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22 January 2021

HIGHLIGHTS

- **Latest developments in digital taxation, including early indications of the Biden Administration's policy**
- **Germany's draft law on withholding tax reform, including extra-territorial taxation of IP income**
- **Detailed analysis of Pillar One: Scope**

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!

Bernie's mittens, **Kamala's** purple, and **Amanda's** words!

Meanwhile, in the tax world…

Italy defers tax, but **Rio Tinto** wants deferred tax accounting; **Janet Yellen** is on board, while **Sierra Leone** joins the club; the **US** thinks **Vietnam** is unreasonable; **Germany** goes extra-territorial; and **Lexel** is free to establish tax avoidance!

But at the end of the week, the most important thing to note is that **the Michelin Guide has gone vegan!**

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 & other global developments
3. Germany's draft law on withholding tax reform
4. Pillar One: Scope (Part 1)
5. Europe
   - ECJ, Italy
6. Treaties

WORTH READING

Sean Foley, Cameron Taheri and Lillie Sullivan
"Survey of Global Secondary Adjustment Rules"
Tax Notes Today International, Tax Analysts, 20 January 2021 (subscription service)

Evert-Jan Spoelder and Johan Loo
"Netherlands – New Withholding Tax on Interest, Royalties and Dividends"
Finance and Capital Markets, IBFD, 2020 (Volume 22), No. 4 (subscription service)

INTERNATIONAL TAX QUIZ

XCo 1, a company resident in X, owns some IP.

XCo 1 licenses the IP to XCo 2, a related company also resident in X, for arm's length royalties.

The IP is registered in many countries throughout the world, including Y.

XCo 1 and XCo 2 do not have any assets or employees in Y.

Under the Y domestic law, royalties which are paid for the licence of IP which is registered in Y, are deemed to be sourced in Y. This means that such royalties are subject to a final Y withholding tax of 25% of the gross amount of royalties.

The X/Y treaty is identical to the 2017 UN model, with the rate in Art. 12(2) being 10%.

Does the X/Y treaty permit Y to impose withholding tax on the royalties paid by XCo 2 to XCo 1? If so, at what rate?

Answer in next week's ITB email alert!

LAST WEEK'S QUESTION

ACo, a company resident in A, has conducted business through a branch in B for many years. The branch qualifies as a PE under the A/B treaty.

Until recently, the B income tax law included these elements:

- Income tax rate on taxable profits of resident companies and branches of non-resident companies: 25%
- Withholding tax on dividends paid to non-residents: 15%
- Tax on profit remittances by branches of non-resident companies: nil

The B income tax law was recently changed to impose a branch profits remittance tax of 20%.

The A/B treaty is identical to the 2017 OECD model treaty.

Does the treaty allow the B branch profits remittance tax to be levied on profit remittances by ACo's branch? If yes, at what rate?

LAST WEEK'S ANSWER

The branch profits remittance tax ("BPRT") is a tax on income, and therefore it would be a tax covered by the treaty: Art. 2(1). It would also probably be covered by Art. 2(4), but that is unnecessary. Also, note that Art. 24 is not limited to taxes covered by Art. 2: Art. 24(6).

Art. 7(1) allows B to tax the profits attributable to the PE. It does not restrict the tax rate, or the manner of imposing tax, on those profits. Thus, Art. 7(1) should be interpreted as allowing the BPRT to be imposed – subject to my comments below.

Art. 24(3) is more difficult. The effect of the BPRT is that the total B tax on the profits attributable to the PE exceeds the B tax which would be levied on a B-resident company carrying on the same activities. Thus, prima facie, the BPRT appears to breach Art. 24(3).

However, para. 60 of the OECD Comm. on Art. 24 says this:

> "In some States, the profits of a [PE] of an enterprise of another Contracting State are taxed at a higher rate than the profits of enterprises of that State…Where such tax is simply expressed as an additional tax payable on the profits of the [PE], it must be considered as a tax levied on the profits of the activities of the [PE] itself and not as a tax on the enterprise in its capacity as owner of the [PE]. Such a tax would therefore be contrary to [Art. 24(3)]."

The phrase, "not as a tax on the enterprise in its capacity as owner of the [PE]", suggests (but does not actually state!) that such a tax would not breach Art. 24(3). B's BPRT is such a tax, and thus there is some support in the OECD Comm. that the BPRT would not breach Art. 24(3).

But that then begs the question: if the BPRT is a tax which is imposed on ACo in its capacity as owner of the PE, and is not a tax on the profits of the activities of the PE itself, does the BPRT comply with Art. 7(1)?

At least one thing is clear: Art. 24 does not require the BPRT rate to be equal to the Art. 10 rate on dividends.

But whether Art. 7(1) and Art. 24(3) allow the BPRT to be imposed at all, is (IMHO) not clear. It's interesting to note that the 2016 US model treaty specifically allows the US's version of B's BPRT: Art. 10(10).

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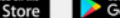

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