. The rate will be 5% for dividends paid by a Moldova company to a Malta company. The rate on interest and royalties will be 5%.

Peru-Portugal – The 2012 treaty entered into force on 12 April 2014 and will apply as from 1 January 2015. When in effect, the treaty provides for a 10% withholding tax on dividends paid to a company (other than a partnership) that holds directly at least 10% of the capital of the payer company where the recipient company is a resident of Portugal or 10% of the voting power of the payer company where the recipient company is a resident of Peru; otherwise, the rate will be 15%. Interest paid on a bank loan will be taxable at a maximum rate of 10%; otherwise, the rate will be 15%. A 10% rate will apply to royalties paid for technical assistance in connection with the use of, or the right to use, a copyright of literary, artistic or scientific work (including computer software, cinematographic films and other means of audio or video reproduction) or a patent, trademark or secret formula or for industrial, commercial or scientific information; otherwise, the rate will be 15%.

Singapore-Sri Lanka – When in effect, the treaty signed on 3 April 2014 to replace the current treaty dating from 1979 provides for a 7.5% rate on dividends paid to a company that holds directly at least 25% of the capital of the payer company; otherwise, the rate will be 10%. A 0% rate will apply to interest paid to a banking or financial institution of a contracting state; otherwise, the rate will be 10%. The rate on royalties will be 10%.

Slovakia-Kuwait – The 2012 treaty entered into force on 21 April 2014 and will apply as from 1 January 2015. When in effect, the treaty provides that dividends may be taxed only in the state of residence of the recipient. A 10% withholding tax will apply to interest and royalties.

Spain-United Kingdom – The 2013 treaty to replace the treaty dating from 1975 enters into force on 12 June 2014 and applies in Spain as from 12 June 2014 for withholding taxes and as from 1 January 2015 for income and other taxes; it applies in the UK as from 12 June 2014 for withholding taxes, as from 1 April 2015 for cooperation taxes and as from 6 April 2015 for income and capital gains taxes. When in effect, the treaty provides that a 0% rate will apply where dividends are paid to a company that controls, directly or indirectly, at least 10% of the capital of the distributing company or where the dividends are paid to a pension scheme; a 15% rate will apply where the dividends are paid out of income (including gains) derived, directly or indirectly, from 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%. Interest and royalties will be taxable only in the state of residence of the recipient.

United States – Intergovernmental agreements (IGAs) to improve international tax compliance and to implement the Foreign Account Tax Compliance Act (FATCA) have been signed between the US and Luxembourg (on 28 March 2014), Honduras (on 31 March 2014) and Estonia (on 11 April 2014); a new IGA was signed between the US and Mexico (on 9 April 2014) to replace the previous agreement signed on 19 November 2012. The Luxembourg and Honduras IGAs both are based on the Model 1A IGA. The Luxembourg IGA includes certain modifications related to written notifications to be exchanged between the competent authorities of the signatory countries with respect to safeguards to ensure the confidentiality of the information and infrastructure for an effective exchange relationship. The Honduras IGA requires reporting of the average monthly account balance or value of each reportable US account or, if the account was closed during the year, the average monthly balance for the calendar year up to the time of closure.

United States – The US Treasury Department has announced that it will treat more than a dozen countries (Australia, Austria, Belgium, Brazil, British Virgin Islands, Croatia, Czech Republic, Gibraltar, Jamaica, Korea (ROK), Kosovo, Latvia, Liechtenstein, Lithuania, New Zealand, Poland, Portugal, Qatar, Romania, Slovenia and South Africa) that have agreed in substance on the terms of an intergovernmental agreement (IGA) with the US as having signed bilateral agreements that will be deemed active for FATCA purposes until 31 December 2014 (the date by which an IGA must be signed in order for this status to continue without interruption). Additional jurisdictions may be added to this list.

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Chile
Sweeping tax reform bill presented to congress
Chile's new president presented a comprehensive tax reform bill to the national congress on 1 April 2014. The proposed reform – which is broader than anticipated – includes many changes that would have an effect on companies doing business in the country, including a gradual increase in the corporate income tax rate, new restrictions on interest deductions, and the introduction of CFC rules and a GAAR.
Issue date: 17 April 2014
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-chile-170414.pdf?id=us:em:na:wta:eng:tax:042514

Denmark
National Tax Board issues favorable ruling on PE and anti-avoidance rules
Denmark's National Tax Board published a binding ruling on 25 March 2014, in which it confirmed that foreign owners investing though a Danish partnership did not have a permanent establishment in Denmark and that the partnership was not taxable under Danish tax law.
Issue date: 12 April 2014
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-denmark-120414.pdf?id=us:em:na:wta:eng:tax:042514

France
Tax authorities issue draft comments on anti-hybrid rule
On 15 April 2014, the French tax authorities issued long-awaited draft comments on the new anti-hybrid rule that limits the deductibility of interest paid to related entities. Although the comments do not resolve all issues relating to the anti-hybrid rule, they provide some welcome clarifications.
Issue date: 17 April 2014
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-france-170414.pdf?id=us:em:na:wta:eng:tax:042514

Iceland
Iceland Introduces New Transfer Pricing Rules
Iceland's Parliament on 1 January 2014, adopted the OECD's Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations into Iceland's Income Tax Act. Regulations to provide additional guidance on documentation are currently being drafted.
Issue date: 14 April 2014
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-tpalert-2014-007-140414.pdf?id=us:em:na:wta:eng:tax:042514

Italy
Italy Clarifies, Amends Transfer Pricing Rules
Italy's Finance Act for 2014 delivered a long-awaited clarification on the applicability of the Italian Regional Tax on Business Activities (IRAP) to transfer pricing adjustments, and introduced changes to the transfer pricing rules applicable to businesses involved in online advertising.
Issue date: 14 April 2014
URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-tpalert-2014-008-140414.pdf?id=us:em:na:wta:eng:tax:042514

Switzerland

Cantons announce lower headline tax rates in anticipation of Corporate Tax Reform III

In anticipation of the Swiss "Corporate Tax Reform III," several cantons have announced a reduction of their headline tax rates and others are likely to follow suit in the near future.

Issue date: 15 April 2014

URL: http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-alert-switzerland-150414.pdf?id=us:em:na:wta:eng:tax:042514