**ITB International Tax Bytes** *by Steve Towers*

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25 September 2020

## HIGHLIGHTS

- **Pillars One & Two: draft blueprint reports**
- **Pillar Two: GILTI, jurisdictional blending, carve-outs**
- **Pillar One: major disagreement areas**
- **EU State aid case: Spanish tax lease system**

## HAPPY FRIDAY!

**Trump** mails disorder; **Wrexham football club** is the latest "must have" investment; and **Thailand** asks for whom the bell has rung!

Meanwhile, in the tax world…

**Russia** tries to dig itself out of a fiscal hole; **Unilever** still plans a costly exit; **Hong Kong** recognises revenue; **Malaysia** reimburses; the **OECD's** blueprints leak; but it's the **Spanish** ships which sink!

And at the end of the week, the most important question is this: **"Have you read the blueprints yet?"**

**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. Other global developments
3. Asia Pacific
   - Hong Kong, Malaysia, Singapore
4. Europe
   - EGC, EU, Netherlands, Russia
5. Africa
   - ATAF
6. Americas
   - US
7. Worth reading

## WORTH READING

Vikram Chand and Kinga Romanovska
"Pillar II of the Digital Debate: Our View on the Approach Towards Blending and Substance Carve Outs to Determine Effective Tax Rates"
Kluwer International Tax Blog (18 September 2020) (freely available)

B. Anthony Billings and Kyungjin Kim
"An Update on Withholding Taxes on Dividend Equivalent Payments"
Tax Notes Today International, Tax Analysts, 16 September 2020 (subscription service)

## INTERNATIONAL TAX QUIZ

## THIS WEEK'S NEW QUIZ

ACo, a company resident in A, owns 100% of the shares in BCo, a company resident in B.

BCo owns land in B – the land has a market value equal to 35% of the aggregate market value of all of BCo's assets.

In September 2020, ACo sold all of its shares in BCo to CCo, an unrelated company resident in C.

The A/B treaty, which was signed and entered into force in 2012, is identical to the 2010 OECD model treaty.

The MLI applies to the A/B treaty. The MLI entered into effect, for both A and B, on 1 January 2020.

Both A and B: (i) reserved against Art. 9(1), MLI for all of their covered tax agreements ("CTAs"); but (ii) did not reserve against Art. 11(1), MLI for any of their CTAs.

In early 2020, B changed its tax law, in regard to the imposition of capital gains tax on sales of shares in "land-rich" companies. Prior to the change, the law applied a "more than 50%" valuation threshold – i.e., the value of the immovable property in B had to be more than 50% of the aggregate value of the assets of the company. There were 2 important changes: (i) the valuation threshold was reduced to "more than 25%"; and (ii) the tax liability was removed from the non-resident seller and instead imposed on the "land-rich" company. These law changes are effective for sales on or after 1 July 2020.

Does the treaty permit B to levy tax in regard to ACo's sale of shares in BCo?

**Answer in next week's ITB email alert!**

## LAST WEEK'S QUESTION

XCo, a company resident in X, owns 100% of the shares in YCo, a company resident in Y.

YCo carries on a manufacturing business in Y.

XCo makes a loan to YCo, for use in its business. The loan carries an arm's length interest rate. Under Y tax law, the interest is fully deductible for YCo. The Y corporate income tax rate is 30%.

Under X tax law, YCo is treated as a branch of XCo.

YCo is therefore a hybrid entity: it's treated as a taxable entity (a resident company) in Y, and as a transparent entity (a branch) in X.

Under domestic law, Y imposes a final withholding tax of 20% on gross outbound interest payments.

Neither X nor Y has introduced hybrid mismatch rules into domestic law.

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

What tax treatment does the X/Y treaty permit or require, in each of X and Y, in regard to the interest payments from YCo to XCo?

## LAST WEEK'S ANSWER

Y tax

The key issue is whether Art. 1(2) applies:

- YCo is "an entity or arrangement that is treated as wholly or partly fiscally transparent under the tax law of either Contracting State"
- However, the interest is not "derived by or through" YCo – it's derived by XCo, and paid by YCo
- Thus, Art. 1(2) should not apply

Art. 11(2) would therefore apply: 10% Y tax would be imposed.

X tax

Art. 23A(2) requires X to allow XCo a credit for the Y tax: see the discussion on "conflicts of qualification" in the OECD Comm. on Art. 23A/B.

However, by virtue of the second sentence in Art. 23A(2), the amount of the credit is limited to the amount of the X tax on the interest income. If the interest income is not recognised under X tax law (because YCo is treated as a branch of XCo), then that amount of X tax is nil.

Thus, no credit.

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