ITB International Tax Bytes by Steve Towers

"International tax news, explained"

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29 January 2021

HIGHLIGHTS

- **Latest developments in digital taxation**
- **OECD's updated guidance on the impact of COVID-19 on double tax treaties**
- **Continuation of in-depth analysis of Pillar One: Scope**

HAPPY FRIDAY!

Mozart writes another melody; **Botticelli** paints money; and **Robin Hood** is sued!

Meanwhile, in the tax world…

Janet makes friends; the **OECD** constructs an interruption; **Australia** is risk-focused; **Hungary** shames tax cheats; **Spain** frees capital; **Africa** trades up; **Israel** gets a recharge; while **CIBC** wins a visa exemption!

But at the end of a rollercoaster week on Wall Street, the most important question is this: **"When will GameStop's game stop?"**

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. Impact of COVID-19 on double tax treaties
3. Pillar One: Scope (Part 2)
4. Asia Pacific
    - Australia, India, Indonesia
5. Europe
    - European Court of Human Rights, Spain
6. Africa
    - African Continental Free Trade Area (AfCFTA)
7. Middle East & Central Asia
    - Bahrain, Israel
8. Americas
    - Canada
9. Treaties

ITB series on Pillar One

- **Scope (Part 1) – ITB (22 Jan 2021)**
- **Scope (Part 2) – ITB (29 Jan 2021)**

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)**

WORTH READING

Álvaro de la Cueva González-Cotera and Adrián Arroyo Ataz
"Spain – Tax Treaty Interpretation: A New Beginning"
European Taxation, IBFD, 2021 (Volume 61), No. 2/3 (subscription service)

J. Clark Armitage, Heather D. Schafroth, Elizabeth J. Stevens and H. David Rosenbloom
"United States – Coke Concentrate: A Recipe for Understanding the IRS's Biggest Win in 40 Years"
International Transfer Pricing Journal, IBFD, 2021 (Volume 28), No. 2 (subscription service)

Borys Ulanenko
"Transfer Pricing"
ADIT 3.03 Module Textbook, StarTax Education, 2020 Edition

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

ACo, a company resident in A, has conducted business with customers in B for 10 years.

ACo has always taken the position that it does not have a PE in B under the A/B treaty, and that therefore it is exempt from B tax on its profits. For that reason, ACo has never filed a B income tax return.

Following a recent tax audit, the B tax authorities have claimed that ACo has had a PE in B for all of the 10 years. The tax authorities have therefore issued a tax assessment to ACo in regard to the 10 years. The tax assessment reflects item (ii) below.

Under B income tax law: (i) the "statute of limitations" (i.e. the time period in which the tax authorities may issue assessments for an income year) only starts to run from the time that the taxpayer files an income tax return for the relevant income year; and (ii) a non-resident taxpayer which fails to file an income tax return within 24 months after the relevant income year, is denied all deductions in calculating its taxable profits for that year. Item (i) applies to both residents and non-residents, but item (ii) applies to non-residents only.

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

Does the treaty permit the tax assessment to reflect item (ii)?

Answer in next week's ITB email alert!

LAST WEEK'S QUESTION

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?

LAST WEEK'S ANSWER

1. Y is modeled on Germany.
2. Art. 12(2) will not apply to permit (and limit) the Y tax, as the royalties do not "arise" in Y (as defined in Art. 12(5)) – regardless of the fact that the royalties are sourced in Y under Y domestic law.
3. Some folks might then consider Art. 21:
    i. Art. 21(3) uses the term, "arising". According to the UN Comm., that term should take its meaning under domestic law. This would mean that the royalties "arise" in Y for the purposes of Art. 21(3), due to the deemed source in Y under Y domestic law (and regardless of the conclusion under Art. 12(5)).
    ii. If Art. 21(3) applies, the treaty would permit Y to impose tax on the royalties, without limitation – i.e. Y tax of 25% would apply.
4. However, Art. 7 should generally apply in this situation. As XCo 1 has no PE in Y, Art. 7(1) would provide an exemption. Art. 21(3) would not apply, as the royalties would be "dealt with" in Art. 7 – i.e., no Y tax would apply.
5. If XCo 1 is a passive IP holding company, and is not considered to carry on an "enterprise" (as defined in Art. 3(1)), then the Y tax authorities might take the view that Art. 7 does not apply to the royalties – in which case, Art. 21(3) should apply (see above).

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

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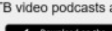

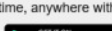

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