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ITB International Tax Bytes *by Steve Towers*

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28 August 2020

HAPPY FRIDAY!

Phil Hogan trips up, while **Japan** runs out of credit card digits!

Meanwhile, in the tax world…

The **UK** plays a straight bat; **India** pays attention (but not interest); **Canada** is lumbered with criticism; **Africa** digitally multiplies; **Mastercard** is whipsawed; and the **EU** and **US** finally agree!

Australia licks envelopes; **Brazil** bills again; **Israel** accelerates; **Poland** saves 1%; **VKC** inverts and converts; **Japan** consolidates; and the **EU** protects against carbon!

But the most important question this week is this: **"Can you smize, while wearing a mask?"**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

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

1. Digital taxation
2. Trade
3. Asia Pacific
   - Australia, Hong Kong, India, Indonesia, Japan, New Zealand, Singapore, Taiwan, Thailand
4. Europe
   - Brexit, Denmark, EU, Guernsey, Luxembourg, Poland
5. Middle East & Central Asia
   - Israel, Uzbekistan
6. Americas
   - Brazil, Chile, US
7. Treaties
8. Worth reading

WORTH READING

Gonzalo Suffiotti
"Indirect Taxation of Digital Services in Latin America: A Comparative Overview of Recent Developments in Argentina, Chile, Colombia, Mexico, Peru and Uruguay"
International VAT Monitor, IBFD, 2020 (Volume 31), No. 6 (subscription service)

Seungho Kim, Sungdoo Jang,and Maria Chang
"Foreign Entity Classification in Korea"
Tax Notes Today International, Tax Analysts, 21 August 2020 (subscription service)

Archie Parnell
"A Tale of Two Tax Systems: Discerning Solutions for India-US Tax Disputes"
Freely available on LinkedIn: click here to access

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

ACo, a company resident in A, makes an interest-free loan to BCo, a related loss-making company resident in B.

The A tax authorities decide not to impute interest on the loan, because they take the view that the loan is quasi-equity under A's transfer pricing rules.

However, the B tax authorities impute interest on the loan under B's transfer pricing rules, and claim that ACo is liable for 10% interest withholding tax (IWT) on the imputed interest (the B domestic law IWT rate is 25%, but Art. 11 of the A/B treaty limits the B tax to 10%). The A/B treaty is identical to the 2017 UN model treaty.

Does the A/B treaty permit B to impose tax on the imputed interest?

Answer in next week's ITB email alert!

LAST WEEK'S QUESTION

XCo, a company resident in X, owned a building in Y which it purchased for $1 million.

XCo derived rent from leasing the building to an unrelated lessee.

Some years later, XCo sold the building, to an unrelated purchaser, for $1.5 million.

Under X law, XCo was subject to tax on the rental income, but was able to claim deductions for tax depreciation on the building. The tax depreciation aggregated to $0.3 million over the years of ownership. When XCo sold the building for $1.5 million, it derived a capital gain of $0.8 million (i.e., $1.5 million minus the reduced cost base of $0.7 million).

Under Y law, XCo was subject to tax on the rental income, but was not entitled to any tax depreciation. When XCo sold the building for $1.5 million, it derived a capital gain of $0.5 million (i.e., $1.5 million minus cost base of $1 million).

Both capital gains are subject to corporate income tax (at the same rate as ordinary income) under the domestic tax laws in X and Y.

The X/Y treaty is identical to the 2017 OECD model treaty, with Art. 23A.

Both X and Y use the same currency.

What will be the tax treatment of XCo, in each of X and Y, in regard to the sale of the building?

LAST WEEK'S ANSWER

Y:

Art. 13(1) permits Y to impose tax on XCo's "gain", which is not defined – its computation is left to Y law: para. 12, OECD Comm. on Art. 13.

Under Y law, XCo's capital gain of $0.5 million is subject to income tax.

X:

XCo's capital gain of $0.8 million will, prima facie, be subject to income tax. However, X must provide relief under Art. 23A.

Art. 23A(1): "Where a resident of [X] derives income…which may be taxed in [Y] in accordance with the provisions of this Convention…,[X] shall…exempt such income…from tax."

What amount will be exempt: $0.5 million or $0.8 million?

These facts are similar to the situation described in paras. 14 & 15, OECD Comm. on Art. 13. The only difference is that, in the situation in those paragraphs, the treatment of the $0.3 million is described as "the depreciation allowances granted earlier may be recovered", whereas (in our facts) XCo's cost base is reduced to $0.7 million. As capital gains are subject to corporate income tax at the same rate as ordinary income, the 2 treatments of the $0.3 million have the same tax effect. Thus, it would be logical to apply the same approach – i.e., $0.5 million would be exempt.

IMHO: $0.5 million will be exempt, and $0.3 million will be taxed.

Tax Quiz Archives

Email Alert Archives

AskSteve

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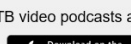

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