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International Tax

World Tax Advisor

10 October 2014

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Canada's new proposed legislation released on cross-border financing and foreign affiliate dumping

Canada's Department of Finance released draft legislation on 29 August 2014 to implement back-to-back financing proposals and numerous other budget measures, and to revise its 16 August 2013 draft amendments to the foreign affiliate "dumping" rules.

The 11 February 2014 Canadian federal budget contained two proposals relating to inbound investment into Canada: an anti-treaty shopping rule and amendments to the thin capitalization and withholding tax rules with respect to debt owed to an intermediary that is backed by loans or certain asset pledges (that may be characterized as the economic equivalent of loans) of non-arm's length nonresidents (the "back-to-back financing proposals"). Both proposals were the subject of extensive consultations.

The Department has announced that after consultations on the proposed anti-treaty shopping rule, the government "will instead await further work" by the OECD and G-20 in relation to their base erosion and profit shifting (BEPS) initiative. It is unclear whether the government has decided to shelve its domestic law proposals or merely to fine tune them once the BEPS

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proposals are further advanced (even though there was little-to-no support for a domestic law approach in the BEPS draft report on the treaty abuse action item).

The back-to-back financing proposals and the foreign affiliate dumping rules contained in the 29 August legislation are described below. It is anticipated that, after a short consultation period, the legislation will be introduced in the House of Commons and passed before the end of 2014.

Back-to-back arrangements

The thin capitalization rules currently do not apply to a loan to a taxpayer from an arm's length lender (intermediary), except in limited circumstances where such a loan is made because a non-arm's length nonresident made a loan to the intermediary "on condition" that the intermediary make a loan to the taxpayer (back-to-back loans). Interest paid to an arm's length lender generally is exempt from withholding tax even where a back-to-back loan is deemed to exist for purposes of the thin capitalization provisions. The budget contained proposals to expand the scope of the existing back-to-back loan rule in the thin capitalization rules and to add a similar rule to the nonresident withholding tax rules.

The expansion in the budget proposal was larger than initially appeared obvious in the budget explanation. The budget proposed that the back-to-back loan rule generally would apply where a taxpayer owes a debt to an intermediary in circumstances where the intermediary has received a loan from a nonresident person "on condition" that the intermediary make a loan to the taxpayer (as under the existing rule), as well as in cases where the intermediary is indebted to a nonresident person under a limited recourse debt or the intermediary has been pledged a property by a nonresident person as security for the debt. In such cases, the debt would be treated as owed to the nonresident person for purposes of the thin capitalization rules, and interest could be treated as having been paid to such person for purposes of the withholding tax rules.

The budget measures, particularly their application to situations where assets are pledged, were excessively broad. It is standard practice for third-party lenders to require that assets of related persons within a corporate or commercial group be pledged as security. In certain cases, the property in question is actually the shares of the Canadian debtor, since this makes it easier for the lender to enforce its rights as creditor to the Canadian entity. Even a Canadian multinational could be subject to the budget's proposed rules in respect of its borrowings from a third party lender, to the extent that the assets of its foreign subsidiaries have been pledged to secure the borrowing.

The proposed rules with respect to the provision of security to an intermediary by a nonresident have been significantly narrowed under the 29 August proposed legislation. Under the new draft legislation, the provision of security would invoke the back-to-back rules only to the extent the intermediary has the right to "use, mortgage, hypothecate, assign, pledge or in any way encumber, invest, sell or otherwise dispose of, or in any way alienate, the property" (defined as a "specified right").

Because the nature of a specified right would be such that the intermediary could obtain financing on the security of the property or dispose of the property, the explanatory notes accompanying the draft legislation characterize a specified right as the economic equivalent of

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a loan but provide that the mere provision of a security interest in a property of a nonresident would not constitute a specified right (presumably on the basis that, absent default on the debt by the taxpayer, the intermediary could not encumber or dispose of the property).

In addition, to invoke the back-to-back rules, the existence of the specified right would have to be required under the terms and conditions of the debt, or it would have to be reasonable to conclude that, in the absence of the specified right, the debt would not be outstanding or would contain different terms and conditions.

A new de minimis rule proposes to prevent the application of the back-to-back rules if the amount of support provided by the nonresident(s) for the borrowing through a back-to-back loan or the granting of a specified right generally is less than 25% of the taxpayer's total borrowing. For example, if the taxpayer has borrowed CAD 100 million from the intermediary and the intermediary has received a loan and/or specified right from the taxpayer's nonresident parent company in an amount of less than CAD 25 million, the back-to-back rules would not apply. The de minimis rule also would take into account circumstances in which the taxpayer and the intermediary are parties to a credit facility involving multiple related borrowers. If the support provided by the parent, for example, is less than 25% of the total of the taxpayer's debt and debts of the other non-arm's length borrowers under the facility, the rules would not apply.

These changes to the proposed rules should significantly alleviate the concerns of taxpayers with respect to many common borrowing arrangements, at least in circumstances where the taxpayer is not in default.

The new proposals in the 29 August legislation are more restrictive than the budget measures in one respect. They would expand the existing conditional loan rule to apply to a loan made by the intermediary that is dependent on a loan received by the intermediary and to circumstances where it is reasonable to conclude that the loan would not have been made to the taxpayer (or the terms and conditions of the loan would not have been the same) if the intermediary was not provided the support of the nonresident(s), whether through a loan or the provision of a specified right.

A number of technical changes also have been made to the proposed rules. It is now clear that if interest is not deductible as a result of the application of the back-to-back rule in the thin capitalization provisions, the rule that deems such interest to be a dividend and subject to dividend withholding tax would take precedence over the back-to-back rule that would have levied withholding tax at the rate applicable to interest. Thus, for example, where the nonresident is a US person, the back-to-back loan rule in the withholding tax context should have no practical effect (provided the person is a qualifying person under the limitation on benefits article in the Canada-US Treaty), except to the extent interest would be deemed to be a dividend as a result of the application of the thin capitalization rules. (Interest paid to US treaty residents generally is exempt from withholding tax, unlike dividends.)

The thin capitalization rules also are proposed to be amended to exclude debt owing to non-arm's-length Canadian residents from the back-to-back rules. This change should eliminate the long-standing need for administrative relief in respect of funds loaned to a Canadian holding company, for example, where those funds are "on-lent" to a Canadian operating company with which the Canadian holding company does not deal at arm's length. If the thin capitalization rules applied to the operating company, in many cases, the operating company would not have

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sufficient equity for purposes of the thin capitalization rules, and a portion of the interest would be disallowed.

While the focus of the consultations has been on third-party financing, the expanded wording in the proposed rules makes it more likely that the back-to-back rules would apply to loans received from related intermediaries (other than non-arm's length Canadian residents). For example, a nonresident parent company may make a loan to a nonresident subsidiary that makes a loan to a Canadian subsidiary. Assume that the withholding tax rate on interest is lower under the treaty between Canada and the country of residence of the intermediary than it is between Canada and the country of residence of the parent company. In this case, the thin capitalization rules would apply in respect of the loan received from the intermediary and the arrangement would not be recharacterized under the back-to-back rules for thin capitalization purposes; however, the back-to-back rules could apply, depending on the terms of the arrangement, to deem the taxpayer to make the interest payments on the loan from the intermediary to the nonresident parent company, and subject the payments to a higher rate of withholding tax. The expanded wording of the provision no longer would restrict its application to circumstances in which the loan from the parent to the intermediary was made "on condition" that the intermediary make a loan to the Canadian subsidiary.

The proposed changes to the thin capitalization rules would apply to taxation years that begin after 2014 and the proposed changes to the withholding tax rules would apply to amounts paid or credited after 2014.

Foreign affiliate dumping

The foreign affiliate dumping rules became law in 2012, effective generally for investments in foreign affiliates made after 28 March 2012. A package of technical amendments to the rules was released for consultation on 16 August 2013. The 29 August 2014 legislation contains revised proposals in response to those consultations. These proposals are quite technical in nature and generally reflect either further refinements to the scope of the rules or new approaches to dealing with certain aspects of the rules.

The foreign affiliate dumping rules generally apply to an investment in a foreign affiliate made by a corporation resident in Canada (referred to as a CRIC) that is or becomes controlled by a nonresident corporation (referred to as the parent). The general rule subjects the investment to withholding tax on the basis that it is deemed to be a dividend paid by the CRIC to the parent, although, in some circumstances, the dividend can be deemed to have been paid by a related Canadian company (a qualifying substitute corporation or QSC) or the paid-up capital (PUC) of the shares of the CRIC or the QSC can be reduced in lieu of the deemed dividend.

Some of the changes in the 29 August 2014 proposed legislation include:

- Amendments to clarify whether a deemed dividend arises and the timing of the deemed dividend, particularly in circumstances where the CRIC becomes or ceases to be controlled by a nonresident person over a period of time that includes the investment in the foreign affiliate by the CRIC;
- Substantial revisions to the rules that allow the PUC reduction to occur in lieu of the deemed dividend, including a new anti-avoidance rule to deal with the potential

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inappropriate enhancement of PUC through the use of holding companies, and the clarification of filing requirements;
- Revisions to the rules that allow the PUC to be reinstated in certain cases upon the unwinding of the investment in the foreign affiliate; and
- Revisions to the rules relating to the reorganization of foreign affiliate investments.

In particular, taxpayers should be aware that the PUC reduction in lieu of a deemed dividend would be, once again, effectively an elective rather than an automatic provision. The legislation in this respect has changed several times, as have the substantive rules. The 16 August 2013 legislation proposed the filing of a prescribed form with the Canada Revenue Agency (CRA), detailing how the reduction of PUC was to be applied, but there were no stated consequences for not filing the form or filing it late, and the CRA has not yet issued the form. The legislation now specifies that, in addition to the PUC reduction, there would be a separate deemed dividend equal to the amount of the PUC reduction if the form is not filed on time. While a mechanism would be provided to refund any tax paid in respect of this deemed dividend if the form is filed late and written application is made to the Minister of National Revenue, substantial penalties and interest may arise. Election forms would be deemed to be filed on time if filed within 30 days of the 29 August legislation receiving Royal Assent.

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UK tax authorities challenging VAT recovery by head offices

There have been several significant developments affecting the approach of the UK tax authorities (HM Revenue & Customs, or HMRC) to challenging the recovery of VAT incurred by UK head offices on costs. HMRC is proactively reviewing VAT recovery arrangements – in particular, in the mining and exploration sectors – and further activity is expected for other sectors in the near future.

Recovery of VAT by head office companies

Many head office functions involve the provision of services to related group companies. Performing services that are treated as taxable supplies for VAT purposes generally provides head offices the right to recover VAT incurred on related expenditure. However, many UK head offices are part of VAT groups with other UK entities that also carry on taxable activities. On this basis, head offices may be recovering VAT incurred on their costs in full, even where they may not be considered to be conducting any taxable activities for VAT purposes themselves. HMRC is challenging this approach and proactively identifying companies it believes have been over-recovering VAT during the past four years (the period open under the UK statute of limitations).

Case law developments

HMRC's renewed focus in this area results from two recent decisions by the UK First-tier Tribunal (FTT) in the cases of *Norseman Gold Plc* and *African Consolidated Resources Plc.*

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Both cases involved the effectiveness of management service agreements in supporting the recovery of VAT incurred on costs by UK head offices in providing management services to subsidiaries in the group. The FTT held that a combination of the following factors would make it difficult for the head office to substantiate that it was providing services:

- A lack of documentation and/or poor documentation of the management service agreement;
- Doubts as to the effective practical execution of the services documented in the agreement;
- Vagueness about when the payments would be made for the services provided and/or the exact nature of the services being provided; and
- A lack of a clear connection between the value of the services provided and the value of the management fees.

In both cases, the FTT concluded that the management services provided by the UK head offices to their subsidiaries did not constitute supplies of services for VAT purposes. Accordingly, there was no basis for VAT recovery on related expenditure.

Another important legislative precedent is the 2013 UK Court of Appeal's decision in the *BAA Limited* case. In this case, the court held that a company that was established to make an acquisition was not carrying on an economic activity at the time it incurred VAT on its expenditure because its management services were not being provided at that time, and there was insufficient evidence to prove an intention to provide such services in the future. Therefore, the VAT incurred was instead a cost related to a non-business activity (i.e. the passive holding of investments), and accordingly it was deemed to be irrecoverable.

While case law still is evolving in this area (e.g. *Norseman Gold* is being appealed by the taxpayer), HMRC already has started to investigate the VAT recovery arrangements of many head office businesses, and to raise assessments for over-recovered VAT. These can be upwards of GBP 2 million of VAT over the course of a four-year period.

Concept of "cost component"

Even where management services genuinely are provided and this is evidenced by well-executed contracts, HMRC is looking closely at situations where the value of VAT that is being recovered on costs appears disproportionately large compared to the value of the onward taxable supplies. To the extent costs on which VAT is incurred do not form a "cost component" of the onward supplies made by the head office, HMRC may consider that VAT on such costs is irrecoverable (e.g. because they do not directly relate to taxable supplies, such as the recharge of those costs). Therefore, additional risk factors that may lead to an investigation by HMRC include the following:

- Significant levels of UK VAT being incurred by a head office, with a comparatively modest charge made to group entities; and
- Costs being incurred by a head office in relation to the entire corporate group, where corresponding service charges are not passed on to all members of that group.

Any business with these risk factors should consider its current VAT recovery position, as well as the positions taken in the past four years.

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Potential actions to mitigate risk

Many head office companies actively carry out services for group entities; however, these are not always sufficiently documented and charged to the same extent as supplies to third parties.

Steps may be taken to arrange and clearly document the taxable activities of head offices, to support the recovery of VAT. Companies with long-standing intercompany service agreements should consider reviewing these to assess whether they are appropriate to cover any charges in the group – including review of the group structure, the costs incurred at a head office level and the services provided throughout the corporate group – so that the reasons HMRC used to challenge VAT recovery in *Norseman Gold* and *African Consolidated Resources* will not apply.

For businesses currently at risk, decisions may need to be made about VAT recovery going forward, as well as assessments of any risks relating to VAT recovery in the past. Businesses may want to consider this matter sooner rather than later (if possible, before HMRC makes inquiries) to allow them to make any changes that could help to safeguard the VAT position.

While this development comes from the UK, businesses should also consider the VAT recovery status of holding companies in other EU member states, given the challenges currently being raised by HMRC.

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China: SAT responds to BEPS

On 17 September 2014, China's State Administration of Taxation (SAT) issued a press release related to the deliverables of the OECD BEPS actions, in which it acknowledged the unavoidable and practical impact of the BEPS initiatives on tax administration in China and that the tax authorities in China will face pressure in fulfilling its corresponding obligations, regardless of the final output of the various BEPS actions.

In the release, the SAT observes that global initiatives allow for a more equitable result by aligning taxation with value creation in a fair and transparent way. As such, the SAT stated that it is important for China to continue to actively participate in these developments to ensure equitable transfer pricing enforcement through an appropriate legislative and administrative framework, as well as international cooperation.

On 25 September, the SAT organized a conference to further discuss its view of BEPS actions with corporate taxpayers and advisers. During the conference, the SAT reiterated its general

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support for the BEPS initiatives, and laid out some important upcoming developments with respect to BEPS:

- Circular No. 2, Measures of Special Tax Adjustments (Trial), which deals with adjustments under the general anti-avoidance rule, transfer pricing and the controlled foreign company and thin capitalization rules, is being revised. The SAT will release a draft for public comments before the end of 2014, and the final rule likely will come out in early 2015.
- The SAT has an internal timetable that corresponds to the OECD timetable. Generally speaking, the SAT should be able to formulate its reaction approximately six to nine months after each OECD recommendation is released.
- The SAT will post on its website a list of what it considers as "unacceptable behavior," which will be the focus of future transfer pricing audits.

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Germany:
Local tax court rules on RETT intragroup restructuring exemption rule

The Local Tax Court of Duesseldorf ruled on 7 May 2014 that the real estate transfer tax (RETT) intragroup restructuring exemption rule applies where the mandatory five-year pre-reorganization holding period is not satisfied because the relevant subsidiary was established in the course of the restructuring.

RETT generally is triggered with respect to real estate owned by a corporation or partnership if one party either acquires or, for the first time, consolidates ownership into a direct or indirect interest of at least 95% in the real estate-owning corporation/partnership. RETT also is triggered by intragroup share transfers/restructurings.

Certain intragroup restructurings can benefit from an exemption from RETT if the following conditions are satisfied:

- The transaction is carried out under specific provisions in Germany's Reorganization Tax Code (e.g. mergers, de-mergers, spin-offs) or comparable rules in other EU/EEA countries, or the transaction is based on company law (e.g. a contribution of shares) or comparable rules in other EU/EEA countries; other transactions (e.g. a straightforward intragroup sale of shares) do not qualify;
- The reorganization involves a controlling entity (entrepreneur) and subsidiaries in which the controlling entity holds, directly or indirectly, at least a 95% interest; and
- At the time the reorganization is carried out, the direct or indirect 95% shareholding has been held for the previous five years and will continue to be held for five years after the reorganization.

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As a result of the five-year pre- and post-reorganization holding periods and the tax authorities' restrictive interpretation of the applicability of the intragroup exemption, the exemption is applied only in rare instances.

The case before the Local Tax Court of Duesseldorf involved the five-year pre-reorganization holding period. A GmbH spun off a business unit, including real estate, into a newly established subsidiary that issued new shares to the GmbH. The tax authorities determined that the five-year pre-reorganization holding period was not satisfied because the subsidiary was established in the course of the restructuring.

The tax court rejected the tax authorities' restrictive interpretation and ruled that the five-year pre-reorganization holding period need not be satisfied if the subsidiary was established during the restructuring. The decision is in line with a previous decision of the Local Tax Court of Nuremberg, in which the court questioned the tax authorities' restrictive application of the RETT intragroup exemption rule, although that case involved a situation where the subsidiary was established by the controlling entity in the course of the five-year pre-reorganization holding period.

The Local Tax Court of Duesseldorf's decision is a welcome clarification of the intragroup restructuring exemption rule and may provide for more flexibility in restructurings. However, the tax authorities are expected to appeal the decision to the Federal Tax Court.

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Germany:
Local tax court rules on subordination-of-claims agreement

The Local Tax Court of Lower Saxony ruled on 12 June 2014 that a subordination-of-claims agreement does not lead to "de-recognition" (i.e. release) of a loan liability in the debtor's tax balance sheet where the agreement specifically refers to repayment in the case of "retained earnings."

Under German income tax law, a loan liability must be de-recognized in the debtor's tax balance sheet if the loan agreement (or side letters) contain a provision indicating that the repayment of the loan is dependent on whether the debtor realizes future profits/revenue. De-recognition of a loan generally triggers taxable income at the level of the debtor.

A similar provision often is included in subordination-of-claims agreements under which the creditor and debtor try to avoid the debtor's overindebtedness from an insolvency law perspective. According to official guidance issued by the tax authorities, de-recognition need not be carried out where the subordination-of-claims agreement specifically refers to "other available assets" as a means for repayment.

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The case before the Local Tax Court of Lower Saxony involved a subordination-of-claims agreement under which the debtor was required to repay the loan only in the case of future "retained earnings." The agreement did not include a reference to "other available assets."

The tax authorities took the position that the loan liability should be de-recognized in the debtor's tax balance sheet because the wording of the agreement implied only a profit-related repayment, and that a reference to "other available assets" was not included.

The tax court denied the de-recognition of the loan liability and referred to the broader definition of the term "retained earnings" under German GAAP rules. Under such rules, "retained earnings" include not only future profits, but also withdrawals from capital or revenue reserves. The court held that the repayment consequently was not dependent only on future profits, but also depended on other, non-profit-related items, such as withdrawals from capital reserves.

The Local Tax Court of Lower Saxony's decision provides welcome clarification of when de-recognition of loan liabilities must be carried out for income tax purposes, but also illustrates that the wording of subordination-of-claims agreements must be chosen carefully and is of upmost importance in determining whether a de-recognition has to take place. The tax authorities are expected to appeal the decision to the Federal Tax Court.

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Gibraltar:
European Commission state aid investigation expanded to include review of tax rulings

The European Commission (EC) has announced that it is expanding the scope of its ongoing state aid investigation into the Gibraltar corporate tax regime to include a review of tax rulings issued by the Gibraltar tax authorities.

Background

In October 2013, following a complaint from Spain, the EC opened an investigation to verify whether Gibraltar's corporate tax regime that came into effect on 1 January 2011, following the introduction of the new Gibraltar Income Tax Act 2010 (ITA 2010), selectively favors certain categories of companies, in breach of EU state aid rules.

The ITA 2010 replaced the previous tax act that was repealed on 31 December 2010. Although the ITA 2010 retained as its basis of taxation the territorial principle that all income "accrued in, or derived from" Gibraltar is taxed, it removed interest income and royalties from the scope of taxation. The EU investigation is focused on examining these two types of income in particular.

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The Gibraltar government was quick to respond, and has since made changes to the ITA 2010 to allay the EU's concerns, bringing into the scope of taxation both intercompany interest income (where this exceeds GBP 100,000 per annum) as of 1 July 2013, and royalty income as of 1 January 2014. (For prior coverage, see the alerts dated 24 December 2013 and 11 June 2013.)
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Tax rulings are available in Gibraltar to allow taxpayers to obtain advance confirmation of how the Income Tax Office will apply local tax legislation to a taxpayer's particular circumstances. In particular, it is common for companies to request advance tax rulings where they believe that their income does not accrue in or derive from Gibraltar (and therefore is outside the scope of taxation), and they want certainty that the Income Tax Office will agree with that interpretation.

The EC confirmed that it has assessed 165 tax rulings granted by the Gibraltar tax authorities in 2011, 2012 and up to August 2013, i.e. the period since the new ITA 2010 came into force. The EC is concerned that rulings may have been granted without performing an adequate evaluation of whether the companies' income has been accrued in or derived from outside Gibraltar, and therefore properly is exempt from taxation in Gibraltar. The EC considers that potential misapplication of the provisions of the ITA 2010 may constitute state aid. Accordingly, it is expanding the scope of its investigation to examine the Gibraltar tax rulings practice.

The Gibraltar government has confirmed that it is confident that all advance rulings are issued within the parameters of the legislation and can be properly substantiated.

Comments

Companies that have obtained advance rulings based on information that properly reflects their actual circumstances should not be overly concerned by the expansion in the scope of the EU investigation. Tax rulings do not confer any additional rights to recipients that they do not already have under the legislation at the time. Therefore, where the location of a company's activity is such that the company's income does not accrue in or derive from Gibraltar, that income will not be taxable in Gibraltar, regardless of whether the company has an advance ruling; in these circumstances, the mere fact of having an advance ruling should not constitute state aid.

In other words, the practice of providing tax rulings after proper consideration of the circumstances should not, in itself, constitute state aid, as rulings do not extend any additional rights to the recipient that do not already exist under current legislation.

All tax rulings are issued with a clause that they are "based on the relevant current law" and that "if any material fact or circumstance upon which these confirmations have been based should change or not materialise or if found to be inaccurate" the ruling can be revoked or anti-avoidance provisions applied. This should ensure that where the authorities become aware that a company's income should be subject to tax, they will revoke the ruling or apply anti-avoidance provisions to ensure the income is taxed.

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Ukraine:
Currency control regulations issued, including temporary restrictions

In August and September 2014, the National Bank of Ukraine (NBU) issued a series of decrees that make significant temporary changes to the rules governing foreign exchange transactions. Although most of the changes tighten the rules, a few changes make the rules less restrictive. The most substantial changes are made by Decree No. 591 of 22 September 2014.

Changes that apply through 21 November 2014

Control over foreign currency transactions is tightened, in particular:

- The NBU has tightened control over the operations of banks; it may suspend risk-bearing transactions and demand the submission of documents supporting the relevant transactions.
- Banks are not allowed to discontinue supervision over foreign currency transactions relating to their clients' export operations based on documents confirming the discharge of obligations through the offset of similar claims (i.e. the offset of similar claims in foreign currency is not allowed).
- Banks are required to exchange foreign currency income for an equivalent amount in UAH on the business day following the date on which that income is credited to a separate analytical account (balance sheet account 2603, "Clearing accounts of business entities"), even if they do not receive the relevant instructions from their client. Banks must file a detailed application with the NBU on the date the clearing account is credited that provides the total amount of the mandatory exchange of foreign currency planned for the following business day.

Additionally, the validity of the maximum deadline of 90 calendar days (rather than 180 days) for the settlement of import and export transactions has been extended through 21 November.

The restriction on the mandatory exchange of foreign currency earnings has been reduced to 75% (until 23 September, 100% of foreign currency earnings were subject to mandatory exchange).

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Changes that apply through 2 December 2014

The following foreign currency transactions are prohibited:

- Payments relating to import transactions that do not involve the import of goods into Ukrainian territory. The relevant NBU decree does not specify whether the ban applies to payments for services provided by nonresidents. It should be noted, however, that some banks refuse to handle payments relating to transactions that involve the import of services, given that the definition of “goods” in the law on foreign economic activities encompasses services as well. The NBU is expected to provide clarification on this issue in the near future.
- Payments made under import contracts more than 180 days after the relevant goods are imported into Ukraine and cleared by customs;
- Payments made to foreign investors following the sale of equity rights (except shares in joint stock companies), or following the over-the-counter sale of securities issued by Ukrainian entities (with the exception of Ukrainian government bonds);
- Payments of dividends to foreign investors (except for refunds of dividends on exchange-traded securities); and
- Foreign currency transactions conducted under individual licenses from the NBU (except for the placement of funds by legal entities into accounts held outside Ukraine under individual licenses from the NBU).

Additionally, the amount of cash denominated in a foreign currency that a banking institution may sell to an individual per business day is restricted to the equivalent of UAH 3,000 (until 23 September, a UAH 15,000 restriction applied). The only exception is the purchase of foreign currency by a resident individual to fulfill his/her foreign currency obligations under a loan agreement concluded with a lending bank. The amount of foreign currency a bank may sell to such an individual is limited to the amount of his/her foreign currency obligations. This exception applies only if the bank exercises control over the intended use of the purchased foreign currency.

In one less restrictive change, it no longer is necessary to convert foreign currency remitted from abroad into UAH if the recipient is an individual that is not opening an account (i.e. a retail money transfer). This measure is expected to increase the inflow of foreign currency to Ukraine from nontrading operations.

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Uruguay:
Tax incentives granted to shared services centers

A decree published on 4 September 2014 that applies as from that date grants tax incentives in the form of tax exemptions or reductions to new shared services centers (SSCs) established in Uruguay that provide services to nonresident related parties.

To obtain the tax benefits, all of the following conditions must be satisfied:

- Services generally must be provided to foreign related parties (except that less than 5% of services may be provided to resident related parties, as described below).
- The services provided must be limited to advice and data processing, and must relate to activities developed, goods located or rights economically used abroad.
- The services generally must be exclusively used abroad (except for the less than 5% of services that may be provided to resident related parties).
- At least 150 new employees must be hired during the first three years of the SSC, and maintained until the end of the fifth year.
- Such employees' remuneration must be equivalent to a "qualified direct work position" (this term has not yet been defined).
- At least 75% of the workforce must be Uruguayan citizens.
- A minimum of approximately USD 1.2 million must be invested in training the workforce of Uruguayan citizens during the first three years of the SSC.

The following tax benefits will be granted to qualifying SSCs:

- A corporate income tax exemption will apply for 90% of the income derived from the activities of the SSC during its first five years of operations (counting from the year following the request for this benefit).
- SSCs under this regime may provide services to resident related parties, but only if such services are less than 5% of the total services the SSC provides for the year. The corporate income tax exemption will not apply for services provided locally.
- If the number of new employees in a qualified direct work position reaches 300 at the end of the fifth year of operation of the SSC and the investment in the training of Uruguayan citizen employees is a minimum of approximately USD 2.4 million, the 90% corporate income tax exemption will last for 10 years. To qualify for the extended exemption, the 300 employees must be maintained until the end of the exemption period.
- Technical service fees paid to a nonresident are subject to withholding tax, but at a reduced rate of 0.6% (rather than the normal 12% rate) during the corporate income tax exemption period.
- Only dividends derived from the 10% of income that is not covered by the corporate income tax exemption and paid to a nonresident are subject to withholding tax, at a 7% rate, during the corporate income tax exemption period.
- Services provided by the SSC to nonresident parties will be considered export services for VAT purposes, subject to a 0% rate.
- A net worth tax exemption for assets allocated to the SSC activities is available for the same exemption period that applies for corporate income tax purposes.

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In brief

Chile – The comprehensive 2014 tax reform was enacted on 29 September 2014, with the effective dates of the changes ranging from 1 October 2014 to 1 January 2017. (For prior coverage, see *World Tax Advisor*, 26 September 2014.)
URL: http://newsletters.usdbriefs.com/2014/Tax/WTA/140926_5.html

India – The Indian budget for 2014-15 received the president's assent on 6 August 2014. Some highlights of the budget changes related to taxes include the following: expenditure incurred on corporate social responsibility activities generally is not deductible for tax purposes; the holding period required for gains from sales of shares of an unlisted company to qualify as long-term capital gains is increased from 12 to 36 months; dividend distribution tax is payable on a "grossed up" basis for dividends distributed on or after 1 October 2014; and a specific tax regime applies to certain real estate investment trusts and infrastructure investment trusts as from 1 October 2014. Other changes relate to advance pricing agreements, the transfer pricing rules and the concessional withholding tax rate that applies to certain interest. There is no change to the corporate tax rate, surcharge or cess. (For prior coverage of the budget, see *World Tax Advisor*, 25 July 2014).
URL: http://newsletters.usdbriefs.com/2014/Tax/WTA/140725_3.html

Indonesia – The corporate income tax return and individual income tax return forms have been revised for tax year 2014. Corporations subject to the reduced corporate income tax of 1% of gross income and individuals subject to the reduced 1% final tax on income must attach a list of gross income and final tax paid during the year to their income tax returns.

Isle of Man – The Treasury has announced that it considers there to be no significant barriers to the introduction of mandatory online filing for company tax returns. It expects to introduce the online filing regime for companies with accounting periods ending on or after 5 April 2015. Some exemptions from mandatory online filing will be available.

Malta – The remittance-based taxation rules for individuals have been retroactively amended effective 1 July 2013. The Malta tax treatment of an individual depends on whether the individual is resident, ordinarily resident and/or domiciled in Malta. Previously, individual residents in Malta who either are not ordinarily resident or not domiciled in Malta were taxable in Malta on a source and remittance basis, i.e. on income and chargeable gains arising in Malta and on foreign income (but not foreign capital gains) received in or remitted to Malta. Under the amended rules, individuals that qualify as a "permanent resident of Malta" or a

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"long-term resident" are taxed on their worldwide income, rather than on a source and remittance basis.

OECD – A revised calendar has been published that includes dates for discussion drafts and public consultations related to 2015 deliverables from the base erosion and profit shifting (BEPS) project.

Ukraine – A new VAT administration model aimed at preventing fraudulent transactions will take effect on 1 January 2015. The new model will require all VAT payers to open special VAT accounts (similar to bank accounts, but that may be used only for specific VAT purposes). Changes also will be made to the VAT recovery regime. The government and the tax authorities are working on developing software to operate the special VAT account system for both the operator (a special bank) and for taxpayers, and on making the necessary changes to the relevant legislation and instructions for the transitional period.

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No new alerts were issued this week. Be sure to refer to the archives to ensure that you are up to date on the most recent releases.

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