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HAPPY FRIDAY!

Ghossn thinks "inside the box"; **Meghan** does a **Yoko**; and **Ricky** wins lots of new friends in Hollywood!

Le Maire and **Mnuchin** hope to reach a compromise by **Davos** – otherwise, it will be all downhill from there!

China is ready for the chop; **Ireland** counts its cost; **Axiata** arbitrates; and **Romania** splits!

Government is back in business in **Austria** and **Spain**; **News Corp** counts zero as a win; **Adams** loses its **Challenge**; and **stock lending** is not beneficial in **Switzerland**!

But at the end of the week, we're left with this question: how did **Carlos Ghossn** walk out of his home and catch the bullet train to **Osaka**, without being recognised?

Have a great weekend!

Steve

THIS WEEK'S PODCAST

(For ITB video subscribers, please log in to access the video and documents/reports)

- Digital taxation
- Trade and other global developments
- Asia Pacific
 - Japan, Malaysia, Nepal, Singapore
- Europe
 - Austria, EU, France, Finland, Italy, Moldova, Poland, Romania, Spain, Switzerland, UK
- Middle East & Central Asia
 - Oman & Qatar
- Americas
 - Argentina, Chile, Colombia, US
- Treaties
- Worth reading

WORTH READING

Mindy Herzfeld

"Rocky Shoals Ahead for International Tax"

Tax Notes Today International, Tax Analysts (December 23, 2019) (subscription service)

Koen van 't Hek

"Mexican Tax Reform in between BEPS 1.0 and BEPS 2.0"

Kluwer International Tax Blog (free service)

Oliver Treidler

"The Arm's-Length Principle Works Just Fine (Most of the Time)"

Tax Notes Today International, Tax Analysts (January 9, 2020) (subscription service)

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

ACO, a company resident in country A, carries on a real estate investment business.

ACO pays \$10,000 to CCO (an unrelated company resident in country C), in consideration for CCO granting ACO an option to purchase some land in country B. At a later time, ACO sells the option to DCO (an unrelated company resident in country D), for a price of \$1 million.

ACO therefore derives a profit of \$990,000 from the acquisition and sale of the option. That profit is taxable under the country B income tax law.

The A/B treaty is the same as the 2014 OECD model treaty.

What is the treatment of ACO's profit under the A/B treaty?

Answer in next week's ITB email alert!

LAST WEEK'S QUESTION

XCO is a company resident in country X.

XCO owns 100% of the shares in YCO, a company resident in country Y.

XCO has made an interest-bearing loan to YCO. Assume that the interest rate satisfies the arm's length principle.

Country Y tax law includes a thin capitalisation rule, which uses a 2:1 non-resident related party debt to equity limit. XCO's loan to YCO exceeds that 2:1 limit. Accordingly, under the thin capitalisation rule, the interest on the excess amount of loan is disallowed as a deduction for YCO. However, the disallowed interest retains its character as interest for withholding tax purposes.

Country Y levies a 25% withholding tax on outbound dividends, and a 15% withholding tax on outbound interest.

Country X taxes resident companies on global income.

The X/Y double tax treaty is identical to the 2014 OECD model treaty.

Based on these facts, what is the tax treatment of each of XCO and YCO in countries X and Y?

LAST WEEK'S ANSWER

The question does not indicate the maximum ratio of related party debt to equity which would satisfy the arm's length principle ("ALP ratio").

We need to compare 3 ratios: (i) ALP ratio, (ii) Y's 2:1 thin cap ratio, and (iii) actual XCO / YCO debt to equity ratio ("actual ratio").

YCO's interest deductions:

- If ALP ratio > actual ratio > 2:1 thin cap ratio, then YCO's deductions are allowable under Art. 24(4) (non-discrimination)
- If actual ratio > ALP ratio > 2:1 thin cap ratio, then YCO's deductions are disallowed under thin cap rule, to extent that actual ratio exceeds ALP ratio: Art. 24(4)

Interest withholding tax:

- 10%, under Art. 11(2) (regardless of the extent to which YCO's deductions are disallowed)
- Note that Y law does not recharacterize disallowed interest as dividends
- Note also that Art. 11(6) is not applicable, as the interest rate satisfies the arm's length principle ("the amount of the interest, having regard to the debt-claim for which it is paid, exceeds ...")
- X must give credit to XCO for the Y withholding tax: Art. 23A(2) / 23B(1)



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