"International tax news, explained"

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8 January 2021

HIGHLIGHTS

- **Review of the top international tax cases of 2020**
- **OECD's guidance on the transfer pricing implications of COVID-19**
- **Latest developments on digital taxation**

ITB series on Pillar Two

1. **GloBE rules**
   - **Scope – ITB (9 Oct 2020)**
   - **Calculating the ETR (Part 1) – ITB (16 Oct 2020)**
   - **Calculating the ETR (Part 2) – ITB (23 Oct 2020)**
   - **Carry-forwards – ITB (30 Oct 2020)**
   - **Carve-out, and computation of the ETR and top-up tax – ITB (6 Nov 2020)**
   - **Income Inclusion Rule – ITB (13 Nov 2020)**
   - **Switch-Over Rule, and Undertaxed Payments Rule (Part 1) – ITB (20 Nov 2020)**
   - **Undertaxed Payments Rule (Part 2) – ITB (27 Nov 2020)**
   - **Associates, joint ventures and orphan entities; and Simplification options – ITB (4 Dec 2020)**
2. **Other topics**
   - **Subject to Tax Rule – ITB (2 Oct 2020)**
   - **Implementation and Rule Co-ordination – ITB (11 Dec 2020)**
   - **Unresolved issues, GILTI & hub jurisdictions – ITB (18 Dec 2020)**

HAPPY FRIDAY!

Neil Young sells his **heart of gold**; **Lewis Hamilton** becomes a **knight** in **Monaco**; but **Washington** resembles **Caracas**!

Meanwhile, in the tax world…

French perfume is saved; **Cairn** makes billions; **Taiwan** aligns; **Australia** overrides; the **UK** tosses out hallmarks; **Oman** names the date; and the **US** rushes to regulate, but still has time to point its finger at **India**, **Italy** and **Turkey!**

But at the end of an unbelievable week in US politics, my advice is this: **the next time an American says to you that the US is "the world's greatest democracy", try not to laugh!**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

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

1. Review of the top international tax cases of 2020
2. Transfer Pricing implications of COVID-19
3. Digital taxation
4. Asia Pacific
   - Australia, India, Indonesia, Taiwan, Thailand
5. Europe
   - Brexit, UK
6. Middle East & Central Asia
   - Oman
7. Americas
   - US
8. Treaties

WORTH READING

Mark Brabazon
"The Oracle, Transparent Entities and Access to Tax Treaties"
Australian Tax Review, 2020 (Volume 49) 250 (subscription service)

Jonathan Schwarz
"Article 3(2) of the OECD and UN Models: An International View"
Bulletin for International Taxation, IBFD, 2021 (Volume 75), No. 1 (subscription service)

INTERNATIONAL TAX QUIZ

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

Services are provided to XCo's PE by Parent Co, which is also a company resident in X. Parent Co is the 100% parent of XCo.

The Y tax authorities consider that the fee charged by Parent Co for the services provided to XCo's PE, exceeds the arm's length price. They therefore propose to deny the PE a deduction for the excessive amount of fee, pursuant to Y's transfer pricing rules.

The X/Y treaty is identical to the 2017 OECD model treaty.

Does the treaty permit the Y tax authorities to deny the deduction for the excessive amount of fee?

Answer in next week's ITB email alert!

LAST WEEK'S QUESTION

ACo, a company resident in A, conducts a manufacturing business in A, using patents and knowhow which ACo owns.

ACo wants to sell its goods in the B market. However, due to customs duties which are imposed on imports into B, ACo is planning to start a manufacturing operation in B, with the finished goods being sold to consumers in B.

ACo would like your advice on whether the B manufacturing operation should be structured as a B-resident subsidiary of ACo or as a branch of ACo.

ACo has told you the following:

- ACo currently has significant tax losses in A. These losses are available for indefinite carry-forward.
- ACo plans to use its existing cash resources to finance the B manufacturing operation – i.e., no borrowing will be done.
- ACo wants to minimise B tax.
- ACo wants to retain, in A, the legal and economic ownership of its IP.
- The B market does not discriminate against branches of companies incorporated in A.

The B corporate income tax law levies the same rate (25%) on resident companies and branches of non-resident companies.

B does not impose tax on outbound dividends or on branch profit remittances. However, B imposes a 10% withholding tax on the gross amount of outbound interest and royalties.

The B tax law does not recognise intra-entity "transactions".

The A/B treaty is identical to the 2017 OECD model treaty, except that Arts. 11 & 12 allow 10% source country tax (on gross payments) to be levied.

What is your advice?

LAST WEEK'S ANSWER

i. The amount of B income tax on profits should be the same for both subsidiary and branch:
   - The same rate is applied to both.
   - In regard to tax base, the profits attributable to the PE (i.e., branch) under Art. 7 should be the same as for a subsidiary, after deducting notional interest and royalty expenses. Although the B tax law does not recognise intra-entity "transactions", such deductions for the branch should be available by virtue of Art. 7 (i.e., by application of the "separate and independent enterprise" assumption). Also, Art. 24(3) will require that outcome.

ii. No B tax is imposed on profit remittances by both subsidiary and branch.

iii. 10% B withholding tax will apply to actual payments of interest and royalties in the subsidiary scenario, but no corresponding withholding tax will apply in the branch scenario: this is because the B tax law does not recognise intra-entity "transactions", and the "separate and independent enterprise" assumption in Art. 7 has no effect on Arts. 11 & 12 or on expanding ACo's tax liabilities under B law.

iv. ACo's A tax losses might be reduced by dividends paid by a subsidiary or by current profits derived by a branch. It is possible that the impact on ACo's A tax losses would not be the same for both subsidiary and branch.

IMHO: I would choose a branch, in order to achieve the savings in B withholding tax (cash and book tax benefit). However, the possibility that a branch might reduce ACo's A tax losses to a greater extent than a subsidiary, should be assessed.

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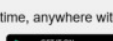

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