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FRANCE

TAX REFORMS, INCLUDING A FINANCIAL TRANSACTIONS TAX

On 16 August 2012, the measures set out in a second rectifying Budget were enacted. The main taxation measures are set out below.

CHANGES TO PERSONAL AND INDIRECT TAXES

– An exceptional wealth surtax on individuals whose net taxable assets are valued at over EUR 1,300,000 will apply for 2012. This will be calculated based on the progressive tax rates used for calculating the 2011 wealth tax, and will be payable on 15 November 2012.

– The tax free allowance for gifts and inheritances to children is reduced from EUR 159,325 to EUR 100,000 for gifts made from 18 August 2012. However, the allowance for gifts by disabled persons will remain at EUR 159,325. The statute of limitations regarding inheritances and donations is raised from 10 to 15 years, also with effect from 18 August 2012.

– Non-French tax residents who receive income from French real estate will be liable for French social contributions amounting to 15.5%. This measure is applicable to French rental income received from 1 January 2012 and to French real estate capital gains realised from 18 August 2012.

– The specific social contributions paid by companies on the grant date of stock options and free-shares will be increased from 14% to 30%, for options and free shares granted from 11 July 2012. The specific social contributions paid by the employee at the sale date on the exercise/vesting gain is increased from 8% to 10% from 18 August 2012.

– The planned increase in the standard rate of VAT from 19.6% to 21.2% has been abolished.

CHANGES TO CORPORATE TAXES

– Until recently, companies that contributed to employee investment funds to a greater extent than that required by the law are, under certain conditions, able to deduct this amount from their taxable profits. This favourable treatment is abolished for fiscal years ending from 17 August 2012.

– There will be an additional 3% Corporation Tax contribution on dividends distributed from 17 August 2012 by French or foreign companies and entities subject to French Corporation Tax. This 3% dividend tax would not increase the withholding tax rate already applicable to dividends and branch profits within domestic provisions or double tax treaties, if any, but is rather regarded as the introduction of a dual CIT rate: one for non-distributed profits liable to the effective CIT rate (i.e. the standard CIT rate, currently 33.1/3%) and one for distributed profits liable to the effective CIT rate + 3%. The 3% dividend tax will not apply in the following circumstances:

  – dividend payments made for collective investment funds;

  – dividend payments made to small or medium-size enterprises;

  – dividend payments made to a company belonging to the same French tax consolidated group (note that setting up a French tax consolidated group requires, among other conditions, a minimum 95% direct or indirect shareholding); and

  – dividends paid in shares.

– Advance payment of the exceptional Corporation Tax contribution for fiscal years ending between 31 December 2011 and 30 December 2013 will be required for companies with a turnover greater than EUR 250 million. The effective CIT tax rate, including this exceptional contribution, will amount to 36.1%.

– A financial transactions tax will be levied on transfers of shares of companies listed on the French stock exchange where the market capital of the company whose stocks are transferred exceeds EUR 1 billion on 1 January in the year of the taxation of the transfer, no

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EDITOR'S LETTER

Welcome to this issue of *BDO World Wide Tax News*. This newsletter summarises recent tax developments of international interest across the world. If you would like more information on any of the items featured, or would like to discuss their implications for you or your business, please contact the person named under the item(s). The material discussed in this newsletter is meant to provide general information only and should not be acted upon without first obtaining professional advice tailored to your particular needs. *BDO World Wide Tax News* is published quarterly by Brussels Worldwide Services BVBA in Brussels. If you have any comments or suggestions concerning *BDO World Wide Tax News*, please contact the Editor via the BDO International Executive Office by e-mail at mderouane@bwsbrussels.com or by telephone on +32 (0)2 778 0130.

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matter where the buyer, seller or transaction is located. The tax applies from 1 August 2012, and has been increased from 0.1% to 0.2% of the purchase price of the stocks. This tax is identical to the one proposed in the European Directive.

CORPORATE ANTI-AVOIDANCE MEASURES

– Two new measures have been introduced in order to limit the possibility of exploiting losses:

1. An additional criterion has been introduced for the request of the transfer of losses carried forward within a group reorganisation scheme, with regard to the identity of the activity for which the transfer of the losses carried forward is requested. As a consequence, the new conditions to request a transfer of losses under Article 209 II of the French tax code are as follows:

   – the restructuring falls within the ambit of the favorable tax regime for mergers;

   – the restructuring is economically justified;

   – the receiving company makes the commitment to retain the loss-making activity for at least 3 years; and

   – the activity which incurred the losses should not have suffered "significant modifications", both in the past, while the losses carried forward were incurred, and also in the future, during the three year period during which the receiving company has to retain the loss-making activity.

2. Introduction of objective criteria for the disqualification of losses where companies have changed their activity: A "significant change in the company's activity" is now defined as follows:

   – the disappearance/disposal of the industrial means necessary for the continuation of an activity for a period exceeding 12 months, or prior to the sale of a majority of the shares of such company, except when such event is economically justified;

   – the addition of a new activity to the former activities which incurred the losses carried forward, when either the global turnover of the company increases by more than 50%, or the global assets and employees of the company increase by more than 50%. These criteria should be reviewed for the fiscal year during which the new activity has been added and the following fiscal year; and

   – similarly, the abandonment or the transfer of an activity which decreases either the global turnover of the company by more than 50%, or the global assets and employees of the company by more than 50%. These criteria should be reviewed for the fiscal year during which the new activity has been added and the following fiscal year.

In order to mitigate the adverse tax consequences of this new provision, prior administrative approval can be sought to secure the losses carried forward further to a restructuring. The prerequisites in order to benefit from this prior approval are that the operations which led to the decrease/increase of the turnover or of the assets/employees of the company are necessary for carrying on the activity which incurred the losses, and for safeguarding the remaining employments in the company.

These provisions entered into force for fiscal years closing from 4 July 2012.

– In a common tax avoidance scheme (known as a "coquillard"), subsidiaries were stripped of all value using dividends which were tax-free under the mother-daughter regime, and a capital loss was then claimed on the reduced value of the shares in the subsidiary. To counter this scheme, the following measures are introduced:

  – any dividends paid by a company whose shares are booked as inventories in the accounts of a real estate dealer company are excluded from the participation exemption regime;

  – losses/depreciation instalments incurred by holding companies on any of their financial company subsidiaries are not tax-deductible up to the amount of dividends received during the current fiscal year and the five previous fiscal years; and

  – losses incurred by companies which merge with their subsidiaries within a period of 2 years after their incorporation are not tax deductible up to the amount of dividends received from the subsidiary.

– For fiscal years ending from 31 December 2012, French companies with branches or companies located in non-EU states with a preferential tax regime will be required to prove that the principal objective of their branches is notably genuine industrial or commercial activity, or have the income of these branches taxed in France.

– New rules have been introduced to prevent waivers of debt of a financial nature from being deductible. Previously, in some circumstances, it was possible for a company to reduce its overall tax bill by waiving a debt it was owed by a foreign subsidiary. The new provisions discourage such strategies, without preventing companies of the same group from providing each other with legitimate aid. Loans of a commercial nature remain deductible, and parent companies wishing to support their subsidiaries in financial difficulty will instead be encouraged to recapitalise.

CARINE DUCHEMIN
cduchemin@djp-avocats-bdo.fr
+33 1 80 18 10 80

ALAIN JOUAN
ajouan@djp-avocats-bdo.fr
+33 1 80 18 10 80

CHINA

FURTHER GUIDANCE ON DETERMINING BENEFICIAL OWNERSHIP UNDER TAX TREATIES

The issue in 2009 of tax circular Guo Shui Han (2009) No. 601 ("Circular 601") gave rise to concerns and uncertainties as to whether foreign investors would qualify as a "beneficial owner" for the purpose of enjoying the preferential tax treatment under a tax treaty. The China State Administration of Taxation has now issued Announcement No. 30 on 29 June 2012 ("Announcement 30"), providing further guidance on determining beneficial ownership in the context of qualifying for China tax treaty benefits. Announcement 30 took effect on its date of issue, and the salient points mentioned in the Announcement are highlighted below.

According to Circular 601, a non-resident recipient of certain China-sourced passive income (e.g. dividends, royalties, and interest) must be the beneficial owner of such income in order to enjoy the benefits (such as a preferential withholding tax rate) under the relevant tax treaty with China. Circular 601 provides a list of unfavourable factors that will be considered by the Chinese tax authorities when assessing whether the non-resident recipient is the beneficial owner. However, Circular 601 provided no further guidance on how to apply these unfavourable factors. Announcement 30 has now provided this guidance.

TOTALITY APPROACH WHEN ASSESSING BENEFICIAL OWNERSHIP

According to Announcement 30, the determination of beneficial ownership should be based on a totality approach under the 'substance over form' principle. No single factor should outweigh other unfavourable factors as stated in Circular 601 when concluding whether beneficial ownership exists. One cannot rely on the ground of "non-existence of objectives of tax evasion or reduction, or profit transfer or accumulation, etc" to conclude the existence of beneficial ownership. In reviewing the factors on a totality approach, according to Announcement 30, reference can be made to the relevant legal and financial documents such as articles of association, financial statements, board resolutions and minutes, functional and risks analysis, legal contracts, patent and copyright ownership certificates, and other relevant documentation.

SAFE HARBOUR PROVISION FOR DIVIDEND WITHHOLDING TAX RELIEF

According to Announcement 30, if a company is a tax resident of the other contracting state under the relevant tax treaty with China, and is publicly listed in the jurisdiction of that contracting state, the company is automatically regarded as the beneficial owner of Chinese dividends that it receives and, accordingly, is entitled to the preferential dividend withholding tax treatment provided under the tax treaty (a safe harbour provision).

Furthermore, a company which satisfies the following conditions may also be automatically regarded as the beneficial owner of Chinese dividends that it receives and hence entitled to the relevant tax treaty benefit:

(i) The company is 100% directly or indirectly owned by its parent company which is a tax resident of the other contracting state under the relevant tax treaty with China, and the parent company is listed in that contracting state; and

(ii) The company is a tax resident of the same contracting state in which its listed parent company resides.

However, if the company is indirectly owned by the listed parent company, and the intermediate holding company is not a tax resident of the same contracting state in which the listed parent company resides, the above safe harbour provision does not apply.

AGENCY AND NOMINEE

According to Announcement 30, if an agent or designated payee receives income for its principal party, this agency relationship should not affect the determination of beneficial ownership status of the principal party. The agent should declare to the China tax authority that it is not the beneficial owner of the income received.

CONCLUSION

Announcement 30 is undoubtedly welcome, in particular, the introduction of the safe harbour provision for listed groups. Current group structures should be reviewed to ensure that they benefit from the safe harbour provision and other issues arising from Announcement 30.

ALFRED CHOI
alfredchoi@bdo.com.hk
+852 2218 8213

ANTHONY HUNG
anthonyhung@bdo.com.hk
+852 2218 8293

NEW ZEALAND

PROPOSED SIMPLIFICATION OF FOREIGN PENSIONS

The Inland Revenue and Treasury have published proposals to simplify the taxation of receipts from defined contribution or defined benefit foreign pension schemes held by New Zealand residents, with the aim of improving the fairness and consistency of the tax treatment.

Receipts from such schemes would no longer be taxed on an accruals basis under the complex foreign investment fund (FIF) rules. Instead, new rules would provide that:

- Pension payments would be taxed at an individual's marginal tax rate when the payments are received;
- Lump sums would be partially taxed using an "inclusion rate". The excluded amount would not be taxable. The taxable amount would depend on the length of time between when an individual arrives in New Zealand and when they withdraw or transfer the superannuation. At the time of the withdrawal or transfer from a foreign superannuation scheme, they would apply the relevant inclusion rate based on the date they became a New Zealand-resident as follows:

Years since migration	Inclusion rate
0-2	0%
3-4	15%
5-8	30%
9-12	45%
13-16	60%
17-20	75%
21-24	90%
25+	100%

An individual's marginal tax rate would be applied to the amount that results after applying the inclusion rate. For example, an individual with a marginal tax rate of 33% who makes a withdrawal of NZD 50,000 when they have been a New Zealand-resident for eight years would have a tax liability of NZD 4,950 (NZD 50,000 x 30% inclusion rate x 33% tax rate). In this case, this represents an effective tax rate of approximately 10%. Tax credits for any foreign tax paid would continue to be available, but only in proportion to the amount of New Zealand tax payable on the lump sum and subject to other relevant limitations;

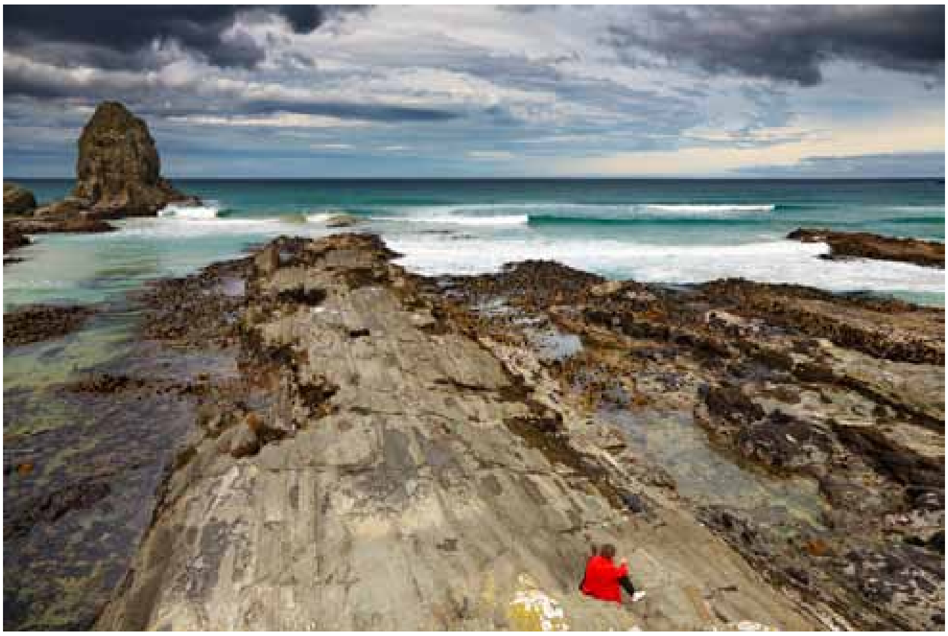
- The temporary exemption for transitional residents would continue to apply to receipts from foreign superannuation schemes. Other rules that exempt Australian superannuation in certain circumstances (such as the New Zealand-Australia double tax agreement, and the arrangement on trans-Tasman portability of retirement savings) will also remain unchanged.

The proposed new rules would apply from the 2011–12 income year. However, individuals who returned FIF income from their foreign superannuation for the 2010–11 income year by 31 March 2012 would continue to have that interest taxed under FIF rules. They would not be taxed on any subsequent distributions under the new rules.

A retrospective measure would allow people who withdrew foreign superannuation as a lump sum between 1 January 2000 and 31 March 2011, and who did not comply with their tax obligations at the time, to elect to use an inclusion rate of 15% for their withdrawal or transfer. To qualify, an individual would have to disclose the existence of the transfer to the Inland Revenue before 1 April 2014. Alternatively, they could choose to return income under the rules which existed at the time.

The Inland Revenue has invited submissions on the proposals, which it is hoped will be included in a tax bill scheduled for introduction later in 2012 or towards the middle of 2013.

IAIN CRAIG
iain.craig@bdo.co.nz
+64 9 373 9612



SRI LANKA

TAX CHANGES FOLLOWING 2012 BUDGET

The 2012 Budget Proposals have been given legal effect by way of amendments to the relevant tax legislation in April 2012. The key changes are summarised below.

CORPORATE TAX

The general tax rate of 28%, and the concessionary rate of 12% for exporters, tourism and construction, remain unchanged for the 2012/13 year of assessment. The concessionary rate is extended to additional sectors including health care, handloom manufacturing and infrastructure projects in electricity and telecommunications.

The 10% tax rate for SMEs introduced last year is not available in the 2012/13 year of assessment to a company belonging to a group, to prevent manipulation of revenue amongst group companies.

Capital allowances for high tech plant, machinery or equipment that is energy efficient have been enhanced from 33.33% to 50%, with effect from 1 April 2012.

The foreign travel expenses deduction for exporters of goods or services has been extended to other businesses, with restrictions on the maximum allowable amount. Restrictions on management fees and pre–commencement expenses have been partly relaxed.

Interest arising to a person outside Sri Lanka on any loan granted to the Government of Sri Lanka, any public corporation, any Government institution or any commercial bank is exempt from income tax with effect from 1 April 2012. Accordingly, the withholding tax provisions would not apply.

Also with effect from 1 April 2012, any Royalty received by an entity in Sri Lanka from a person outside Sri Lanka is exempt from income tax if it is remitted to Sri Lanka through a bank in foreign currency.

INDIRECT TAXES

VAT

The scheme introduced last year, under which zero-rated exporters and approved projects can obtain refunds of VAT paid, remains in force.

With effect from January 2012, exempt businesses can set off unabsorbed VAT input tax credits against other taxes administered by the Commissioner General, up to a maximum of 30% of the credit per quarter.

The exemption for local textile and fabric manufacturers has been extended to businesses that provide services of improving the character, value and quality of the fabric or garment, with effect from 1 April 2012. This is a boost to the local textile manufacturing industry.

NBT

Exporters are exempt from Nation Building Tax (NBT). However, there was an anomaly as to whether this exemption applied to exports made through a "Trading House" established for export purposes. An amendment has been introduced in March 2012 extending the exemption to such trading houses, with retrospective effect from January 2009.

Imports of aircraft and ships were exempted from VAT, but not NBT, with effect from July 2007 and January 2006 respectively. An amendment to the NBT law in March 2012 exempts these imports from NBT at the point of importation with retrospective effective from August 2009.

ESC

The Economic Service Charge (ESC) is charged on the turnover of every business at different rates, ranging from 0.25% to 1%. The tax charged is allowed as a deduction against the corporate tax payable by such businesses. With effect from 1 April 2012, ESC is not payable by businesses that are liable to income tax.

KUMAR RAJ
kumarraj@bdo.lk
+94 11 242 1878

BELGIUM

THIN CAP RULES STRENGTHENED

The Belgian thin capitalisation rules have been strengthened with effect from 1 July 2012.

The former thin cap rule provided for a 7 to 1 debt/equity ratio, but only for loans where the beneficial owner of the interest is not subject to income tax or where it is subject to a tax on such interest income that is substantially more beneficial than in Belgium.

From 1 July 2012, interest expenses on intra-group loans will no longer be tax deductible to the extent that a 5 to 1 ratio has been exceeded.

In order to determine the debt/equity ratio, the following definitions should be applied:

- Debt includes all inter-company loans (with the exclusion of bonds, other debt issued by public offering and loans granted by financial institutions) and also third party loans secured by group companies.
- Equity is considered as the sum of the taxed reserves at the beginning of the taxable period and the paid-up capital at the end of the taxable period.
- A group comprises all affiliated companies as defined by Belgian company law. Companies are legally deemed to be affiliated when one company has control over the other or is being controlled by the other, or when they are part of a consortium (jointly controlled).
- Control is defined as the legal or factual power to have a decisive influence on the appointment of the majority of the members of the Board of Directors or on the policy of the company.

Qualifying cash pooling companies can apply a netting system to determine the amount of the interest expense being subject to the thin cap rule (equal to the difference between the interest income and interest expense, realised in the framework of the group cash pooling activity).

MARC VERBEEK
marc.verbeek@bdo.be
+32 2 778 01 00

CYPRUS

NEW TAX INCENTIVES

A number of new tax incentives were voted by the House of Representatives on 24 May 2012. These incentives aim to make Cyprus a preferred intellectual property (IP) holding jurisdiction and to enhance its position as a location for financing companies. They also make Cyprus attractive for the importation of private aircraft in the EU when used for business purposes and enable the acquisition of new private residences at the reduced VAT rate of 5%.

1. Intellectual property (effective from 1 January 2012)

The Income Tax Law has been amended to provide generous tax exemptions for income related to IP. In particular:

(i) 80% of any income from IP owned by Cypriot resident companies (net of any direct expenses) will be exempt from income tax;

(ii) 80% of profits from the disposal of IP by Cypriot resident companies (net of any direct expenses) will be exempt from income tax;

(iii) the definition of IP includes all intangible assets, including copyrights, patents and trademarks; and

(iv) any capital expenditure in relation to the acquisition or development of IP will be allowed as a deduction in the tax year in which it was incurred and the immediate four following years, on a straight-line basis.

2. Deductibility of interest (effective from 1 January 2012)

Interest incurred for the acquisition of 100% of the share capital of a subsidiary company (direct or indirect) will be deductible for income tax purposes provided that the subsidiary company does not own any assets that are not used in the business. Loans receivable are deemed to constitute assets that are used in the business.

If a subsidiary company owns assets that are not used in the business, interest incurred by the Cyprus tax resident parent company in relation to such assets will not be tax-deductible.

Assets not used in the business include shares and other securities as defined under the Law, income from which is generally exempt from taxation in Cyprus under other provisions of the Law.

Shares acquired before 1 January 2012 which previously attracted a restriction of interest for seven years will remain under the 7-year rule.

3. Incentives to capital investment

Machinery and equipment acquired during the tax years 2012, 2013 and 2014 will be eligible for accelerated tax allowances at the rate of 20% per annum (increased from 10%).

Tax allowances at the rate of 7% per annum (increased from 4%) may be claimed for industrial and hotel buildings which are acquired during the tax years 2012, 2013 and 2014.

The acquisition cost of machinery, equipment and buildings will be treated as deductible from accounting profits for deemed distribution purposes. This is relevant only to companies whose ultimate beneficial shareholders are Cyprus residents.

4. Group relief

Where a subsidiary company is incorporated by its parent company during a particular tax year, the subsidiary company will be treated as being a member of the group for the whole tax year and will therefore be able to claim group relief for that tax year, with effect from 1 January 2012.

5. Contributions to Funds

Contributions to Pension Funds, Provident Funds or any other Insurance Funds will be deductible in calculating the taxable income of an individual with effect from 1 January 2012, provided that such Funds are approved by the Commissioner of Income Tax.

6. VAT on private aircraft

Private aircraft can be imported from a place outside the EU without payment of VAT on importation. This applies when the importer is a taxable person and the importation takes place within the context or for the promotion of his business activity.

The VAT arising on importation need only be reported in the VAT return of the taxable person if no cash outflow is created as a result of the importation of the aircraft into Cyprus. The Commissioner can demand a guarantee from the importer, which must not exceed the amount of VAT chargeable on the importation of the aircraft.

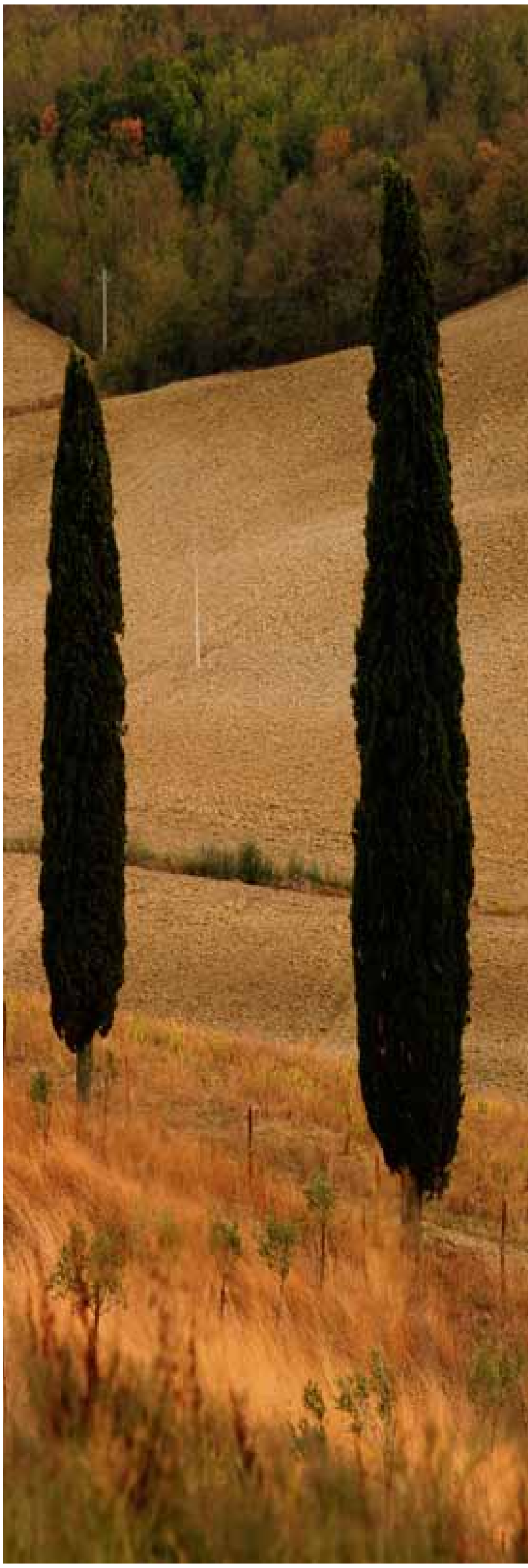
Aircraft that are used by an airline engaged mainly in the international transportation of passengers for profit continue to be subject to VAT at the zero rate.

7. VAT incentives for the acquisition and/or construction of residential properties

The reduced VAT rate of 5% which applies to the construction or acquisition of residential property that is used as the primary and permanent place of residence is extended from 8 June 2012 to include acquisitions by individuals who do not ordinarily reside in Cyprus but acquire the property to use as their residence whilst in Cyprus.

KARLOS ZANGOULOS
kzangoulos@bdo.com.cy
+357 2249 5707

ANGELOS PETROU
apetrou@bdo.com.cy
+357 2249 5707



IRELAND

SPECIAL ASSIGNEE RELIEF PROGRAMME IMPROVED

With a view to continually increasing Ireland's competitiveness on the international stage, and in order to attract the necessary business and key skills to Ireland, the Government has introduced a new and improved Special Assignee Relief Programme (SARP).

EXISTING SARP SCHEME

The previous SARP relief continues to apply up to 31 December 2015 where individuals are eligible for the relief in 2009, 2010 or 2011. This incentive provided limited relief for individuals coming to work in Ireland for the first time. This old SARP applied only to non-Irish domiciled individuals with earnings in excess of EUR 100,000 per annum and, as those earnings had to be paid outside of Ireland, this often proved a difficulty for multinationals based in Ireland who wished to directly employ individuals within the Irish operation.

NEW SARP SCHEME

The new SARP relief is aimed at improving the terms of the relief to match similar regimes in other countries.

The relief applies for individuals who arrive in Ireland in 2012, 2013 or 2014 to work here for a minimum period of 12 months and has the following key features:

- Qualifying individuals will be entitled to exclude 30% of employment earnings over EUR 75,000 from the charge to Irish tax. The maximum earnings upon which relief may be claimed is EUR 500,000.
- The relief applies to Irish domiciled and non-Irish domiciled individuals.
- The relevant employer must have been a company incorporated and tax-resident in a country with which Ireland has a double tax treaty or in a country with which Ireland has a tax information exchange agreement.

The employee must:

- Have been employed for at least 12 months by their foreign employer prior to arriving in Ireland;
- Perform the duties of their employment in Ireland for 12 consecutive months;
- Not have been tax resident in Ireland for the 5 tax years prior to their arrival in Ireland; and
- Earn a minimum base salary (excluding bonuses, share awards and benefits-in-kind) of at least EUR 75,000 from this employment.

The relief does not extend to the Universal Social Charge or Pay Related Social Insurance, where applicable. The individual is required to submit an annual tax return in order to claim the relief. However, relief may be granted at source through payroll, provided that prior approval has been received from the Revenue Commissioners.

While the relief must be claimed by the employee, the employer must certify that the relevant conditions to qualify for the relief have been satisfied.

Individuals that qualify for this relief are also entitled to recover the cost of a return trip to their home country for them and their families from their employer tax-free. In addition, school fees (of up to EUR 5,000 for each child) may be paid tax-free by their employer

EXAMPLE

John is employed by a US Multinational under a US contract of employment for 8 years up to 31 December 2011. On 1 January 2012, John is assigned to the Irish Subsidiary and will devote his time to developing the Irish operations. The assignment is expected to last for 4 years.

In 2012 John has the following remuneration package:

	EUR
– Base salary	250,000
– Company Car BIK	12,500
– Bonus	60,000
– Share Award	20,000
– School fees	4,000 *
– Private Travel costs	3,000 *
Total Package	**349,500**

**Tax relief is available for school fees and travel costs home.*

Under the new SARP Regime, the deduction would be:

(EUR 342,500 - EUR 75,000) x 30% = EUR 80,250

The tax repayment due would be 41% of this amount, i.e. EUR 32,903.

John must submit an annual income tax return in Ireland for 2012, which is due for submission on or before 31 October 2013.

KEVIN DOYLE
kdoyle@bdo.ie
+353 1 4700 271

CIARÁN MEDLAR
cmedlar@bdo.ie
+353 1 4700 271

DIRECTOR'S FEES AND IRISH INCORPORATED COMPANIES

Following a period of review, the Irish Revenue Commissioners have clarified their position regarding the Irish tax treatment of income arising from an individual having or exercising the public office of director of an Irish incorporated company.

Revenue have confirmed that a director (including non-executive directors and non-Irish resident directors of an Irish incorporated company) are within the charge to Irish income tax and Universal Social Charge (USC). Furthermore, tax must be withheld at source under the PAYE/USC systems. In very limited circumstances, fees paid to a non-resident director may be relieved from the Irish tax charge under a double tax treaty.

The position in relation to what Revenue describe as the "mandating, allocating, directing, routing, etc to a "third party" (e.g. to a firm or company) of remuneration arising from an individual having or exercising an office or employment is also covered. Revenue state that such arrangements do not bring the remuneration outside the Irish tax net or the requirement for the relevant company to deduct tax at source.

Situations where Irish incorporated companies have non-Irish resident directors on their board should be reviewed, and tax compliance re-examined. Company recharges or management charges of various expenses within a group, including the provision of a director(s) to an Irish incorporated company, should also be examined in light of the above clarification.

KEVIN DOYLE
kdoyle@bdo.ie
+353 1 4700 271

NETHERLANDS

PARTICIPATION DEBT INTEREST LIMITATION

Some of the Dutch government's 2013 Budget proposals will affect international groups. Proposals to limit the deductibility of interest on participation debt will affect Dutch companies financed with debt.

Currently, interest on loans in relation to the acquisition of subsidiaries ('participation debt') is generally tax-deductible. For qualifying subsidiaries, dividends and capital gains derived from the participation in that subsidiary are exempt, based on the participation exemption rules. According to the government, this is not always a balanced situation, especially where excessive interest arises on debt used to finance the acquisition of subsidiaries. In June 2012 the Government proposed new rules to change this situation, which should take effect from 1 January 2013.

PARTICIPATION DEBT INTEREST LIMITATION

The proposal is that interest on participation debt will not be tax-deductible insofar as such interest exceeds EUR 750,000. Participation debt is defined as the excess amount of the cost price of the taxpayer's participations over the taxpayer's equity for Dutch corporation tax purposes. 'Participations' in this context means participations that qualify for the participation exemption. The limitation will not be applicable to debt subject to other interest deduction limitations.

The excessive interest is calculated by means of a formula:

$$\text{interest costs} \times \frac{\text{average amount of participation debt}}{\text{average amount of total debt}}$$

In addition to interest expenses, the new rule also catches hedging costs and foreign exchange differences with regard to such interest, so these also need to be included in the above formula. The average is calculated using the relevant amounts at the beginning and end of the taxpayer's accounting year.

It should be noted that finance leases and hire purchase contracts, as well as loans, are within the scope of this provision.

The interest deduction limitation is therefore a mathematical, dynamic concept that can be influenced by matters such as losses and profits made by the entity holding the subsidiaries. Although this has nothing to do with the financing of the subsidiaries, it can lead to a higher or lower interest deduction limitation.

The cost price of subsidiaries comprises the actual purchase price, costs related to that purchase, and capital injections (including informal capital injections). The cost price will be reduced when capital is repaid by the subsidiary. Furthermore, when subsidiaries are not valued at cost price in the accounts, this needs to be recalculated for the purposes of the proposed rule. This may be quite difficult in the case of older acquisitions.

EXCEPTION FOR EXPANSION INVESTMENTS

Debt used to finance so-called 'expansion investments' is excluded in the calculation of participation debt. As a result, insofar as the debt relates to the acquisition or expansion of the interest in an operational subsidiary, the interest on this debt is deductible. Examples of operational activities are production, distribution and sales activities. Interest on debt used for a capital injection in an operational subsidiary also falls outside the scope of the limitation.

Interest on the loan is only deductible insofar as the amount is used for expansion or diversification of operational activities. Whether or not expansion investments are made is to be examined at group level. 'Group' in this respect means the taxpayer and its related entities, in which there should be an (in)direct interest of at least one third. The expansion investment or the capital injection should relate to an expansion of the operational activities of the group at that time, or in a preceding or subsequent twelve month period. This could also be applicable for expansion investments made prior to the introduction of this rule. Furthermore, it may not always be easy to point specifically to the expansion of operational activities, especially when the activities of a subsidiary grow continuously.

To simplify matters, a special rule is proposed for old investments. The taxpayer is allowed to choose that 90% of the purchase price of a subsidiary can be ignored for the calculation of participation debt if and to the extent that the acquisition or additional investment into that subsidiary took place before 1 January 2006.

SITUATIONS THAT ARE NOT CONSIDERED EXPANSION INVESTMENTS

The following situations cannot benefit from the expansion investment exclusion:

- When it is likely that the interest is deducted twice (double dip);
- When a hybrid loan (e.g. a profit participating loan) is provided to the subsidiary; and
- When the financing is artificially constructed specifically in order to obtain the interest deduction.

Whilst the first two exclusions are relatively straightforward, the third could lead to difficult discussions with the Dutch tax authorities, as it concerns a main purpose test. Only the second exception can be avoided via a rebuttal that whilst the interest on the loan is deductible, the interest income received is subject to at least 10% corporate income tax (measured according to Dutch accounting standards) at the level of the creditor.

PERMANENT ESTABLISHMENTS

It is stipulated that this provision does not cover loans that are to be attributed to a permanent establishment abroad.

ACTIVE FINANCING COMPANIES

Taxpayers that are mainly engaged in active group financing activities are excluded from the application of the proposed interest limitation rule to the extent that the debt finance relates to loans granted as part of these activities. For companies to be considered active they must employ their own personnel, in line with the nature and function of the company, and they must have business premises equipped with the facilities that are commonly used in the financial sector.

ENTRY INTO FORCE

The new rule is expected to enter into force on 1 January 2013. The proposal is being discussed in Parliament so the final rule may be subject to change.

HANS NOORDERMEER
hans.noordermeer@bdo.nl
+31 10 24 24 660

PORTUGAL

EXPATRIATE TAX RULES RELAXED

The Portuguese Revenue has issued a circular announcing relaxations in the requirements for foreigners applying for the special expatriate tax regime which is available to 'non-habitual residents' who, when becoming tax-resident in Portugal, have not been subjected to personal income tax in Portugal as residents in the previous five years..

The special regime was introduced in 2009, with the aim of attracting high net worth individuals to Portugal. Eligible high net worth individuals, who may be employed or self-employed, are subject only to a 20% flat rate tax on their Portuguese-source income, and are exempt from Portuguese tax on their foreign income, for a 10-year period.

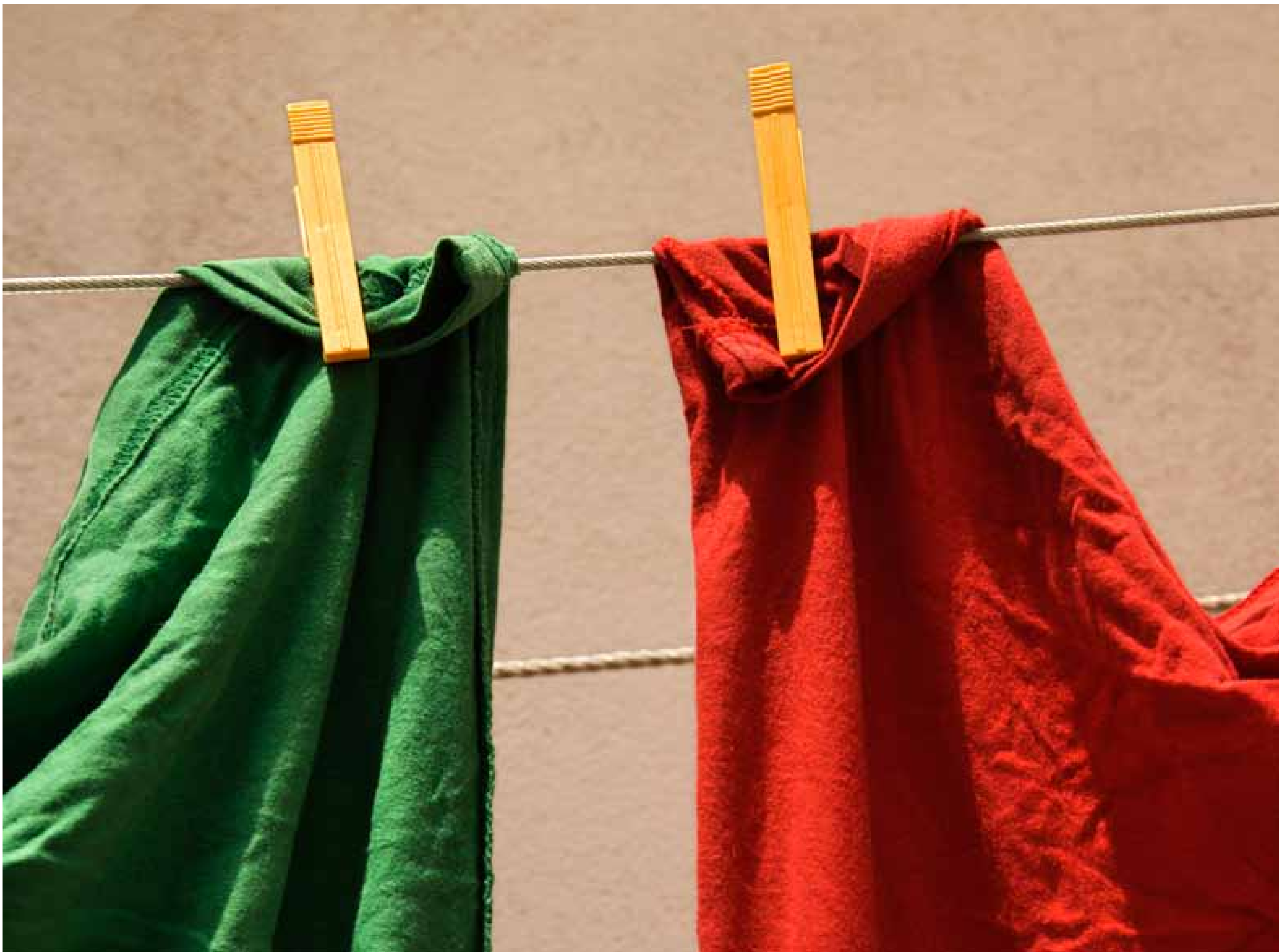
The main qualifying condition is that the individual must not have been resident in Portugal for tax purposes in the five years before applying for treatment under the special regime. Until recently, it was a requirement to provide documentation from a foreign tax authority confirming that the individual had been resident abroad, and that their foreign income had been effectively taxed before and after they commenced residence in Portugal.

However, the new circular states that it will now only be necessary for the individual to provide a declaration that they were previously resident abroad. The Portuguese Revenue will then only request further evidence if it has reason to believe that the declaration may not be correct. This relaxation should particularly help internationally mobile individuals who may have lived in several different jurisdictions during the previous five years.

In addition, the operation of the scheme will be more straightforward, with a 20% withholding tax now applying to Portuguese income, instead of the former procedure under which eligible individuals were initially subject to tax at normal rates and were then required to claim refunds.

The government hopes that these relaxations will help to attract high net worth individuals to Portugal, bringing much-needed funds into the country.

PAULO FERREIRA ALVES
paulo.alves@bdo.pt
+351 217 990 436



SPAIN

GOVERNMENT APPROVES TAX AMNESTY

On 30 March 2012 the Spanish Government approved new tax and administrative measures to reduce the public deficit. One of the most discussed measures was a special voluntary disclosure method commonly known as a "tax amnesty".

This amnesty will enable Spanish taxpayers to disclose assets (or rights to assets) that have been acquired with funds that were not declared to the tax authorities in the tax periods in which they were generated, and that were owned by taxpayers (i.e. real or economic ownership) on 31 December 2010 (in the case of tax resident individuals) or on the closing date of the last tax period that ended before 31 March 2012 (in the case of tax resident companies and non-resident companies or individuals).

Furthermore, the amnesty covers cash amounts, as long as the taxpayer declares that he or she owned these prior to 31 December 2010, if these amounts were transferred to an account at a bank or credit institution that is tax resident in Spain or a Member State of the EU or the EEA that has signed a Double Tax Treaty with an exchange of information clause, except for territories that are listed as high risk, deficient or non-cooperating jurisdictions by the Financial Action Task Force.

In contrast to the general voluntary disclosure method (i.e. the filing of amended tax returns), amounts disclosed under the amnesty will be subject to a fixed tax rate of 10% of the acquisition value of the relevant assets or rights, rather than to progressive tax rates or the significantly higher tax rates applicable to corporations and non-residents under the general method. If the required special tax return is filed with the Spanish tax authorities by 30 November 2012, the authorities have expressed that no penalties, surcharges or late payment interest on such tax will be charged.

It must be stressed that the amnesty merely covers taxes on income. The tax authorities therefore still have the right to audit the transactions that gave rise to the acquisition of the relevant assets and rights from an indirect tax perspective (i.e. VAT, transfer tax and capital duty purposes), as well as from an inheritance, gift and wealth tax perspective.

The Government has stated that taxpayers who have undeclared wealth and who do not use the current opportunity to regularise the situation will have to face increased penalties and criminal procedures if challenged after 30 November 2012.

It should also be stressed that the Association of Spanish Tax Inspectors does not wholly agree with the guidelines for the tax amnesty published by the Ministry of Finance and Public Administrations on 27 June 2012 and stated to apply to all the mechanisms available for investigating and identifying any hidden wealth. In addition, the Spanish Labour Party (Partido Socialista Obrero Español) has filed several objections to this measure before both the National and the Constitutional Court., It will therefore be interesting to see how the regulations concerning the amnesty develop in the next couple of months. Nevertheless, taxpayers that may be affected by this measure should seek professional advice in order to review their tax risks and seek the most appropriate solution.

TAX BENEFITS FOR FILMS "MADE IN SPAIN"

Films "made in Spain" may benefit from a very advantageous tax incentive consisting of a tax credit of 18% on the film production costs. The incentive is aimed at encouraging private investors to participate in the development of the film industry in Spain by benefiting from such tax credits. The interpretation of the provisions of the Corporate Income Tax (CIT) law given by the General Tax Directorate provides that such investments can be made through either Venture Capital or Joint Ventures that have the legal form of Spanish Agrupaciones de Interés Económico (AIE), which may operate as transparent entities in certain cases. Apart from the tax credit, investors holding interests in an AIE may also benefit from tax losses that the AIE may generate during the first years of production.

Specifically, the tax credit amounts to 18% of total production costs (excluding subsidies and distribution or advertising costs) for film producers, and 5% of such costs for financial co-producers, as long as the following requirements are met:

- The investments must be used for the production of Spanish films, i.e. films mainly shot on Spanish territory, by Spanish producers and with Spanish actors.
- The tax credit will be increased to 38% for producers that are established in the Canary Islands, and 25% for financial co-producers established in that territory, if the following additional requirements are met:
  - The Canary Island co-producer must participate with a principal actor/actress or a secondary actor/actress or a technician that is resident in the Canary Islands, and the majority of the employees must also be resident in the Canary Islands.
  - The production activities must take place in the territory of the Canary Islands for at least two weeks.

LIMITED RISK DISTRIBUTOR: SPANISH COURTS INCREASE THE PE EXPOSURE

On 12 January 2012, the Spanish Supreme Court issued a ruling stating that a Swiss pharmaceutical company, operating in Spain through a subsidiary, triggered a Permanent Establishment (PE) on the grounds that the contracts signed between both entities meant that the Swiss company was effectively operating in Spain. This ruling may have an impact for other multinational companies - in particular, pharmaceutical, life science and medical device companies that operate in Spain through manufacturing or distributing subsidiaries.

On the basis of the above Judgment, the Central Economic and Administrative Court (TEAC) issued a very detailed decision in June 2012 in which it analyses the PE risk of a Spanish subsidiary that acts as commission agent of its Irish shareholder which, in turn, acts as distributor of an Irish hardware manufacturer for the EMEA Region.

The analysis of the two Courts has been made on the basis of the OECD Commentaries on the Model Tax Convention, but the decision of the TEAC stresses the strict criteria applied by the tax authorities in determining the concrete facts of the case, and also makes it clear that the tax authorities and the Spanish Courts will analyse the operational reality in detail and apply the substance over form principle in order to determine the existence of a PE.

Entities which use limited risk distributor or commission agent schemes to sell their products in Spain should therefore review their operational structures in order to identify potential risks and mitigate them, as far as possible.

NEW PROTOCOL AMENDING THE US-SPAIN DOUBLE TAX TREATY SIGNED

On 25 May 2012, the negotiations regarding the new Protocol amending the current US-Spain Double Tax Treaty, in force since 1 January 1991, resulted in a final text, as announced by the Spanish Ministry of Finance in a press release dated 4 June 2012. The new Protocol aims to foster cross-border investments between the two countries, achieve tax neutrality, prevent tax distortions and generally update the former tax treaty to adapt it to new business and economic circumstances.

It is expected that the new Protocol, which has not yet been published by the Spanish tax authorities, will change the taxation of capital gains arising on the transfer of shares, specifically in cases where U.S. companies hold a significant interest in Spanish entities, as Spain had a right to tax such gains. With regard to royalties, it is expected that the categories of royalties will be simplified and that a single tax rate of between 0% and 5% will be introduced (currently there are three different WHT rates of 5%, 8% and 10%, depending on the nature of the royalties). Concerning taxation of dividends, a 0% tax rate on dividend distributions is expected for holdings of at least 10% (under the current rules, dividends distributed to the U.S. are generally taxed at a rate of 15%, or 10% for holdings of more than 25%). Other aspects include bringing S Corporations and LLCs within the scope of the treaty and elimination of branch tax.

The Spanish Secretary of State for Finance confirmed in the press release that the new Protocol amended 14 articles of the former tax treaty. In addition, he emphasised that the new text will foster cross-border investments and adapt the convention to the new circumstances. He further confirmed Spain's promise to cooperate with the U.S. regarding the FATCA regulations.

It is expected that the Protocol will be officially signed and ratified by the Contracting States in the near future. Although it is difficult to predict a potential date for its entry into force, according to the trend observed in other ratification procedures, it is unlikely that this will be before 1 January 2013. However, companies currently engaged in operations involving Spain and the United States should be aware that the current tax treaty may change significantly in the near future.

EUGENIO GARCÍA
eugenio.garcia@bdo.es
+34 914 364 195

UNITED KINGDOM

RESIDENTIAL PROPERTY TAXATION CHANGES

The Government has published further information on its proposals to introduce a new annual tax on the value of residential properties worth over GBP 2 million which are owned by 'non-natural persons', and to extend the capital gains tax regime to disposals of such properties which are owned by non-resident non-natural persons. Both measures are intended to come into force in April 2013.

NEW ANNUAL CHARGE

The charge will apply to interests in residential property valued at over GBP 2 million owned solely or jointly by companies, partnerships with one or more corporate members, and collective investment vehicles. It will not apply to interests owned by:

- Trustees, other than bare trustees. Where a company is a bare trustee it will be transparent for this purpose, and whether or not the annual charge applies will depend on the status of the beneficial owner of the property;
- Charities; or
- Bona fide property development businesses, provided the business has been operating for at least two years, and the property was acquired for re-development and re-sale. HMRC has acknowledged the concerns that the charge could seriously affect many genuine property development businesses, and has asked for recommendations on how best to exclude such businesses.

The charge will apply pro-rata where an interest in a property is owned by a liable person for part of a tax year.

The value of the property for the purposes of the charge will be that on 1 April 2012 or a later acquisition date, plus the value on any later creation or cessation of a relevant subordinate property interest, with a revaluation every five years.

The proposed bands and charges for 2013/14 are as follows:

Property value	Annual charge 2013/14
GBP 2m - GBP 5m	GBP 15,000
GBP 5m - GBP 10m	GBP 35,000
GBP 10m - GBP 20m	GBP 70,000
GBP 20m+	GBP 140,000

The charge will be indexed to the Consumer Price Index in future years.

Payment will normally be due in advance, on 15 April each year, but for 2013/14 the due date will be 1 October 2013.

EXTENSION OF CGT REGIME

The CGT regime will be extended to gains made on UK residential property by non-resident non-natural persons, where the disposal consideration exceeds GBP 2 million. The categories of non-resident non-natural persons liable include:

- Companies and other corporate bodies;
- Trustees (excluding bare trustees but including trustees who are themselves individuals) and collective investment vehicles;
- Personal representatives;
- Clubs and associations; and
- Entities that exist in other jurisdictions that allow property to be held indirectly.

For non-UK resident companies that are currently liable to UK corporation tax (because, for example, they have a UK permanent establishment), gains arising from the disposal of UK residential property will be chargeable to corporation tax. For non-UK resident companies that are not liable to corporation tax, gains will be chargeable to CGT (rather than bringing these companies into the corporation tax regime).

Charities which are currently exempt from CGT will also be exempt from the new regime.

The extended regime will apply to gains on the disposal, or part disposal, of relevant UK residential property, including the grant of an option over such property. It will also apply to gains on the disposal of assets (of whatever form) that directly or indirectly represent relevant UK residential property, including shares, interests or securities in a property-owning company where more than 50 percent of the value of the asset is derived from UK residential property.

The applicable rate of tax will be announced at Budget 2013.

RICHARD MONTAGUE
richard.montague@bdo.co.uk
+44 20 7893 2213

ARGENTINA - CHILE

DOUBLE TAX TREATY TERMINATED

On 29 June 2012, Argentina notified Chile that it was unilaterally terminating the double taxation convention between the two countries, which has been in force since 1985. In common with other double tax treaties, this agreement provided that income, earnings or profits will normally only be taxed in the source country where the assets that generate the income are located or, in the case of personal services, where these services are provided.

In accordance with the provisions of Article 26 of the Convention, it will cease to have effect:

a) For individuals, from 1 January 2013; i.e. the beginning of the calendar year following the unilateral termination of the convention.

b) For companies, from the beginning of the fiscal year following the unilateral termination of the convention. This will be from 1 July 2012 In the case of Argentina, and from 1 January 2013 in the case of Chile.

The benefits granted under the agreement, such as the exemption from tax on personal property for residents in Chile who have assets in Argentina, will therefore no longer be available. Consequently, Chilean residents will begin to pay a 0.5% property tax on their participation or interest in Argentinian companies.

Although both parties will probably pursue the negotiation of a new double taxation agreement based on the OECD model treaty, the legislation in each country provides unilateral measures to mitigate double taxation, although not as effectively as the provisions of the former agreement.

In both Chile and Argentina, a system of ordinary credits exists in respect of taxes paid abroad, but with a narrower scope. For example, in the case of dividends and withdrawals of profits Chile grants a credit of up to 30% of the lower of the tax paid abroad or the amount actually paid. This credit is deductible from the First Category Income Tax (Corporate Tax), and if surpluses remain, these may be used either against the Global Complementary Tax or the Additional Withholding Tax. In the case of Argentina, the credit is 35% of the lower of the tax paid abroad or the amount actually paid, and a surplus can be carried forward.

With regard to the income of permanent establishments, and income from the use of trademarks, patents, formulas, technical consultancies and similar services paid abroad, the Chilean credit is the lower of the rate of the First Category Income Tax or the amount actually paid, which may only be imputed against the First Category Income Tax.

In Argentina, only foreign source income can be used as a tax credit against income tax paid abroad. Argentinian source income that is subject to the Chilean Withholding Tax is treated as a deductible expense.

ALBERTO F. MASTANDREA
amastandrea@bdoargentina.com
+54 11 5274 5100

RODRIGO BENÍTEZ CÓRDOVA
rbenitez@bdo.cl
+562 729 5002

CANADA

NEW TAX RETURN FILING RULES THAT WILL BENEFIT U.S. CITIZENS LIVING IN CANADA

There has been a lot of press coverage in Canada in the past 18 months regarding the obligation of U.S. citizens living abroad to continue to file U.S. personal income tax returns, as required under the Internal Revenue Code. For various reasons, some U.S. citizens have not kept up with their U.S. obligations, and many fear that substantial penalties could apply if they brought their U.S. tax filings up to date. The penalty issue was of particular concern for U.S. citizens resident in Canada, as many believed that the penalties could be substantial when compared with a relatively low or non-existent U.S. tax liability (once Canadian taxes and the related foreign tax credit were taken into account).

On 26 June 2012 the Internal Revenue Service (IRS) announced that a new procedure for dealing with low-risk U.S. tax filings for U.S. citizens living abroad will go into effect on 1 September 2012. Although more details will be forthcoming, the new procedure will be applicable for U.S. citizens who have not filed U.S. tax returns and who owe less than USD 1,500 in respect of each of the past three years' tax returns. To take advantage of this new process, these individuals will need to file tax returns for the past 3 years, a Report of Foreign Bank and Financial Accounts (FBAR) for the past 6 years, and a letter explaining why the returns and FBAR forms were not filed on a timely basis.

Of particular interest to U.S. citizens living in Canada who have Registered Retirement Savings Plan and Registered Retirement Income Fund accounts, the IRS will allow a late-filed election to defer the income tax on income on these plans, and late-filed forms 8891 (U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans).

The information submitted will be used by the IRS to assess the risk that the taxpayer owes more U.S. tax. The IRS has promised to release more details regarding the specific risk factors prior to the 1 September 2012 effective date. The IRS has stated that for those taxpayers presenting a low compliance risk, the submission review will be expedited and the IRS will not assess penalties or pursue follow-up actions. Submissions that present a higher compliance risk will be subject to a more thorough review and possibly a full examination, which may include more than three years, as well as the assessment of additional taxes, interest and penalties.

STAN ZINMAN
szinman@bdo.ca
+1 416 865 0200

UNITED STATES OF AMERICA

NEW TEMPORARY RULES FOR EXPANDED AFFILIATED GROUPS AND FINAL RULES ON SURROGATE FOREIGN CORPORATIONS

On 7 June 2012, the Treasury Department and the Internal Revenue Service (IRS) issued new temporary regulations under section 7874 (T.D. 9592) providing a bright-line test for determining whether an expanded affiliated group (EAG) has substantial business presence in a relevant foreign country. A new 25% test replaces the facts-and-circumstances test contained in the 2009 temporary regulations, thereby providing more certainty in application of section 7874 to corporate inversion transactions. In addition, final regulations (T.D. 9591) were issued on the determination of whether a foreign corporation will be treated as a surrogate foreign corporation under section 7874. These regulations generally made permanent the regulations issued in 2009, with some amendments. The changes will affect domestic corporations and partnerships, their owners and foreign entities that acquire substantially all of the properties of such domestic corporations or partnerships.

SECTION 7874: GENERAL PRINCIPLES

Section 7874 applies to a transaction completed after 4 March 2003, if under a plan or series of related transactions:

- A foreign corporation acquires (directly or indirectly) substantially all the properties of a domestic corporation (or partnership) (the "acquisition test");
- The shareholders (or partners) of the domestic corporation (or partnership) acquire at least 60% of the vote or value of the foreign corporation by reason of holding stock in the domestic corporation (or interest in the partnership) (the "ownership test"); and
- The foreign corporation, considered together with all companies connected to it by a chain of greater than 50% ownership (i.e., the EAG), does not conduct substantial business activities in its country of incorporation compared with its total worldwide business activities (the "substantial activities test").

If an inversion transaction meets all the above tests, the foreign acquiring corporation is treated as a surrogate foreign corporation with respect to the expatriated domestic corporation or partnership. The tax treatment of the surrogate foreign corporation varies, depending on the level of shareholder continuity. If the shareholders of the inverted United States corporation own, by vote or value, 80% or more of the surrogate foreign corporation following the inversion, the foreign corporation is treated as a domestic corporation for all purposes of the Code and for all United States treaty purposes. If the ownership by former shareholders of the inverted corporation is less than 80% but is at least 60%, the surrogate foreign corporation is treated as a foreign corporation. However, the expatriated entity is denied the use of its tax attributes (e.g., net operating losses or foreign tax credits) to offset the inversion gain and certain other income for the succeeding ten-year period.

T.D. 9592: SUBSTANTIAL ACTIVITIES TEST

The most significant change in the 2012 temporary regulations relates to the determination of whether an EAG has substantial business activities in the relevant foreign jurisdiction. The prior 2006 regulations provided for two alternative tests: a facts-and-circumstances test and a safe-harbour test (former Temp. Reg. § 1.7874-2T(d)). Under the prior safe-harbour test, the EAG's business activities in the relevant foreign country were treated as substantial if at least 10% of its employees, assets, and sales were located in or attributable to that foreign country. The 2009 regulations completely eliminated this safe-harbour test, but retained the facts-and-circumstances general rule. The elimination of the safe-harbour test was not welcomed by many taxpayers and practitioners due to the increased uncertainty it caused for many inversion transactions.

In response to these comments, the newly-issued 2012 temporary regulations implemented two major changes. First, the new regulations reinstated the old safe-harbour rule provided in the 2006 regulations, but with an increased percentage threshold (and certain other clarifications and modifications). Second, the 2012 regulations completely eliminated the facts-and-circumstances test contained in the prior 2009 regulations. Thus, under the new rules, an EAG will only be considered to have substantial business presence in a relevant foreign country if at least 25% of the group employees, assets, and income are located in (or derived from) that foreign country. The preamble states that a bright-line test would provide more certainty in applying section 7874 and improve the administration of this provision.

The 2012 temporary regulations provide more detailed guidance on the application of the 25% business activities test. Specifically, in determining the 25% threshold as it applies to employees, the rules include two criteria. The first criterion is based on the number of group employees physically based in the relevant foreign country compared to the total number of employees on the applicable date. The other criterion compares compensation for employees based in the foreign jurisdiction to the total compensation of all group employees during a one-year testing period ending on the applicable date. Both criteria need to be satisfied for the 25% employee-based test to be met. The 25% asset test is calculated based on the gross (i.e., not reduced by liabilities) fair market value (or the adjusted tax basis) of real and tangible personal property used or held for use by the EAG in the active conduct of the foreign trade or business divided by the total fair market value (or the adjusted tax basis) of all group assets, determined on the applicable date.

For this purpose, the group assets include property rented by the EAG members from non-members, with the value of the rented property deemed to be eight times the net annual rent paid or accrued with respect to the property. The 25% income test is calculated as the EAG's gross income derived in the relevant foreign country from transactions with unrelated customers divided by the total group income earned during the one-year testing period ending on the applicable date. For the purposes of the above tests, the applicable date is either the date on which the acquisition is completed or the last day of the month immediately preceding the month in which the acquisition is completed. Lastly, for the purposes of the testing, the partnership items would only be taken into account if one or more EAG members hold, in the aggregate, more than 50% of the partnership interest (by value).

The new rules are effective for inversion transactions completed on or after 7 June 2012 (with an exception for certain transactions that were either described in a filing with the Securities and Exchange Commission made on or before 7 June 2012, or subject to a written agreement that was binding on or before 7 June 2012). The text of the temporary regulations also serves as the text of proposed regulations that will be finalised at a later time, following the expiration of a comment period and the holding of a public hearing, if one is requested.

T.D. 9591: FINAL RULES ON SURROGATE FOREIGN CORPORATIONS

The 2009 surrogate foreign corporation regulations generally provide that an option or similar interest in a corporation or partnership is treated as stock of the corporation with a value equal to the holder's claim on the corporation's equity. The IRS and Treasury have generally retained this claim-on-equity approach in the final 2012 regulations. However, for the purposes of determining the voting power of stock under section 7874, the 2012 regulations provide that an option will be treated as exercised if a principal purpose of the issue or acquisition of the option is to avoid treating the foreign corporation as a surrogate foreign corporation. Further, the claim-on-equity approach does not apply if, at the time of the acquisition, the probability that the option will be exercised is remote (or if a principal purpose of the issue of the option is to avoid the foreign corporation from being treated as a surrogate foreign corporation). These final regulations apply to all domestic or foreign corporations and partnerships. The final regulations clarify that the rules addressing options also apply for purposes of determining the membership of an EAG, and that a claim-on-equity equals the value of the stock or partnership interest that may be acquired under the option, less the exercise price.

In addition to clarifying the treatment of options, the final regulations also clarify the treatment of downstream mergers. Specifically, a downstream merger of a domestic corporation or partnership into its foreign subsidiary is treated as an acquisition by the foreign subsidiary of the transferor's properties for purposes of section 7874(a)(2)(B)(i).

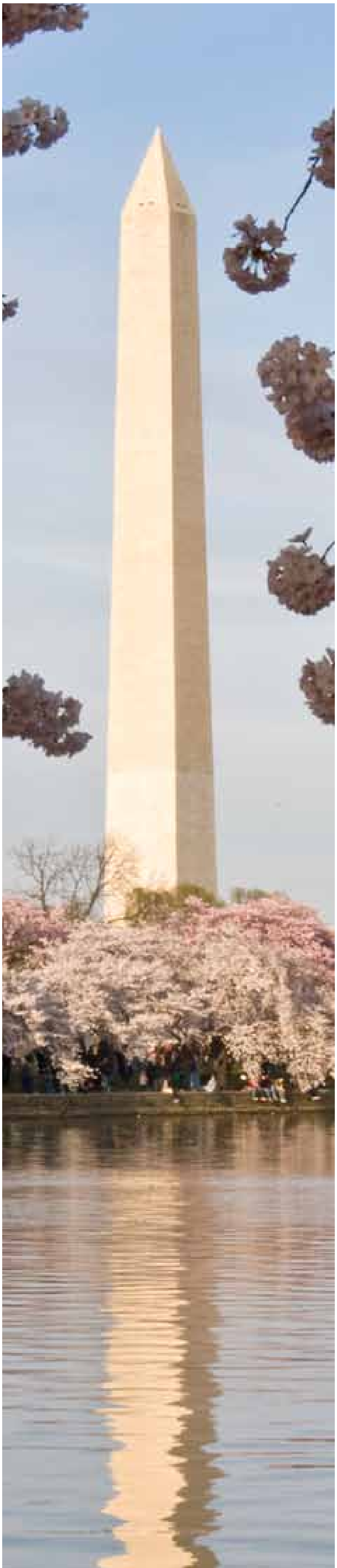
Despite some welcome clarifications provided in the 2012 regulations, many questions raised with respect to the application of section 7874 remain unanswered. Specifically, the final regulations do not address the application of Treas. Reg. § 1.7874-1 (i.e., the rule disregarding the affiliate-owned stock) in the case of multiple acquisitions of two or more domestic entities treated as a single domestic entity. Further, the regulations do not address the interaction of Treas. Reg. § 1.7874-1 with various other rules, such as public offering rule and Notice 2009-78 (determination of ownership fraction when stock is issued in exchange for certain types of property). In the preamble, the IRS and Treasury requested comments regarding the interaction of these rules.

The final section 7874 regulations apply to acquisitions completed on or after 7 June 2012.

ROBERT PEDERSEN
rpedersen@bdo.com
+1 212 885 8398

NATALLIA SHAPEL
nshapel@bdo.com
+1 212 885 8195

WILLIAM F. ROTH III
wfroth@bdo.com
+1 616 776 3761



SEYCHELLES

INTRODUCTION OF VAT POSTPONED

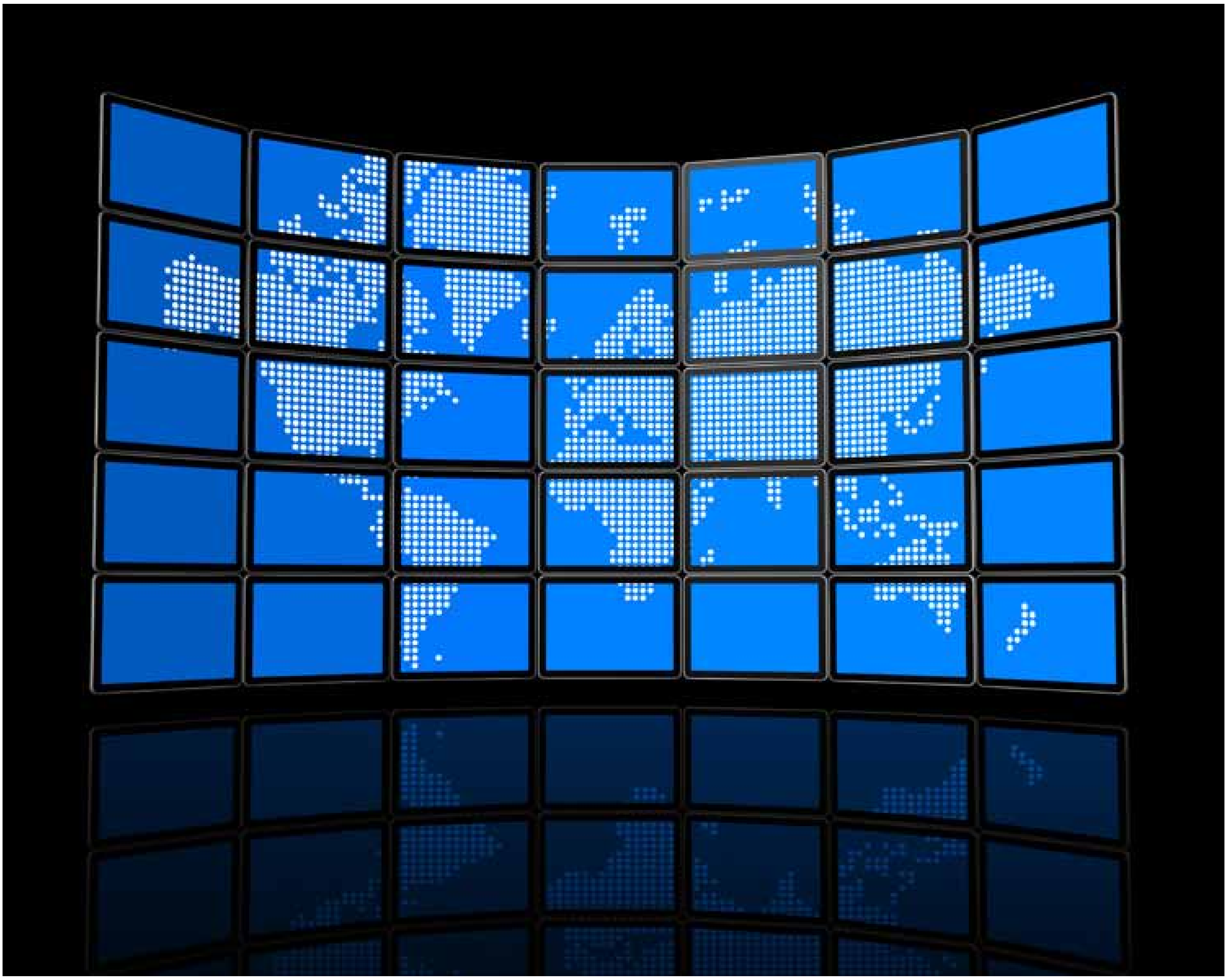
The Seychelles Revenue Commission has confirmed that the proposed introduction of Value Added Tax (VAT) on 1 July 2012 has been postponed. The Seychelles President stated that the reason for the postponement was to facilitate the good performance of the private sector and to stimulate the economy.

The introduction of VAT, at a proposed rate of 15%, and with a registration threshold of SCR 5 million, would have replaced the current Goods and Services Tax (GST), which has been in existence since 2001. The postponement is for the moment considered indefinite, with the President stating that the Government would continue consultations and analysis on the matter. In the meantime, GST will remain in force.

The postponement will particularly benefit businesses which carry out activities that are currently not subject to GST, but would be subject to VAT, including:

- Retailing and wholesaling;
- Renting or leasing offices, shops, factories, plant, vessels, and aircraft;
- Building and all other forms of contracting activities, such as painting, electrical wiring, and air-conditioning work;
- Garage services;
- Ship repairing;
- Sporting and other clubs which are not for the purpose of charitable or religious functions;
- Quarrying and other types of mining-related activities;
- Long-term leasing of land; and
- The sale or long-term leasing of immovable property constructed for the purposes of re-sale or Integrated Resorts schemes.

NAZRAH B RAMDIN
nazrah.ramdin@bdo.sc
+248 461 1005



CURRENCY COMPARISON TABLE

The table below shows comparative exchange rates against the euro and the US dollar for the currencies mentioned in this issue, as at 17 August 2012.

Currency unit	Value in euros (EUR)	Value in US dollars (USD)
Euro (EUR)	1.00000	1.23068
British Pound (GBP)	1.27545	1.56975
New Zealand Dollar (NZD)	0.65652	0.80804
Seychelles Rupee (SCR)	0.06291	0.07743
US Dollar (USD)	0.81249	1.00000

CONTACT

Contact Mireille Derouane in Brussels on **mderouane@bwsbrussels.com** or **+32 (0)2 778 0130** for more information.

www.bdointernational.com