ITB International Tax Bytes *by Steve Towers*

"International tax news, explained"

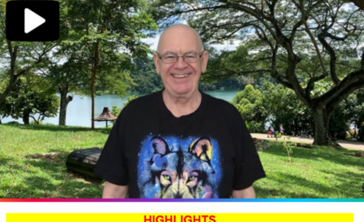
Want to learn more about ITB? Sign up for a free trial by emailing us

Check out our suite of subscription plans: individual (standard), student, university faculty, young professional, and enterprise

Free Trial

Subscribe

23 October 2020



HIGHLIGHTS

- **Pillar Two detailed analysis: GloBE rules – calculating the ETR (Part 2)**
- **4 cases (Australia, India, Denmark, France)**
- **US: IRS advice on IP contributions to foreign partnerships**

HAPPY FRIDAY!

Iran hacks; **AOC** twitches; **Google** is sued; **Trump** goes mute; but it's **Korea's finance minister** who's left homeless!

Meanwhile, in the tax world…

India retrospectively helps a taxpayer; **France** favours Italians; **Turkey** slices; **Argentina** discloses; **Denmark** exacts a price; while the **IRS** cries abuse!

But at the end of the week, the most important question is this: **"Do you need to be a good accountant to understand the GloBE rules?"**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

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

1. Global developments
2. Pillar Two: GloBE Rules – Calculating the ETR (Part 2)
3. Asia Pacific
    - Australia, India
4. Europe
    - Denmark, France, Spain, Turkey, UK
5. Africa
    - Tunisia
6. Americas
    - Argentina, US
7. Treaties

WORTH READING

John F. Avery Jones
"A Fresh Look at Article 3(2) of the OECD Model"
Bulletin for International Taxation, 2020 (Volume 74), No. 11 (subscription service)

Michael Lang
"Tax Treaty Interpretation – A Response to John F. Avery Jones"
Bulletin for International Taxation, 2020 (Volume 74), No. 11 (subscription service)

INTERNATIONAL TAX QUIZ

ACo (a bank resident in A) has several individual customers in C.

ACo enters into an equity swap with each of those customers. The equity swap tracks a portfolio of publicly listed shares in companies resident in B (collectively, "BCos"), and a cash balance held by the customers with CCo (a bank resident in C). ACo and CCo are members of an MNE group.

When ACo enters into the equity swaps, it does not own any of the shares in the relevant portfolio. In order to hedge its position, ACo purchases the portfolio of shares which are tracked in the equity swaps.

The equity swaps exchange the economics of ownership of the portfolio of shares (e.g., dividends and share price changes) and ownership of the cash balances (e.g., interest). A single payment is made under each equity swap (either from ACo to the customer, or vice versa) at the end of every quarter. The economics are taken into account in the formula which calculates the quarterly single payment. There is no contractual right to the individual components in the formula.

Each equity swap contains a "force majeure" clause, which does not cover the failure of the BCos to pay dividends (other than by virtue of B government action).

All 3 countries use the same currency.

A and B each impose a 20% final withholding tax on outbound dividends.

The A/B treaty, which was signed and entered into force in 2011, is identical to the 2010 OECD model treaty, except that there is a single rate of 0% in Art. 10(2).

The A/C treaty is identical to the 2001 UN model treaty, except that there is a single rate of 10% in Art. 10(2).

The MLI (in particular Art. 7(1)) applies to both treaties.

There is no B/C treaty.

Q1: Does the A/B treaty permit B to impose withholding tax on dividends paid to ACo?
Q2: Does the A/C treaty permit A to impose withholding tax on payments made by ACo under the equity swaps?

Answer in next week's ITB email alert!

LAST WEEK'S QUESTION

XCo, a company resident in X, has a branch in Y.

The branch conducts a manufacturing business in Y.

Excess cash generated by the branch is "deposited", on a short term basis, with the XCo head office in X. When the cash is needed by the branch, it is "repaid" by the head office to the branch.

The branch's financial statements and income tax return do not recognise any interest income on these "deposits".

The Y tax authorities impute arm's length interest income to the branch under the Y domestic law transfer pricing rules. Those rules apply to "transactions" between a branch and head office, where one is located in Y and the other is located in another country. Those rules do not apply if the branch and head office are both located in Y.

The X/Y treaty, which was signed and entered into force in 2009, is identical to the 2008 OECD model treaty.

Does the treaty permit the Y tax authorities to impute arm's length interest income to the branch?

LAST WEEK'S ANSWER

The Y branch is a PE under the treaty.

Under Art. 7(2), and the 2-step approach described in the OECD Comm., it is likely that the "deposit" would be characterised as a loan from the PE to the head office in X, and that arm's length interest may be imputed by the Y tax authorities under an analogous application of Art. 9(1).

However, Art. 7(2) is subject to Art. 7(3). In the OECD Comm. on Art. 7(3), it is stated that (except for financial enterprises such as banks) "internal interest" on "internal loans" between head office and PE need not be recognised. However, those statements refer to the situation where the "internal loan" is from the head office to the PE, and the "internal interest" is sought to be deducted by the PE under Art. 7(2). That is also the situation which is addressed in Art. 7(3) itself. Neither Art. 7(3), nor the OECD Comm. on Art. 7(3), is directed towards the alternative situation where the "internal loan" is from the PE to the head office.

The OECD Comm. on Art. 7(3) reflects a qualification on the full implementation of the OECD PE Reports (2008 & 2010). However, if Art. 7(3) does not apply to "internal loans" from the PE to the head office, that qualification is not relevant.

Thus, in my view, Art. 7(2) should allow the imputation of arm's length interest by the Y tax authorities.

Note that the Y law allows the imputation of interest between a branch and head office, but these rules do not apply if the branch and head office are both located in Y. Is that a breach of Art. 24(3)? No – the OECD Comm. states that Art. 24(3) is subject to the PE profit attribution rules in Art. 7(2).

Tax Quiz Archives

Email Alert Archives

AskSteve

Referral Program

What is ITB?

If you have a friend or colleague who you think might find this email alert interesting, please forward it to them.

Watch ITB video podcasts anytime, anywhere with our App!

© 2020 International Insights Pte Ltd. All rights reserved.

UNSUBSCRIBE
If you no longer wish to receive emails from us, please click here