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INTERNATIONAL TAX REFORM

Against the background of the debate on tax avoidance, morality, and the practices of multinational companies, the Organisation for Economic Co-operation and Development (OECD) has published its preliminary report on Addressing Base Erosion and Profit Shifting (BEPS). This proposes the development of a comprehensive action plan to be presented to the G20 group of nations in July 2013, which may lead to fundamental reform of the international tax system.

BASE EROSION AND PROFIT SHIFTING – AN OVERVIEW

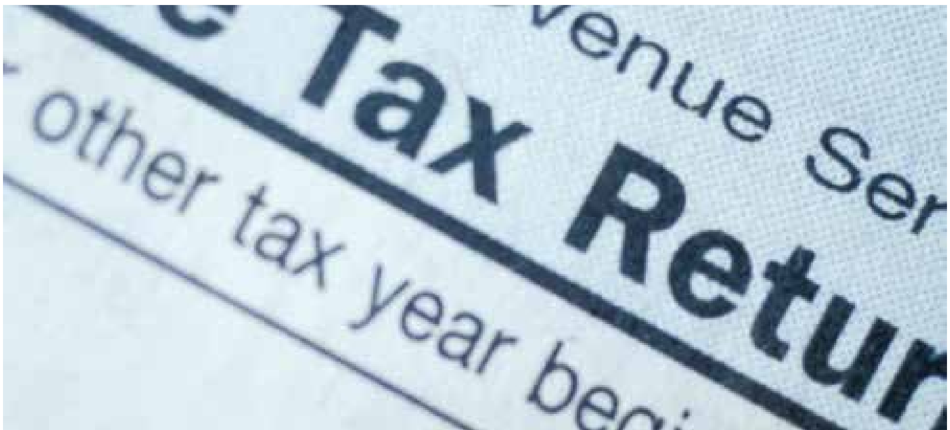
In the words of the OECD, "broadly speaking, BEPS focuses on moving profits to where they are taxed at lower rates and expenses to where they are relieved at higher rates. Specific strategies may also be put in place to make use of existing "tax attributes, such as tax credits, loss-carry forwards, etc".

The OECD sees an urgent need for reform arising from international tax principles not having kept pace with the changing business environment (more global businesses and new ways of operating cross-border), and the perception that the tax practices of some multinational companies have become more aggressive.

Having reviewed the available studies and data in the public domain, the OECD identifies six key pressure areas:

1. International mismatches in entity and instrument characterisation, including hybrid mismatch arrangements and arbitrage;
2. Application of treaty concepts to profits derived from the delivery of digital goods and services;
3. The tax treatment of related party debt financing, captive insurance and other intra-group financial transactions;
4. Transfer pricing, in particular the shifting of risks and intangibles, and the artificial splitting of asset ownership between group entities which would rarely take place between independents;
5. The effectiveness of anti-avoidance measures, in particular general anti abuse rules (GAARs), controlled foreign company (CFC) regimes, thin capitalisation rules and rules to prevent tax treaty abuse; and
6. The availability of harmful preferential regimes.

The OECD notes that these areas currently provide an unintended competitive advantage to some businesses which operate cross-border compared with businesses which operate domestically.



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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 would like more information on any of the items featured, or would like to discuss their implications for you or your business, please do not hesitate to contact me by telephone: **028 9043 9009** or by email: **peter.burnside@bdo.co.uk** or contact the person named under the items(s).

Kind Regards,

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NEXT STEPS – OECD OBJECTIVES

The OECD urges governments to work together, rather than taking unilateral actions which could increase uncertainty ("a battle to be the first to grab taxable income") and the likelihood of double taxation.

A global action plan will be developed by the OECD by June 2013 identifying the required actions and setting out the resources and deadlines for them to be achieved. Input will be sought from all stakeholders.

While this plan may propose some incremental actions, it will also "revisit the fundamentals of the existing standards" so, in theory at least, it could propose radical changes to existing international tax principles.

IMPLICATIONS

The OECD report has been explicitly welcomed by the G20 and should be seen in the context of the growing perception of governments that they lose substantial corporate tax revenues because of planning which shifts profits to low tax jurisdictions.

Whilst specific proposed changes will not be known until the summer, these are likely to include a greater emphasis on commercial substance. Meanwhile, tax authorities will continue to increase their scrutiny of current trading and transfer pricing arrangements.

WHAT DO COMPANIES NEED TO CONSIDER?

Multinational groups which may be affected by potential changes to the international tax environment should consider:

– Reviewing the group's international structure and trading model to assess its dependence on the pressure areas identified by the OECD for reform;

– Reviewing the substance requirements to support existing trading and transfer pricing arrangements; and

– Taking extra care if planning to implement business change, including procurement, supply chain arrangements and eCommerce

These issues are considered in more detail in the following article on value chain management.

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The pace and nature of change in the business world has increased dramatically over the last decade. Reductions in trade barriers across the globe and significant improvements in technology and how businesses connect with their customers have all contributed to this - even for relatively small family owned businesses that increasingly now operate internationally. And as the world has changed, in their efforts to remain competitive, businesses of all sizes have had to examine whether their business models remain fit-for-purpose for their target markets so as to produce and deliver their goods or services as efficiently and cost effectively as possible.

Changes in a business model will often have a major impact on key elements of that organisation's value chain – those critical activities and assets required to generate profits. There are a range of events which could alter where functions, assets or risks, and their associated business value drivers, sit within a business. Examples include:

– The development and launch of new products;

– Setting up in new markets;

– Introducing centralised services, including procurement;

– Outsourcing;

– Moving production to lower-cost countries;

– Changing how and where the business is managed; and

– Integrating new acquisitions into the organisation.

The point at which businesses restructure to achieve this is an ideal time to examine how they manage one of the largest expenses on their income statement – their corporate income tax expense. With proper tax planning, the commercial benefits achieved by proactively managing a business's value chain can be enhanced.

TAX EFFECTIVE VALUE CHAIN MANAGEMENT – HELPING BUSINESSES TO MANAGE THEIR GLOBAL TAX EXPENSE

WHAT ARE THE KEY TAX ISSUES IN BUSINESS RESTRUCTURINGS?

Any business considering making changes to their value chain will need to address a number of tax issues to effectively manage their tax cost and tax risk. These issues include:

- Dealing with potential tax (and the preservation of tax attributes (e.g. losses)) on the movement of assets or functions to different jurisdictions;
- Managing tax costs and risks associated with having a permanent establishment in a jurisdiction;
- Setting and defending transfer pricing policies for the organisation globally to ensure that they meet the arm's length standard;
- Identifying and focusing activities in lower tax jurisdictions and ensuring that appropriate substance exists in these jurisdictions to support the economic characterisation of those activities and the income/profit allocated to them;
- Identifying and addressing other tax risks including controlled foreign corporation issues, sales taxes and custom duties; and
- Embedding new policies and effecting change.

What is critical is that any tax planning done in conjunction with a business restructuring reflects the commercial realities of the organisation's business. It is only possible to effectively manage an organisation's tax cost if the new structure makes business and commercial sense and the activities are actually carried out in the jurisdictions where they are intended to be carried out.

WHAT ARE THE TAX RISKS ASSOCIATED WITH BUSINESS RESTRUCTURINGS?

Tax authorities have always been aware of tax planning accompanying value chain change. In practice, this has typically involved principal structures being implemented or intangible assets being transferred to low taxed group entities.

The increasing adoption of multinational business models and recent public debate about the transfer pricing arrangements of a number of high profile multinationals has elevated this focus, coupled with broader domestic pressures on tax authorities to minimise loss of tax from income streams moving abroad. As a result, tax authorities are paying far more attention to the taxes that companies who operate in their territories are paying, to ensure that these companies pay their 'fair share' of tax on profits earned – or, to put it another way, that 'taxation of economic activity should transparently reflect where that activity occurs' – with governments investing in additional transfer pricing specialists, and tax authorities around the world increasingly cooperating with each other in a much more proactive and transparent manner.

Such an 'activity' and 'substance' based approach follows the direction that OECD consultation on its transfer pricing guidance concerning business restructuring and the pricing of intangible assets (such as brands) has taken in recent years.

As such, there seems little question that any value chain restructuring will be scrutinised by tax authorities, and the seriousness and strength of a challenge by a tax authority should not be underestimated. Tax authorities are likely to look at all aspects resulting from the change process, the obvious questions being:

- What has really changed?
- Would a third party agree, for example, to sell to another party its 'crown jewels' intellectual property or its customer contracts or other key functions and attributes which are core to its ability to generate profit?
- What is the substance of new arrangements?
- Does the reality of arrangements going forward match the stated policy?

That is why it is extremely important that organisations that restructure are able to illustrate that they both do so in a manner that makes commercial sense and that their transfer pricing policies, together with other tax arrangements, matches the commercial fact pattern. Organisations that have a well thought-out plan where local levels of activity and substance can be defended, the tax results are consistent with the commercial facts, and robust documentation exists to support it, should be in a good position to defend themselves from tax authority scrutiny.

HOW BDO CAN HELP

BDO's global network of Tax Effective Value Chain Management specialists have experience in delivering coordinated global support to organisations embarking on significant business restructurings. Our approach is a flexible and scalable one which helps our clients to build on their commercial priorities and, in doing so, manage their group tax risk and create sustainable, tax-efficient models that complement commercial requirements. In other words, we provide advice which is tailored to the commercial realities of your organisation. We will:

- Support your organisation's finance function throughout your decision-making process around restructuring your value chain;
- Offer advice that respects commercial priorities and helps manage and mitigate the tax consequences of the business changes you are undertaking;
- Work with your finance team to build a sustainable, practical tax-efficient model for your organisation; and
- Support your organisation during and after the implementation of your restructuring

To learn more about how BDO can help your organisation, contact your BDO advisor.

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HONG KONG

2013/14 BUDGET HIGHLIGHTS

Financial Secretary, Mr John Tsang, delivered his sixth Budget on 27 February 2013 against the backdrop of the continued deteriorating external environment of the US fiscal cliff/European debt crisis and repeated internal calls from all directions for more long-term effective relief measures.

With an estimated budget surplus of HKD 64.9 billion for 2012/13, and a small deficit of HKD 4.9 billion forecast for 2013/14, there are few tax changes.

PROFITS TAX

The rates of tax for incorporated and unincorporated businesses, deductions and depreciation allowances are all unchanged for 2013/14.

The waiver of 75% of the tax liability continues to apply for 2012/13, but the cap has been reduced from HKD 12,000 to HKD 10,000.

Two new fiscal measures are proposed for the financial services industry, to attract more private equity funds and captive insurance companies in Hong Kong:

– The extension of the 100% profits tax exemption for offshore funds to include transactions in certain private companies; and

– The extension of the 50% profits tax exemption on offshore reinsurance income of reinsurance companies to offshore insurance income of captive insurance companies.

PERSONAL AND SALARIES TAXES

There are no changes to the standard and progressive tax rates, or most personal allowances. However, allowances for children have been increased for 2013/14, from HKD 126,000 to HKD 140,000 in the year of birth, and from HKD 63,000 to HKD 70,000 in other years.

The waiver of 75% of the tax liability continues to apply for 2012/13, but the cap has been reduced from HKD 12,000 to HKD 10,000.

For 2013/14 the maximum allowable contributions to recognised pension schemes have been increased from HKD 14,500 to HKD 15,000, and the maximum deduction for self-education expenses has been increased from HKD 60,000 to HKD 80,000.

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INDIA

2013/14 BUDGET SNAPSHOT

The 2013 Union Budget was tabled in Parliament by the Finance Minister on 28 February 2013. The Budget was presented against a background theme of "The worst is over", with the aim of returning to an 8% growth rate. The main tax measures are summarised below.

PERSONAL TAXATION

The rates of income tax are unchanged for 2013/14, but a 10% surcharge has been introduced for one year only on total income in excess INR 10 million of persons other than companies.

A rebate of INR 2,000 has been introduced for taxpayers with income between INR 200,000 and INR 500,000.

An additional interest deduction of INR 100,000 will be allowed on housing loans of up to INR 2.5 million taken out by first-time buyers on houses with a value of up to INR 4 million in the year ending 31 March 2014.

CORPORATE TAXATION

Corporate basic tax rates are unchanged for both domestic and foreign companies. However, surcharges are increased for one year only as follows:

– Domestic companies with total income in excess of IRD 100 million: surcharge increased from 5% to 10%; and

– Foreign companies with total income in excess of IRD 100 million: surcharge increased from 2% to 5%.

Manufacturing companies will be entitled to a total investment allowance of 15% for two years on investments of over INR 1,000 million in new plant and machinery during the year ended 31 March 2014.

The concessional 15% rate of tax on dividends from foreign subsidiaries has been extended for one more year.

The rate of tax deducted at source on payments of royalties/fees for technical services has been increased from 10% to 25%.

Where an unlisted company buys back its shares, an additional 20% income tax charge will be payable on the excess over the original subscription price, with effect from 1 June 2013. Where the company is liable to pay this additional tax, the amount received by the shareholders will be tax-exempt.

PROPERTY TRANSFERS

From 1 June 2013 a tax charge of 1% of the sales consideration for transfers of immovable property will be payable by deduction at source if the sales consideration exceeds INR 5 million.

INDIRECT TAXES

The rate of service tax remains unchanged.

However, the negative list for service tax purposes will be enlarged to cover vocational courses offered by institutions of the State Council of Vocational training and testing activities in relation to production of agricultural produce. All air-conditioned restaurants will have to charge service tax from 1 April 2013.

The rates of Securities Transaction Tax in respect of certain types of securities will be reduced from 1 June 2013.

The import duty concession in respect of specified parts of electric and hybrid vehicles has been extended up to 2015.

Customs duty has been increased in respect of high-end luxury cars, motor cycles exceeding 800 cc, set top boxes, raw silk and steam coal. Customs duty has been reduced in respect of certain goods, including specified agricultural goods, pre-forms of precious and semi-precious stones, bitumous coal, specified machinery used in the leather and footwear industry, and textile machinery and parts.

A new Commodities and Transaction Tax, at a rate of 0.01%, will be payable by sellers of commodity derivatives in respect of commodities other than agricultural commodities, from a date to be announced.

The draft Goods & Services Tax legislation is now at an advanced discussion stage, and the draft legislation will be placed before Parliament in a few months.

TAX AVOIDANCE

The modified General Anti Avoidance Rule will come into effect from 1 April 2016. The provisions will now apply where the main purpose of an arrangement is to obtain a tax benefit (and not, as previously proposed, where the main purpose, or one of the main purposes, of an arrangement is to obtain a tax benefit).

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NEW ZEALAND

PROPOSED THIN CAPITALISATION RULES CHANGES MAY AFFECT NON-RESIDENT INVESTORS

The Inland Revenue's Policy Advice Division has proposed tightening the thin capitalisation rules to ensure that New Zealand "collects its fair share of tax" from foreign investors.

The thin capitalisation rules reduce tax deductions for interest where the New Zealand operations of multinational enterprises are excessively debt-funded. The rules currently only apply when a single non-resident controls the investment, and the Policy Advice Division now proposes that they should be extended to groups of non-resident investors acting together. The aim is to prevent circumvention of the current rules by private equity investors working together in groups in a way that mimics control by a single controlling investor, and also to increase the effectiveness of the rules where debt funding for an entire global group comes from the ultimate shareholders rather than from third parties.

The Inland Revenue's main concern is the use of related-party debt when overall debt levels are high. It therefore proposes to exclude related-party debt from the debt-to-asset ratio of a multinational's worldwide group for the purposes of the thin capitalisation calculations. The Inland Revenue believes that this would ensure that high debt levels in New Zealand could only be justified where the world wide debt ratio genuinely reflects third-party borrowing by the worldwide group.

Several other technical changes are proposed, including ignoring increased asset values as a result of internal asset sales, excluding capitalised interest from assets when a tax deduction for the interest has been claimed in New Zealand, and bringing more trusts within the scope of the thin capitalisation rules.

The Inland Revenue is now consulting on the proposals, and proposes that any changes should take effect from the income year beginning after the enactment of new legislation. The income year 2014 would therefore be the earliest year for which any changes would apply. However, it is unclear whether the changes would affect existing structures or only arrangements entered into after the changes take effect.

The Inland Revenue believes that the proposed changes will not have a significant effect on overall levels of foreign investment, but existing or potential new investors in New Zealand will need to review current and proposed arrangements in light of the proposals, and monitor the outcome of the consultation.

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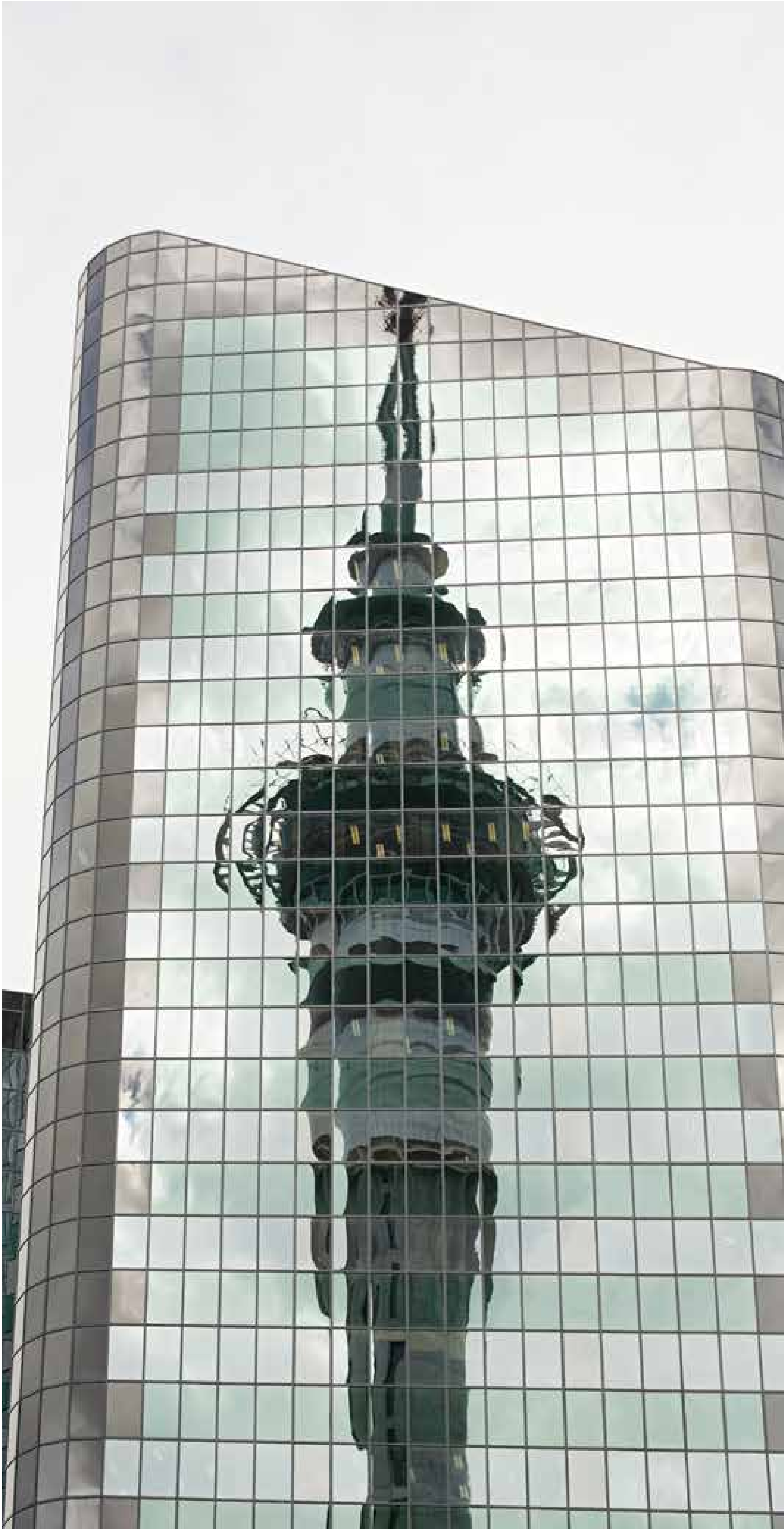


SINGAPORE

SINGAPORE BUDGET SUMMARY

The Minister of Finance presented the 2013 Budget on 25 February 2013. The Budget aims to promote sustained productivity through innovation rather than reliance on manpower growth, providing incentives and support to encourage changes for efficiency and productivity to help businesses upgrade, create better jobs and raise wages for Singaporeans. The main tax measures are summarised below.

CORPORATE TAX

- A corporate income tax rebate of 30% will be granted for three years from Year of Assessment (YA) 2013 to 2015, capped at SGD 30,000 per YA. The rebate will be assessed automatically by the Inland Revenue Authority of Singapore (IRAS), and will be given to all companies, including registered business trusts, but not partnerships. The rebate will not apply to the amount of income derived by a non-resident company that is subject to final withholding tax.

- The Productivity and Innovation Credit (PIC) scheme which allows enhanced allowances and/or deductions of up to 400%, subject to an expenditure cap of SGD 400,000 per YA for each activity will be further enhanced to include intellectual property (IP) in-licensing as a qualifying activity. As a result, the current PIC qualifying activity of "Acquisition of Intellectual Property" will be renamed to "Acquisition and in-Licensing of Intellectual Property". This enhancement is aimed at helping businesses, especially SMEs that license IP rights rather than acquire the IP for innovation or productivity improvements. IP acquisition and in-licensing costs will be eligible for enhanced allowances/deductions under the PIC scheme, up to a combined cap of SGD 400,000 per YA. Similarly, IP acquisition and in-licensing costs will qualify for a cash payout under the PIC, subject to conditions. This change will take effect for IP in-licensing costs incurred from YA 2013 to YA 2015.

- The Government will make it easier and allow more equipment to qualify for PIC benefits with effect from YA 2013, through the following changes:

  (i) For equipment that is not on the prescribed list, IRAS will assess and grant approval for PIC benefits based on the following liberalised conditions:

    a. The equipment wholly or partly automates or mechanises core or non-core business work processes;

    b. The equipment enhances business productivity (for example, in terms of reduced man hours, more output or improved work processes); and

    c. Equipment that is a basic tool will be allowed, so long as it increases productivity compared to the existing equipment used in the business, or it has not previously been used in the business.

  (ii) The term "automation equipment" is also changed to "IT and automation equipment", as PIC already supports IT-related software besides automation equipment.

  (iii) The prescribed equipment list will be updated regularly to take into account feedback from businesses

- Businesses that spend a minimum of SGD 5,000 in qualifying PIC investments in a YA will receive a matching cash bonus of up to SGD 15,000, from YA 2013 to YA 2015. The cash bonus is in addition to the existing PIC benefits.

- The Start Up Tax Exemption scheme, which provides tax exemptions in the first three years for new companies, will no longer be available to property development or investment holding companies. However, such companies will still enjoy the partial tax exemption that is generally available to all companies.

- The maximum tenure of the Maritime Sector Initiative – Approved International Shipping Enterprise Award, which confers tax exemption on qualifying income derived from international shipping operations, will be extended from 30 to 40 years.

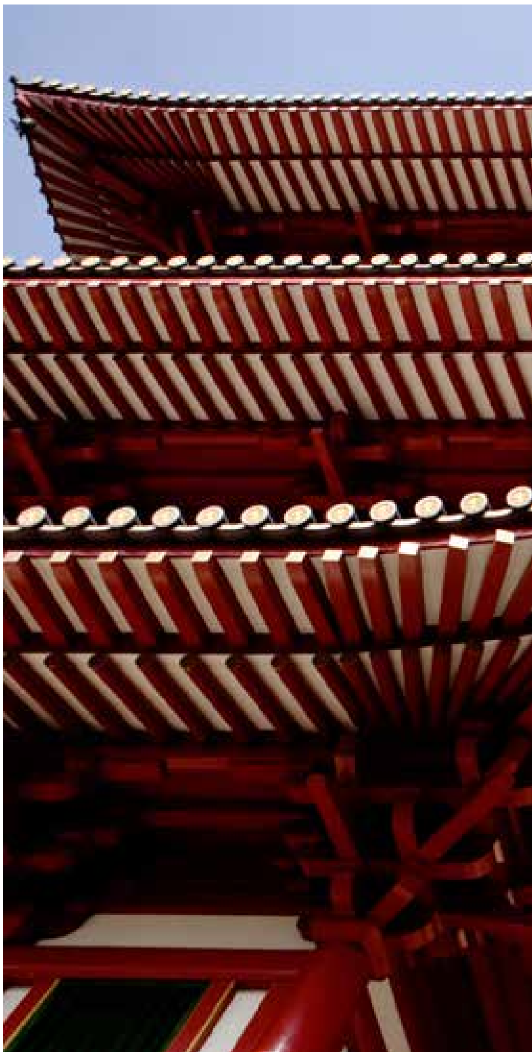
- The Financial Sector Incentive Scheme, under which certain financial services companies enjoy concessionary tax rates, which was due to expire in 2013, has been extended to 2018. Some improvements will be introduced from 1 January 2014.

- Tax incentives for offshore insurance broking businesses are to be extended and enhanced.

PERSONAL TAX

- For YA 2013 only, a personal income tax rebate of up to SGD 1,500 will be granted to Singapore resident individuals. The rebate will be 30% for individuals aged below 60, and 50% for individuals aged 60 and above.

- Tax on the benefit of housing accommodation provided to employees will be increased from YA 2015. The tax charge will be based on the annual value of the premises, less rent paid by employee, and the taxable value of furniture and fittings will be based on a percentage of the annual value of the housing accommodation. The taxable value of hotel accommodation will be the actual cost of the hotel stay benefit provided to the employee. The IRAS will provide further details by October 2013.



PROPERTY TAX

– Property tax rates for high-end residential properties will be increased, the largest increases being for properties held for investment purposes (i.e. non owner-occupied). The new tax rates and bands will be phased in over two years, as follows:

Non owner-occupied

Annual value	Tax rate %		
	Before 1 January 2014	From 1 January 2014	From 1 January 2015
First SGD 30,000	10	10	10
Next SGD 15,000	10	11	12
Next SGD 15,000	10	13	14
Next SGD 15,000	10	15	16
Next SGD 15,000	10	17	18
Excess over SGD 90,000	10	19	20

– The property tax refund concession for vacant residential and non- residential properties will be permanently removed from 1 January 2014. However, in certain situations owners will be able to apply to be taxed at owner-occupier residential property tax rates.

Owner-occupied

Annual value	Tax rate %	
	From 1 January 2014	From 1 January 2015
First SGD 8,000	0	0
Next SGD 47,000	4	4
Next SGD 5,000	5	6
Next SGD 10,000	6	6
Next SGD 15,000	7	8
Next SGD 15,000	9	10
Next SGD 15,000	11	12
Next SGD 15,000	13	14
Excess over SGD 130,000	15	16

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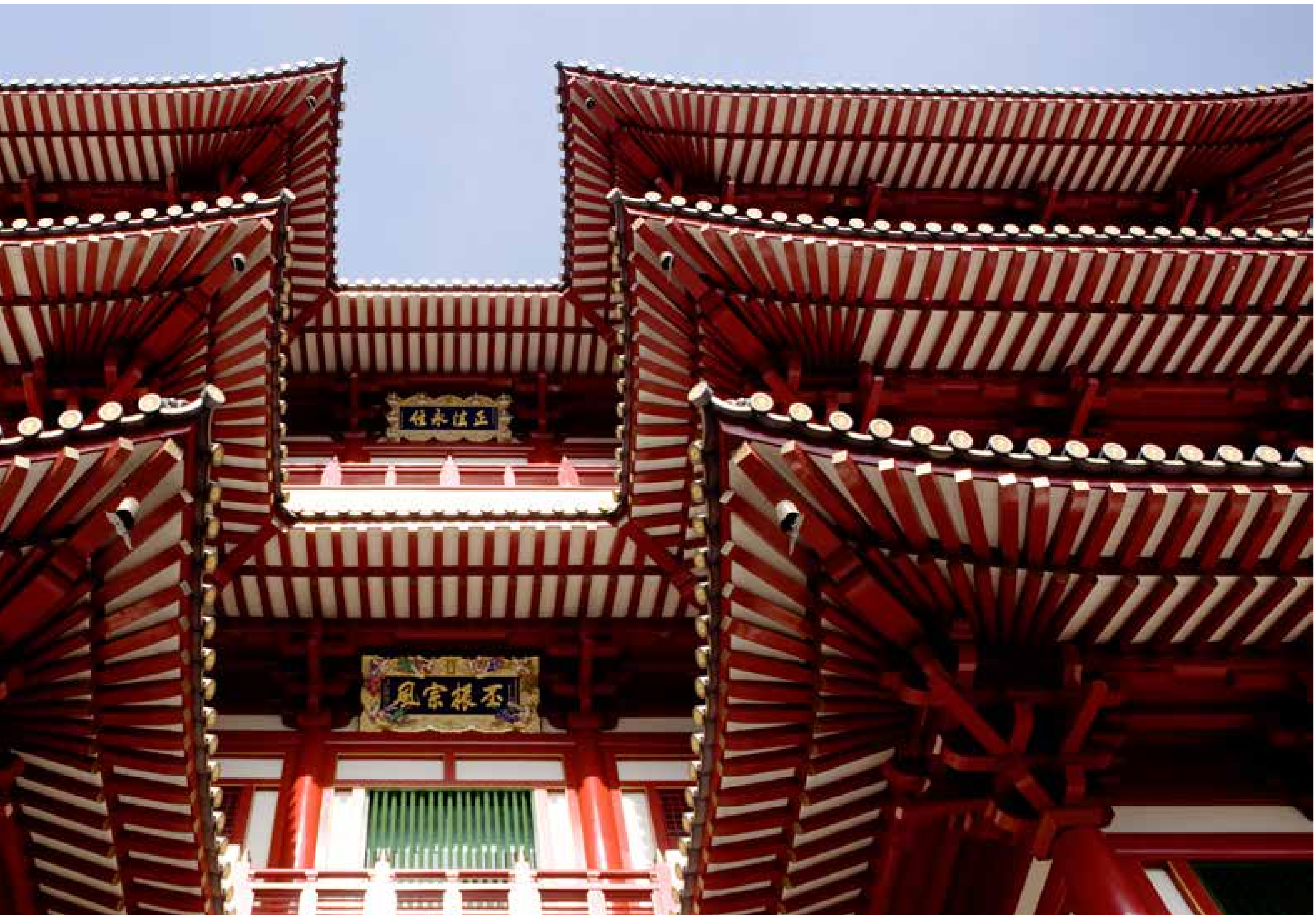

FRANCE

FRENCH FINANCE LAW FOR 2013 AND CORRECTIVE FINANCE LAW FOR 2012

France has implemented a number of changes to its tax law in the third corrective finance law for 2012 dated 29 December 2012 (*loi de finances rectificative pour 2012*) and the finance law for 2013 dated 30 December 2012 (*loi de finances pour 2013*), (together, the "Finance Laws").

These changes particularly impact the tax situation of high net worth individuals and larger companies, while preserving and deepening the advantageous rules applicable to small and medium sized companies. Given the important tax changes that have been introduced lately, the French government recently clarified that no tax modification, or only very minor modifications, should occur in the forthcoming years.

CHANGES TO PERSONAL TAXATION

The Finance Laws increase the highest income tax rate from 41% to 45% for taxable income earned in 2012 above EUR 150,000 (for a single person).

In addition, it should be remembered that an income surcharge is applicable on income earned as from 2011, of:

- 3% on income between EUR 250,001 and EUR 500,000 for a single taxpayer, and between EUR 500,001 and EUR 1,000,000 for a married taxpayer; and
- 4% on income exceeding EUR 500,000 for a single taxpayer, and EUR 1,000,000 for a married taxpayer.

However, the "exceptional solidarity contribution on very high income" on income from professional activities (wages and business income) exceeding EUR 1 million per taxpayer has been cancelled, although it may be re-introduced by the forthcoming corrective Finance Law for 2013.

Modification of the net wealth tax

For assets owned as of 2013, a taxpayer is subject to wealth tax when the net value of his/her assets exceeds EUR 1,300,000. The applicable tax bands are as follows:

Tax Band (EUR)	Tax rate %
Up to 800,000	0
800,000 - 1,300,000	0.5
1,300,000 - 2,570,000	0.7
2,570,000 - 5,000,000	1
5,000,000 - 10,000,000	1.25
Over 10,000,000	1.5

However, this tax is capped at 75% of the taxpayer's 2012 annual income.

Capping of reliefs

The tax credit or reduction that a taxpayer can obtain for various tax investments/costs is limited to EUR 10,000 for income earned as from 2012. For investments in SOFICA and in overseas French departments, the limit is EUR 18,000.

Changes to the taxation of dividends, capital gains realised on movable assets, interests, and vesting gains

- **Capital gains**: Currently, capital gains on movable assets (including shares) are taxed at a fixed rate (19% for 2011 and 24% for 2012). As from January 2013, these gains will be subject to the progressive income tax rates. To encourage long term ownership, an allowance would be applicable for income tax only depending on the number of years of ownership (maximum exemption of 40% after 6 years).

  In addition, the current flat tax rate of 19% (before social taxes) remains applicable (subject to election) to the capital gain derived from the sale of shares held in an operating company controlled by the vendor and their relatives, subject to the following conditions :

  - A requirement of a minimum 10% holding;
  - The vendor has been exercising eligible executive functions (or has been employed) in that company over the preceding five years; and
  - The vendor retains a minimum 2% holding.
- **Vesting gains**: Currently, vesting gains on awards (stock options, RSU, etc.) could benefit from reduced tax rates. For options granted after 28 September 2012, such gains will be subject to the progressive income tax rates.
- **Dividends and interest**: The fixed tax rate option which was previously available has been removed, so from 1 January 2013 dividends and interest will be automatically subject to the progressive income tax rates.

Consequently, these types of income (i.e. capital gains, vesting gains, dividends and interest) will be taxed at the marginal rates up to 45% (plus income surcharge and exceptional solidarity contribution, if any) in addition to social surcharges at 15.5%.

Share for share transactions by individuals

For transactions carried out on or after 14 November 2012, the former automatic postponement of taxation (*sursis d'imposition*) on inherent capital gains arising on share for share transactions has been replaced with a specific deferral of taxation (*report d'imposition*) when the recipient of the shares contributed is controlled by the contributor. The deferral regime is valid until:

- The sale, buy-back, reimbursement or cancellation of the shares received in consideration of the contribution;
- The sale, buy-back, reimbursement or cancellation of the shares contributed, if realised within 3 years following the contribution, unless at least 50% of the proceeds of this operation are reinvested in a qualifying investment in the 2 following years (subject to conditions and to a commitment); or
- The transfer of the contributor's tax residence outside France.

Change to the real estate capital gains tax regime

The tax treatment of capital gains realised on the sale of immovable properties by individuals or transparent real-estate companies has been tightened, even for sales which benefit from a tax exemption under the immovable property capital gains regime (i.e. sale of the main residence, etc.). Capital gains realised on the sale of these immovable properties will be subject to a newly created specific tax:

- The tax will apply to sales carried out from 1 January 2013 (except where a sale commitment was signed before 7 December 2012 (subject to conditions);
- The rate is determined by reference to progressive tax bands, the highest rate being 6% for net capital gains exceeding EUR 260,000.

CHANGES TO CORPORATION TAX

Introduction of a competitiveness and employment tax credit

A new competitiveness and employment tax credit (*crédit d'impôt compétitivité emploi*) (CICE) is introduced, and will be calculated on the basis of the aggregate gross wages paid to employees, excluding wages which exceed two and a half times the minimum wage in France (i.e. EUR 3,575 per month in 2013). This measure applies to wages paid from 1 January 2013. The CICE rate will be 4% of the eligible wages in 2013 and 6% as from 2014.

The CICE will be available for offset against the corporate income tax due. Any excess which cannot be offset can be immediately refunded to small and medium enterprises. For other companies, the CICE is carried forward to the three following fiscal years, and any portion still remaining will then be refundable.

General limitation of the tax deductibility of interest payments

The possibility for companies to deduct their net financial expenses paid to both related and unrelated parties, will be limited to 85% in 2013, and further reduced to 75% as from 2014. However, this measure will only apply to companies whose net financial expenses exceed EUR 3 million per year, and it is applicable for fiscal years ended as from 31 December 2012.

The net expenses are equal to the difference between (i) interest expenses (after application of thin capitalisation rules and other anti-abuse measures) and (ii) interest income. Rents relating to operating leases on assets (with related parties only) and financial leases are included within financial expenses.

Within tax consolidated groups, the limitation will apply at the tax-consolidated group's level, resulting in (i) application of the limitation only to interest expenses paid to or received from non-tax-consolidated entities, (ii) the EUR 3 million threshold will apply globally at group level, and (iii) any potential recapture of excessive interest payments could be offset against losses carried forward of the tax consolidated group.

As a matter of fact, the deduction of interest payments in France would need to be scrutinised through the following tests: (i) arm's length test of the interest rate (i.e. 3.39 % for calendar year 2012); (ii) thin capitalisation rules, (iii) control over the acquired shareholdings in the case of LBOs; and (iv) general limitation of the tax deductibility of interest payments, as described above.

Capital gains realised on the disposal of shares

For fiscal years ended as from 31 December 2012, capital gains arising on the disposal of qualifying shareholdings by entities subject to corporate income tax in France are tax exempt, subject to the recapture of a lump sum of 10% of the net capital gains. The Finance Laws increase the lump sum to 12%, which would now be computed on the basis of the gross capital gains realised on the disposal of qualifying shareholding, instead of the net capital gains.

Capital gains realised by non-residents on the disposal of substantial shareholdings in French companies

Before the enactment of the Finance Laws, capital gains realised by foreign taxpayers on the disposal of substantial shareholdings were subject to a withholding tax of 19% in France. 'Substantial shareholdings' are a minimum of 25% of the share capital (i.e. 25% of the voting rights and/or of the rights to dividend payments) of the French company.

For disposals of shareholdings from 1 January 2013, the Finance Laws increase the levy to 45% for non-resident taxpayers located in a foreign jurisdiction and 75% for non-resident taxpayers located in non-cooperative states or territories. However, in practice, this levy will be neutralised/mitigated under the application of (i) double tax treaties which do not include any substantial shareholding provision and/or (ii) to the extent the non-resident taxpayer is located in the European Union. A cash impact and a minor tax burden should nevertheless be anticipated in certain circumstances.

Rules governing the carry-forward of losses

The carry-forward of losses is now limited to 50% of the current year profit in a given offsetting year, on the portion of profit in excess of EUR 1 million. However, the taxpayer is allowed to carry forward to subsequent years (without time limitation) the losses it has not been allowed to set off against profits in a particular year. This measure is applicable for fiscal years ended as from 31 December 2012.

Extension of the scope of the French research and development tax credit (RTC) for small and medium enterprises

The expenses eligible for the RTC now include expenses in relation to innovation and conception of prototypes.

The increased rates of 40% and 35% which applied for the two first years of claiming a RTC are removed, so that only a unique rate of 30% applies for the computation of the RTC. These measures are applicable on eligible expenses incurred as from 1 January 2013.

Transfer of headquarters or permanent establishment to an EU member state

An option to defer the taxation of unrealised capital gains on transfers of a company or one of its permanent establishments from France to another EU Member State or to Norway or Iceland has been introduced for transfers from 14 November 2012. Payment can be made over five years (i.e. corporation tax could be paid through five annual instalments of 20%). This measure aims to render French tax law compliant with the CJEU decision of 29 November 2011 in the National Grid Indus BV case.

CHANGES TO VALUE ADDED TAX

Tax representative

The appointment of a French tax representative will no longer be mandatory in order to introduce a 13th Directive claim or to file French VAT returns for companies established in a third country, having signed with France a tax treaty of mutual assistance regarding the exchange of information and recovery of VAT. Comments from the French tax administration have not yet been released, but the following countries could particularly be affected: USA, Australia and Switzerland.

France has implemented Directive 2010/45/UE regarding VAT

- **Territoriality of invoice rules**: The French invoice rules are applicable to the following operations:
  - o Operations located in France, except in the case of a reverse charge in France by the French client of an operation performed by a foreign supplier established within the EU (unless excepted);
  - o Operations performed by a French company subject to the reverse charge mechanism in another EU Member State (unless excepted);
  - o Operations performed by a French company located in a third country.
- **Electronic invoicing**: As from 1 January 2013, companies can use any technical means to transmit electronic invoices provided that the authenticity of their origin, their integrity and their legibility can be proved by reliable controls so that the link between the invoices transmitted/received and the supply of goods or services can be made.

  We are awaiting comments from the French tax administration regarding these new rules, but we understand that France disagrees on electronic invoices sent by email in Acrobat Reader or Word format.
- **Other important changes**: Invoices relating to exempted intracommunity deliveries and assimilated operations, deliveries of new means of transport and services in the scope of article 44 of the VAT Council Directive (general rule of the B to B relationships) must be issued within the 15th days of the month following the taxable event.

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ISRAEL

TAX AUTHORITY ISSUES CLARIFICATION ON RESIDENCY

The Israeli tax authority (ITA) issued Circular 2/2013 (The Circular) on 13 January 2013, in order to clarify and improve procedures regarding tax residency status approvals for "New Immigrants" and "Veteran Returning Residents".

Following amendment 168 to the Israeli Tax Ordinance (ITO), substantial tax benefits were granted to individuals who were considered as "New Immigrants" or "Veteran Returning Residents". As a result of these amendments, many applications were submitted to the ITA by individuals seeking approval of their particular status. The uncertainty and lack of clarity over how to obtain approval of such applications was addressed in the Circular.

The Circular establishes two routes (the "Green Route" and the "Individual Route") to receive status of "New Immigrants" and "Veteran Returning Residents", which will be determined according to the particular individual's ties to Israel. It should be noted that applications for such approval from the ITA can be made both by individuals who have not emigrated to Israel yet but are planning to do so, and also by individuals who are residing in Israel.

The Green Route – this route is for those individuals who have minimal ties to Israel. These individuals will receive their status approval under an accelerated process. Should the tax assessing officer not approve the requested residency status under this route, the individual will still be able to seek approval via the Individual Route. Under the Green Route, the individual must meet all the conditions of either of the two alternatives detailed in the relevant form related to the days spent in Israel in a period of 10 years prior to his immigration, social security rights, medical care and other conditions.

The individual applying for residency status approval under the Green Route must, inter alia, declare in the relevant form the day on which he arrived in Israel, that he has met all the conditions required (whether under either of the alternatives) and that all the information in the form is correct. In addition, the individual must attach all relevant documents.

The Individual Route – this route is for those individuals who have more substantial ties to Israel. These individuals will receive a residency status approval after a thorough examination by a tax assessing officer.

Following this Circular, it would appear that the stringent conditions of the Green Route deny residency status as "New Immigrants" or "Veteran Returning Residents" for those individuals who preserved their social security rights in Israel, even if they did not maintain a permanent home in Israel and did not reside in Israel for even a single day prior to their emigration to Israel. New immigrants who visited Israel in the past for long periods will also be denied residency status through the Green Route, but they can seek their residency status approval through the Individual Route.

It should be noted that these residency status approvals are not considered as a Certificate of Residency for the purpose of benefiting from Israel's double taxation treaties, which are usually given only after the individual proves a change of his "centre of life" to Israel, and fulfils other criteria.

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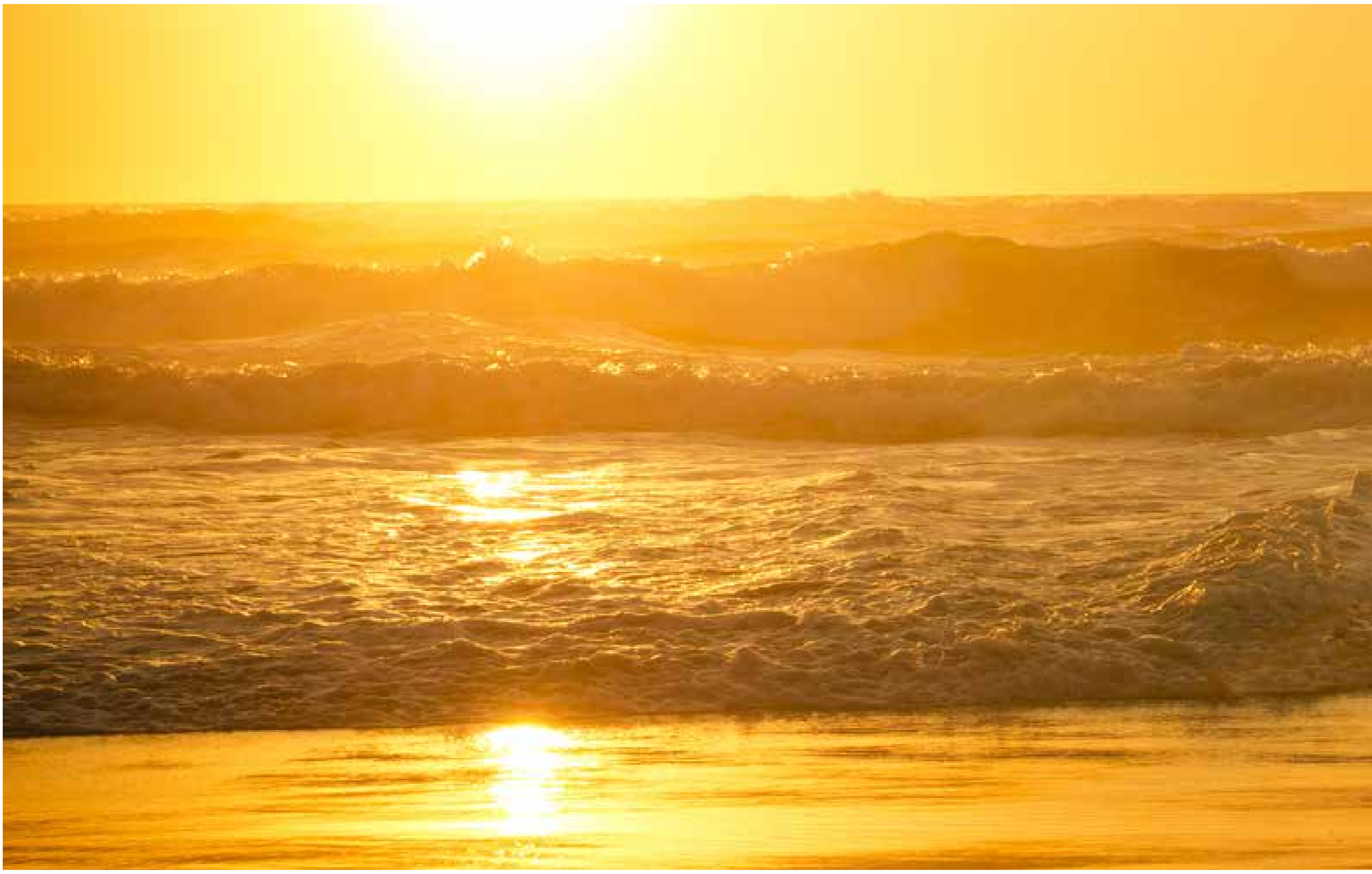
PORTUGAL

RESIDENCE PERMITS FOR INVESTMENT IN PORTUGAL - GOLDEN RESIDENCE PERMIT



The The Ministry of Foreign Affairs and Ministry of the Interior have recently enacted some measures which simplify and provide more flexibility to the granting and renewal of Residence Permits, in particular, removing the requirement of a residence visa for investment activity in Portugal (ARI) - the so-called "golden Visas" regime.

Through the implementation of this scheme, which reinforces the national policy of attracting foreign investment in Portugal, starting in 2009 with the introduction into the Portuguese tax system of non-habitual residents, Portugal aims to be in the spotlight as a prime option jurisdiction for high net worth individuals (both European and non-European), aiming to change their residency. Portugal offers individuals the opportunity to develop their activities or simply enjoy their retirement in the sun in a country with advantageous tax regimes and the possibility of a low cost high standard of living.

In particular, the Golden Residence Permit for Investment in Portugal (GRP) allows nationals of third countries to apply for a residence permit to conduct an investment activity in Portugal for a minimum of five years. After this period they may further apply for a permanent authorisation, or even be granted Portuguese nationality.

The main changes to this scheme are briefly listed below:

INVESTMENT ACTIVITY REQUIREMENTS

Nationals of third countries will have an "Investment Activity" in Portugal if, personally or through a company, they fulfil at least one of the following conditions for the minimum period of five years:

– Transfer capital of at least EUR 1 million;

– Create at least 10 job positions; or

– Acquire property with a value of at least EUR 500,000.

The recent changes aimed to provide more flexibility with the minimum requirements of the scheme by:

– Allowing investment in stocks or shares of unlisted companies;

– Reducing from 30 to 10 the minimum number of jobs to be created; and

– Allowing the joint purchase of properties (whilst still requiring a minimum investment of EUR 500,000 for each joint owner); the investment may be made through a promissory contract, provided that the advance payment is at least EUR 500,000;

– Allowing investment through the acquisition of property where there is a charge of more than EUR 500,000 on the property; and

– Allowing the property to be used for leasing, commercial exploration, agriculture or tourism.

RESIDENCE TIME

The granting of ARI assumes a minimum period of residence in Portuguese territory, which the recent changes have reduced from 30 to 7 days (consecutive or intermittent) in the first year, and from 60 to 14 days (consecutive or intermittent), in subsequent periods of two years.

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UNITED KINGDOM

2013 BUDGET AND FINANCE BILL

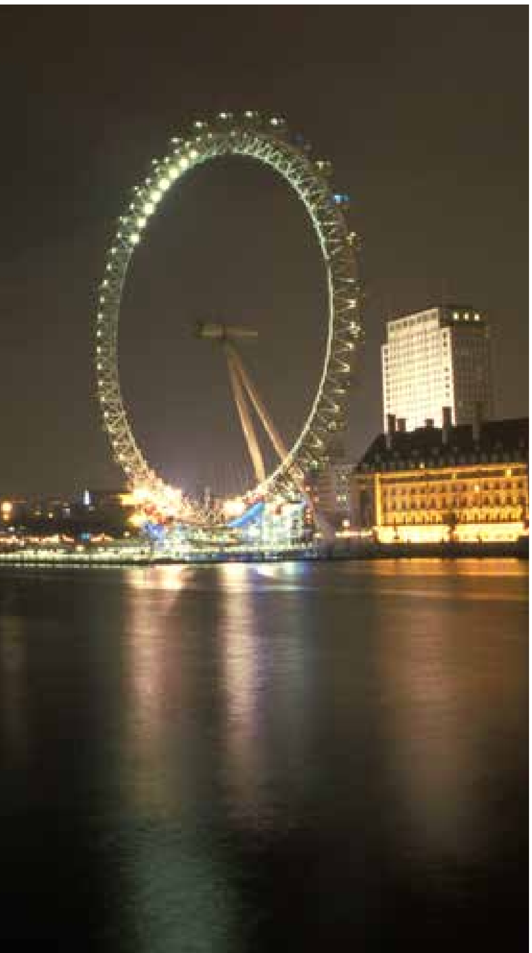
The Chancellor of the Exchequer delivered the 2013 Budget on 20 March 2013, and the Finance Bill 2013 was published on 28 March 2013. We summarise below some of the proposals which are of international interest.

MAIN CORPORATION TAX RATE TO BE FURTHER REDUCED

The main rate of corporation tax, which applies to companies with a taxable profit of GBP 1.5 million or over, already reduced to 23% from 1 April 2013 and 21% from 1 April 2014, will be further reduced to 20% from 1 April 2015. This rate, one of the lowest in the G20 group of nations, will increase the attractiveness of the UK as a location for larger businesses. In addition, it will mean that companies with profits between GBP 300,000 and 1.5 million will no longer need to carry out complicated 'marginal relief' calculations.

DEFERRAL OF PAYMENT OF CORPORATION TAX EXIT CHARGE

The Finance Bill contains a proposal to allow a company that transfers its place of effective management to another European Union or European Economic Area member state to elect to defer the payment of exit charges which arise under the existing legislation. This follows a European Court of Justice ruling that member states must offer a choice between immediate payment or deferral, subject to certain conditions.



Under the new measure, a company can elect for deferral under one or both of two options, as long as it clearly states which method is adopted for which assets when applying for deferral.

– **Option one**: a calculation is made of the amount of tax due on all assets at the time of migration, with payment of the tax due in six equal annual instalments. The first payment is due within nine months and one day of the end of the migration accounting period.

– **Option two**: a calculation of the tax due is made at the time of exit, which is allocated on an asset by asset basis, taking into account the useful economic life of individual assets. Companies will then be obliged to provide HMRC with an annual statement identifying the realisations of assets in that period, at which point the tax would become payable on any assets that have been disposed of. For intangible assets, derivative contracts and loan relationship profits, the useful economic life of each asset must be determined at the point of migration. The tax is then payable in equal annual instalments over the useful economic life of the asset. The payment may be deferred for up to a maximum of ten years or until the asset is disposed of, if sooner.

Under both options, the amounts deferred will be subject to interest. The measure will apply retrospectively to allow companies to opt for a deferred payment arrangement in respect of exit charges arising on or after 11 December 2012.

HIGH VALUE RESIDENTIAL PROPERTIES HELD BY 'NON-NATURAL PERSONS'

The Finance Bill also contains the previously-announced changes to the taxation of high value (over GBP 2 million) residential property which will apply to certain non-natural persons (broadly companies, partnerships with one or more corporate members and collective investment schemes). These relate to three measures:

– **Annual Tax on Enveloped Dwellings (ATED)**: ATED, effective from 1 April 2013 is an annual tax on the market value of high value residential properties held by non-natural persons. The charge for 2013/14 will be as follows:

Residential property value (GBP)	Charge (GBP)
Over 2 million to 5 million	15,000
Over 5 million to 10 million	35,000
Over 10 million to 20 million	70,000
Over 20 million	140,000

Various reliefs will apply, including where the property is:

o Held as part of a genuine property development, investment or trading businesses;

o Open to the public for at least 28 days a year on a commercial basis;

o Held for employee accommodation;

o Owned by a charity and held for charitable purposes;

o A diplomatic property or working farmhouse.

– **Capital Gains Tax (CGT)**: CGT, at a rate of 28%, will apply to disposals for over GBP 2 million of residential property by non-natural persons on or after 6 April 2013. The charge will only apply to the extent that the vendor was subject to the ATED. It will only apply to gains accruing from 6 April 2013 to the date of disposal of the property, and will be tapered for certain sales which just exceed the GBP 2 million threshold to ensure that the tax payable does not distort the sales price.

– **Stamp Duty Land Tax (SDLT) at 15%**: The 15% rate of SDLT on acquisitions of residential dwellings worth more than GBP 2 million by non-natural persons, which came into effect on 20 March 2012, is to be relaxed as follows from Royal Assent to the Finance Bill:

o The two year trading history requirement for relief to apply where a developer acquires the property will be dropped; and

o Further reliefs will be introduced in line with those set out above which apply to the ATED. However, where relief is claimed, this may be clawed back within the three years following acquisition of the property if the conditions for relief are no longer satisfied.

STATUTORY RESIDENCE TEST

The statutory residence test (SRT) to determine whether an individual is resident in the UK for income tax and capital gains tax purposes is finally about to be enacted, and will be effective from 6 April 2013. The basic form of the test remains largely as announced in 2011 (as reported in WWTN August 2011), but the details have undergone several changes during consultation, and further changes appeared in the draft legislation published on 28 March 2013.

In summary, an individual will be UK-resident for a particular tax year if he does not satisfy the 'automatic overseas test' and meets the 'automatic residence test' or 'sufficient ties test' for that year:

– **Automatic residence test**: an individual will be UK-resident for a year in which he meets at least one of four 'automatic UK tests' and none of five 'automatic overseas tests':

o **Automatic UK tests**:

1. The individual spends at least 183 days in the UK in the tax year.
2. The individual has a home in the UK during all or part of that year, at which he is present for part or all of the time on at least 30 days in that year. There must be at least one period of 91 consecutive days (of which at least 30 days fall into that tax year) during which the individual owns that home and either owns no overseas home or spends less than 30 days in that tax year in such a home.
3. The individual 'works sufficient hours' in the UK in the tax year (detailed rules apply).
4. The individual dies during the tax year, having a UK home and having met the automatic residence test in each of the three previous tax years.

o **Automatic overseas tests**:

1. The individual was UK-resident for one or more of the three previous tax years, spends less than 16 days in the UK in the tax year and does not die in the tax year.
2. The individual was not UK-resident in any of the three previous tax years and spends less than 46 days in the UK in the tax year.
3. The individual 'works sufficient hours' overseas in the tax year (detailed rules apply).
4. The individual dies during the tax year, having been non-UK resident in each of the two previous tax years (or non-UK resident in the previous tax year, following a split tax year), and having spent less than 46 days in the UK in the tax year.
5. The individual dies during the tax year, having been non-UK resident in each of the two previous tax years by virtue of 'working sufficient hours overseas' (or non-UK resident in the previous tax year by virtue of 'working sufficient hours overseas', following a split tax year), and 'works sufficient hours overseas' (appropriately modified for the date of death) in the tax year.

An individual will not be UK-resident for a tax year in which he meets any of the automatic overseas tests.

– **Sufficient ties test**: if none of the 'automatic UK tests' or the 'automatic overseas tests' are met, an individual will be UK-resident for a tax year in which he has sufficient ties to the UK. The possible ties are defined in detail, and depend on whether the individual is an 'arriver' (i.e. was not UK-resident for any of the three previous tax years), or a 'leaver' (i.e. was UK-resident for one or more of the three previous tax years):

o **Arrivers**: there are four possible ties:

1. A family tie (where a family member is resident in the UK);
2. An accommodation tie (where UK accommodation is available for at least 91 consecutive days in the year, and occupied for at least one day);
3. A work tie (where the individual works in the UK for more than 3 hours a day for at least 40 days in the year); and
4. A 90-day tie (where the individual spent more than 90 days in the UK in either or both of the two previous tax years).

The individual will be UK-resident for a tax year in which he has sufficient ties, depending on the number of days spent in the UK:

- 46 – 90: all four ties;
- 91 – 120: three or more ties; or
- 121 – 182: two or more ties.

o **Leavers**: there are five possible ties:

1. A family tie;
2. An accommodation tie;
3. A work tie;
4. A 90-day tie; and
5. A country tie (where the individual is in the UK at midnight on more days than in another country).

The individual will be UK-resident for a tax year in which he has sufficient ties, depending on the number of days spent in the UK:

- 16 – 45: four or more ties;
- 46 – 90: three or more ties;
- 91 – 120: two or more ties; or
- 121 – 182: at least one tie.

The SRT will bring a welcome degree of certainty to establishing whether an individual is tax resident in the UK and provide a more robust basis for planning. However, there are many detailed provisions and definitions and, due to the level of detail and complexity in the legislation, professional advice about the application of the new rules to each case will be essential in all but the simplest circumstances.

INHERITANCE TAX: SPOUSES AND CIVIL PARTNERS DOMICILED OVERSEAS

From 6 April 2013, the inheritance tax (IHT) exemption for gifts of assets by a UK-domiciled individual to a non-UK domiciled spouse or civil partner is increased from GBP 55,000 to GBP 325,000. The limit will be pegged to future changes in the IHT nil rate band.

Non-UK domiciled spouses or civil partners of a UK-domiciled person will also be able to elect to be treated as UK domiciled for inheritance tax purposes.

TRANSFERS OF ASSETS ABROAD BY INDIVIDUALS

The transfer of assets abroad rules, designed to stop individuals avoiding tax by arranging for their income to accrue to non-resident entities such as offshore trusts and companies, will be amended as a result of the EU Commission having declared that the provisions do not comply with EU law.

There will be a new exemption for 'genuine' transactions, defined as being on arm's length terms and where taxing the transfer would constitute an unjustified and disproportionate restriction on an EU treaty freedom. Where a transaction contains both 'genuine' and 'non-genuine' parts, the income will be apportioned and only the 'non-genuine' part will be liable to tax.

Other changes will include a provision to prevent a claim that a double tax treatment overrides the rules. The legislation will have retrospective effect from 5 April 2012.

GENERAL ANTI-ABUSE RULE

The Finance Bill also includes the previously-announced general anti-abuse rule (GAAR), which will apply to income tax, National Insurance Contributions, corporation tax, capital gains tax, inheritance tax, petroleum revenue tax, stamp duty land tax and the annual tax on enveloped dwellings.

The legislation will provide for the counteraction of tax advantages arising from abusive tax arrangements entered into on or after Royal Assent to the Finance Bill. HMRC will have to follow set procedural requirements in order to apply the terms of the GAAR to any such arrangements. It is stated that counteraction will be on a 'just and reasonable' basis, and it is hoped that these requirements will protect any genuine, commercial planning.

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ARGENTINA

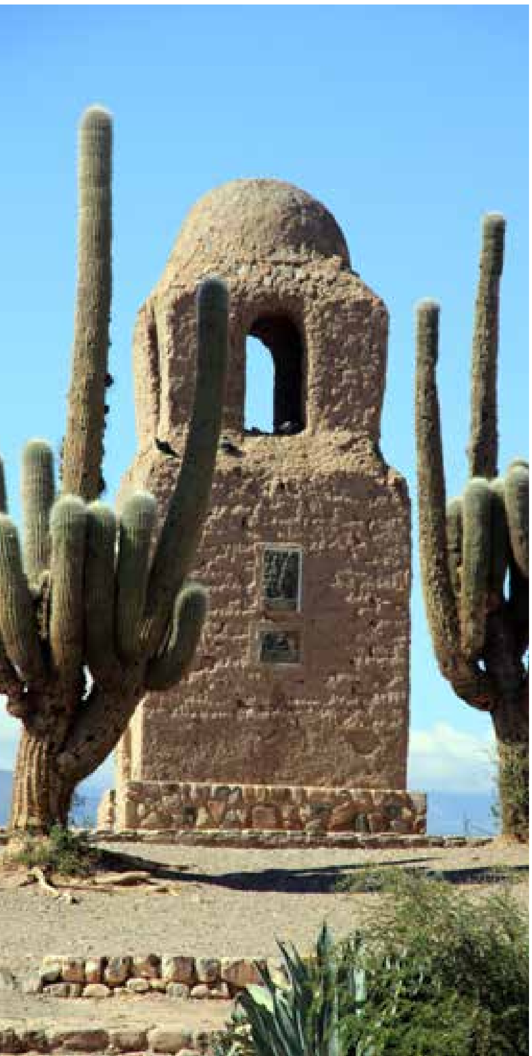
NEW TAX, CUSTOMS AND SOCIAL SECURITY PAYMENT PLAN

The Argentinean tax authority has introduced a special payment facility which will enable companies and individuals to settle tax and social security liabilities in up to 120 monthly instalments, with a monthly interest rate of 1.35%. The payment plan will be available for liabilities due up to 28 February 2013. Applications to use the facility can be made from 15 April 2013 to 31 July 2013.

ELIGIBLE LIABILITIES

The liabilities which are covered by the facility are:

- Tax and social security liabilities due up to 28 February 2013, including interest, adjustments and fines;
- Fines or additional charges made by the Customs Service up to 28 February 2013 in relation to import or export taxes, including interest and adjustments;
- Tax on non-documented operations;
- Tax debts arising from inspections, provided the taxpayer agrees the assessment;
- Debts under discussion at an administrative, litigation or judicial level;
- Liabilities currently included in "Mis Facilidades" payment plans.



INELIGIBLE LIABILITIES

The facility does not include:

- Withholding taxes, except for personal contributions for employees;
- Advance payments;
- Employer and employee contributions for the National Board of Public Works; except for those in the "Monotributo" scheme;
- Any charges related to Labour Risk Insurers (ART);
- Social security contributions for domestic servants;
- Contributions in relation to workers in the Monotributo scheme up to June 2004;
- Monthly contributions for the Register and the National Workers Agricultural Employers (RENATEA);
- Existing payment plans other than "Mis Facilidades" plans;
- Compensatory and punitive interest, penalties and other amounts;
- Additional Emergency Tax on cigarettes, including interest, compensatory and punitive fines and other amounts;
- Income tax and minimum presumed income tax for the fiscal years ending on or after 1 October 2012, and the Personal Property Tax for the fiscal year 2011;
- Value added tax for the provision of services made abroad, where the use or actual exploitation is carried out in the country;
- Tax liabilities resulting from the repeal of the ability to compute 100% of contributions paid as a credit VAT tax for certain companies;
- Customs charges generated by differences in export duty agricultural products subject to Law No. 21,453;
- Liabilities for individuals charged with criminal offences or common offences for tax evasion.

OUR COMMENTS

Our opinion is that this facility seeks to provide benefits to those parties that: (i) owe amounts to the tax authorities or (ii) have pending litigation and they understand that the ruling will be unfavourable.

However, while the facility allows an alternative method of payment of the tax amount and the respective compensatory interest and fines at a very economical financial rate, it does not forgive any sanction for those parties that have previously filed their tax returns and are currently amending them.

That is to say, those parties interested in voluntarily amending any tax return, having detected some tax omission for whatever reason (such as wishing to amend the criterion previously applied), can finance the payment of the unpaid tax amount and respective compensatory interest, but not fines.

In such circumstances, in deciding whether to use the facility, the implications should be analysed on a case-by-case basis.

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CANADA

BUDGET INCLUDES INTERNATIONAL CHANGES

On 22 March 2013 the Canadian government released its annual budget. The budget focused on job creation, economic development and on eliminating the budget deficit by the 2015-16 fiscal year. With respect to tax measures, the budget focused on closing some "tax loopholes" to ensure fairness in the Canadian tax system.

With regard to international tax measures, the budget contained the following three items:

THIN CAPITALISATION

The Canadian thin capitalisation rules limit the deductibility of interest expense of a Canadian resident corporation in circumstances where the debt owing to specified non-residents exceeds a 1.5-to-1 debt-to-equity ratio. A specified non-resident shareholder is a non-resident person or group owning shares representing more than 25% of the votes or value of the company. The 2012 budget extended these rules to apply to partnerships of which a Canadian-resident corporation is a member.

The 2013 budget further extends the scope of the thin capitalisation rules. They will now apply not only to Canadian corporations and partnerships, but also to Canadian-resident trusts, and non-resident corporations and trusts that operate in Canada. This will impact Canadian investments that were set up in this manner to avoid the Canadian thin capitalisation rules. The extension of the rules to partnerships has also been extended and will now apply where a Canadian-resident trust or a non-resident corporation or trust is a member of a partnership.

These changes apply to taxation years that begin after 2013. They apply to existing as well as new loans.

TREATY SHOPPING

In recent years, the Canadian courts have ruled in favour of the taxpayer in two significant "treaty shopping" cases. "Treaty shopping" is the process of structuring a business that operates internationally through jurisdictions to take advantage of more favourable treaties available in those jurisdictions than if the investment had been made directly. In both the Prevost and Velcro cases, the courts respected tax planning that involved the flow of dividends, in the case of Prevost, and royalties, in the case of Velcro, through an entity set up in the Netherlands, as this entity was considered to be the beneficial owner of the income streams it received.

In the 2013 budget, the government announced its intention to consult on possible measures that would protect the integrity of Canada's tax treaties by limiting "treaty shopping" while still preserving a business tax environment that is conducive to foreign investment. A consultation paper will be publicly released to give taxpayers an opportunity to comment on possible measures before any action is taken. As a result of this process, Canada may soon join a number of other countries that have passed anti-treaty shopping laws to prevent this type of planning.

INTERNATIONAL TAX EVASION AND AGGRESSIVE TAX AVOIDANCE

The government announced two measures aimed at ensuring that Canadian residents are paying tax on their worldwide income and not evading Canadian taxes through the use of investments made in tax havens:

- Beginning in 2015, certain financial intermediaries (including banks, credit unions, caisses populaires, trust and loan companies, money service businesses and casinos) must report international electronic fund transfers of CAD 10,000 to the Canadian tax authorities; and
- The "Stop International Tax Evasion Program" will be launched, under which the Canadian tax authorities will pay rewards of up to 15% of the tax collected to individuals with knowledge of major international tax non-compliance when they provide information to the tax authorities that results in additional assessment of Canadian federal tax exceeding CAD 100,000. All rewards will be based on federal tax collected and will be subject to income tax. Further details of this program will be announced in the coming months.

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PUERTO RICO

NEW TAX INCENTIVES TO ENCOURAGE RELOCATION TO PUERTO RICO

Puerto Rico is making bold moves to attempt to reverse its negative economic trends and bring individuals (including Puerto Rican nationals who may have left many years before), families, and businesses back to its economy.

These moves include the following tax measures which were enacted in 2012:

– Act No. 22 of 2012 (Act No 22), which contains numerous incentives to encourage individuals to relocate to Puerto Rico. New residents in Puerto Rico will receive a100% tax exemption from Puerto Rico income taxes on all dividends, interest and long-term capital gains accrued from qualifying investments after the individual becomes a bona-fide resident of Puerto Rico. The new resident must not have been a resident of Puerto Rico at any time during the 15-year period preceding the effective date of Act 22, i.e. from 16 January 1997 to 16 January 2012;

– The Export Services Act (Act 20 of 2012), which provides for a 4% maximum tax rate on income related to export services provided by new Export Services businesses in Puerto Rico; and

– The International Financial Center Regulatory Act (Act 273 of 2012), which aims to make Puerto Rico an international banking and financial centre by providing tax incentives (mainly, a 4% income tax rate) for new banking and financial activity in Puerto Rico on behalf of clients outside of Puerto Rico.

INCENTIVES GUARANTEED

Prior to relocating, individuals can apply for a Puerto Rico tax decree, which would serve as a contract guaranteeing the incentives from any subsequent changes in local legislation until 2035.

U.S. INDIVIDUALS WHO BECOME BONA FIDE RESIDENTS OF PUERTO RICO

In general, a U.S. individual remains subject to full Federal income tax regardless of where he or she is domiciled. However, the U.S. Internal Revenue Code of 1986, as amended (the Code), provides special rules for an “individual who is a bona fide resident” of Puerto Rico. Under these special rules, income from sources within Puerto Rico is not included in gross income and is not subject to U.S. federal income tax. Thus, there are two levels of inquiries for U.S. individuals who relocate to Puerto Rico. First, is the individual a bona fide resident of Puerto Rico? If so, second, what items of income can be included in his or her Puerto Rico income, and thereby excluded from U.S. income?

BONA FIDE RESIDENTS OF PUERTO RICO

An individual is considered to be a bona fide resident of Puerto Rico if three tests are met:

1. The individual must be present for at least 183 days during the taxable year in Puerto Rico (the presence test). This test is loosened by Treasury Regulations. Under these regulations, an individual will be considered to meet the presence test if one of five tests is met:

   i. The individual was present in Puerto Rico for at least 183 days during the taxable year;

   ii. The individual was present in Puerto Rico for at least 549 days during the 3-year period consisting of the current taxable year and two immediately preceding taxable years, provided that the individual was present in Puerto Rico for at least 60 days during each of such years;

   iii. The individual was present in the United States for no more than 90 days during the taxable year;

   iv. During the taxable year, the individual had earned income (meaning wages, salary, professional fees and compensation for personal services actually rendered) of less than USD 3,000 and was present for more days in Puerto Rico than in the United States; or

   v. The individual had no significant connection to the United States during the taxable year. This test will be satisfied if any of the three following conditions are met: the individual has no permanent home in the U.S., no current U.S. voter registration, or no spouse or child under the age of 18 whose principal place of abode is in the United States unless the child is living in the U.S. with a custodial parent under a custodial decree or the child is in the U.S. as a student.

2. The individual must not have a tax home (a regular or principal place of business, or a regular place of abode) outside of Puerto Rico during the taxable year.

3. The individual must not have a “closer connection” to the United States or a foreign country than Puerto Rico during the taxable year. The closer connection test is a facts and circumstance test. Specifically, an individual is considered to have a closer connection to Puerto Rico than elsewhere if he or she maintains more significant contacts with Puerto Rico than the United States. The factors to take into account are the location of the individual's permanent home, family, belongings, organisations, personal bank, business activities, driving licence and voter registrations, and the country of residence designated by the individual on forms and documents. In addition, an individual must be considered to possess a closer connection to Puerto Rico than to the United States or a foreign country <u>for the entire taxable year</u>.

Special rules apply to determine whether the tax home test and the closer connection test are satisfied in the taxable year during which the individual relocates to Puerto Rico. An individual is eligible to take advantage of the special rule if three tests are met:

1. The individual must not have been a bona fide resident of Puerto Rico during each of the three taxable years preceding the year of the move.

2. During the second half of the year of the move, the individual must not have had a tax home in, or closer connection to, the United States or a foreign country than Puerto Rico.

3. The individual must be a bona fide resident of Puerto Rico for each of the three years following the year of the move to Puerto Rico.

If all of these conditions are met, the individual will be considered to have satisfied the tax home and closer connection tests for the year of the relocation.

INCOME ELIGIBLE TO BE EXEMPT FROM UNITED STATES FEDERAL INCOME TAX

There seems to be a common misconception that once an individual has become a bona fide resident of Puerto Rico, all income earned by the individual escapes U.S. federal income tax. However, Code § 933(1) limits the exemption to "income derived from sources within Puerto Rico." Applicable regulations provide detailed rules on when income will be considered to have been derived from Puerto Rican sources.

For example, the source of investment income, such as interest and dividends, retains its U.S.-source income status when paid by U.S. corporations to a bona fide resident of Puerto Rico. All income earned in connection with the conduct of a trade or business in the United States is also treated as U.S.-source income. Anti-avoidance rules also apply.

U.S. EXPATRIATION RULES DO NOT APPLY TO A RELOCATION TO PUERTO RICO

The U.S. expatriation tax rules, including Code § 877, under which former U.S. taxpayers who expatriate for tax purposes remain subject to U.S. tax for a ten year period, and Code § 877A, which charges tax on unrealised gains at the time of expatriation, do not apply to a U.S. individual who relocates to Puerto Rico.

SUMMARY

Puerto Rico Law 22 provides a clear Puerto Rican tax incentive for investors to consider the arduous process of relocating their personal life and business affairs to Puerto Rico. This may be particularly attractive to U.S. taxpayers, following the income tax increases recently signed by President Obama. However, the benefits of the new Puerto Rican tax regime are substantially tempered by the existing U.S. rules which continue to apply to Puerto Rican residents, except for income from Puerto Rican sources and capital gains economically attributable to the holding period during which the individual is a resident of Puerto Rico.

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UNITED STATES OF AMERICA

THE AMERICAN TAXPAYER RELIEF ACT OF 2012 EXTENDS FAVOURABLE INTERNATIONAL TAX PROVISIONS

INTRODUCTION

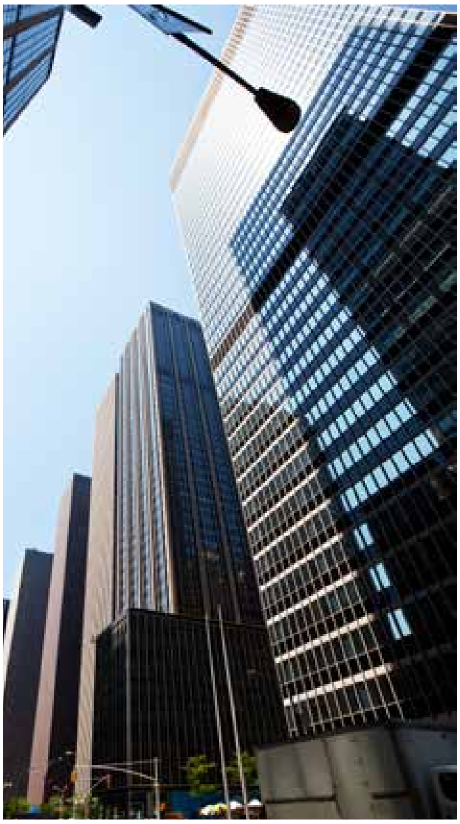
On 1 January 2013, Congress passed the American Taxpayer Relief Act of 2012 (the Act), which the President quickly signed into law on 2 January 2013. The Act extends a host of expired and expiring tax breaks for businesses and individuals, and adds a number of new provisions as well. Some of the international tax highlights are discussed below.

IMPACT

Certain provisions of the Act affect international structures and transactions by extending: (1) the look-through rules between controlled foreign corporations (CFCs) and (2) the qualified dividend income (QDI) tax rates, providing for maximum rates identical to those applicable to long-term capital gains on dividends received by qualified foreign subsidiaries. In addition, the enactment of permanent QDI maximum tax rates and other rules can present additional tax benefits for individual shareholders of Interest Charge Domestic International Sales Corporations (IC-DISCs).

EFFECTIVE DATES

The extension of the CFC look-through rules applies to taxable calendar years of foreign corporations through to 31 December 2013. For fiscal year foreign corporations, the extension applies through to the fiscal tax year ending after 31 December 2013. The extension and modification of the QDI maximum tax rates apply to taxable years beginning after 31 December 2012.



PLANNING OPPORTUNITIES

- **CFC look-through rules**: one of the key provisions extended by the Act is the CFC look-through rule under section 954(c)(6). Originally enacted in 2005 (and subsequently extended in 2008 and 2010), section 954(c)(6) provides that dividends, interest, rents, and royalties received or accrued by a CFC from a related CFC shall not be treated as foreign personal holding company income as long as the paying CFC generated qualified active (i.e. non-subpart F and not United States effectively connected) income.
- **Enactment of permanent maximum QDI rates**: another significant outcome of the Act was the enactment of permanent maximum tax rates for QDI rate under section 1(h)(11). This provision provides tax planning opportunities for United States businesses operating as S corporations and partnerships (including limited liability companies taxed as partnerships) that engage in cross-border activities.

  Dividends that are considered qualified dividends are taxed at the same federal tax rates as long-term capital gains for individuals. This rate (depending on income) is generally either 15% or 20% before consideration of the newly-introduced additional 3.8% tax on net investment income. The reduced tax rate is attributable to qualified dividends received from qualified foreign corporations as well as gains from the disposition of the shares that are subject to section 1248.

  Qualified foreign corporations are defined under section 1(h)(11)(C) as corporations that are incorporated in a possession of the United States or foreign corporations that are eligible for benefits of a comprehensive income tax treaty with the United States which the Secretary of the Treasury determines is satisfactory and which includes an exchange of information program.

  The Service has provided guidance (most recently in Notice 2011-64) on the specific countries with which the United States has a comprehensive income tax treaty that may allow for qualified dividend treatment on the receipt of dividends from corporations in those respective countries. Other guidance regarding the types of income earned by the foreign country corporation and the availability for the qualified dividend rate is provided in Notice 2004-70.

  As United States businesses consider how to organise foreign activities, a structure that allows the use of the qualified dividend rate should be considered, while also taking into account local country corporate income and withholding taxes.
- **IC-DISC and QDI opportunities**: the enactment of a permanent reduced rate of either 15% or 20% with respect to QDI may allow for tax planning opportunities for United States businesses with certain export transactions. For those United States entities engaged in export transactions, the use of an IC-DISC can result in a reduced tax rate on export-related profits. One of the tax benefits of using an IC-DISC is that dividends paid to individual shareholders are eligible for the qualified dividend rate discussed above.

  IC-DISCs are United States corporations that can be utilised in conjunction with S corporations, partnerships (including limited liability companies taxed as partnerships), and closely-held C corporations to achieve a favourable tax result related to a company's profits attributable to products that are manufactured for export from the United States. IC-DISCs are not subject to federal corporate income tax. In its simplest form, the benefit is attributable to the manufacturer (the related United States entity) being entitled to a deduction, at ordinary tax rates, for a commission paid to the IC-DISC and the subsequent distribution from the IC-DISC being eligible for the lower rate as it is treated as qualified dividend income in the hands of the shareholder.

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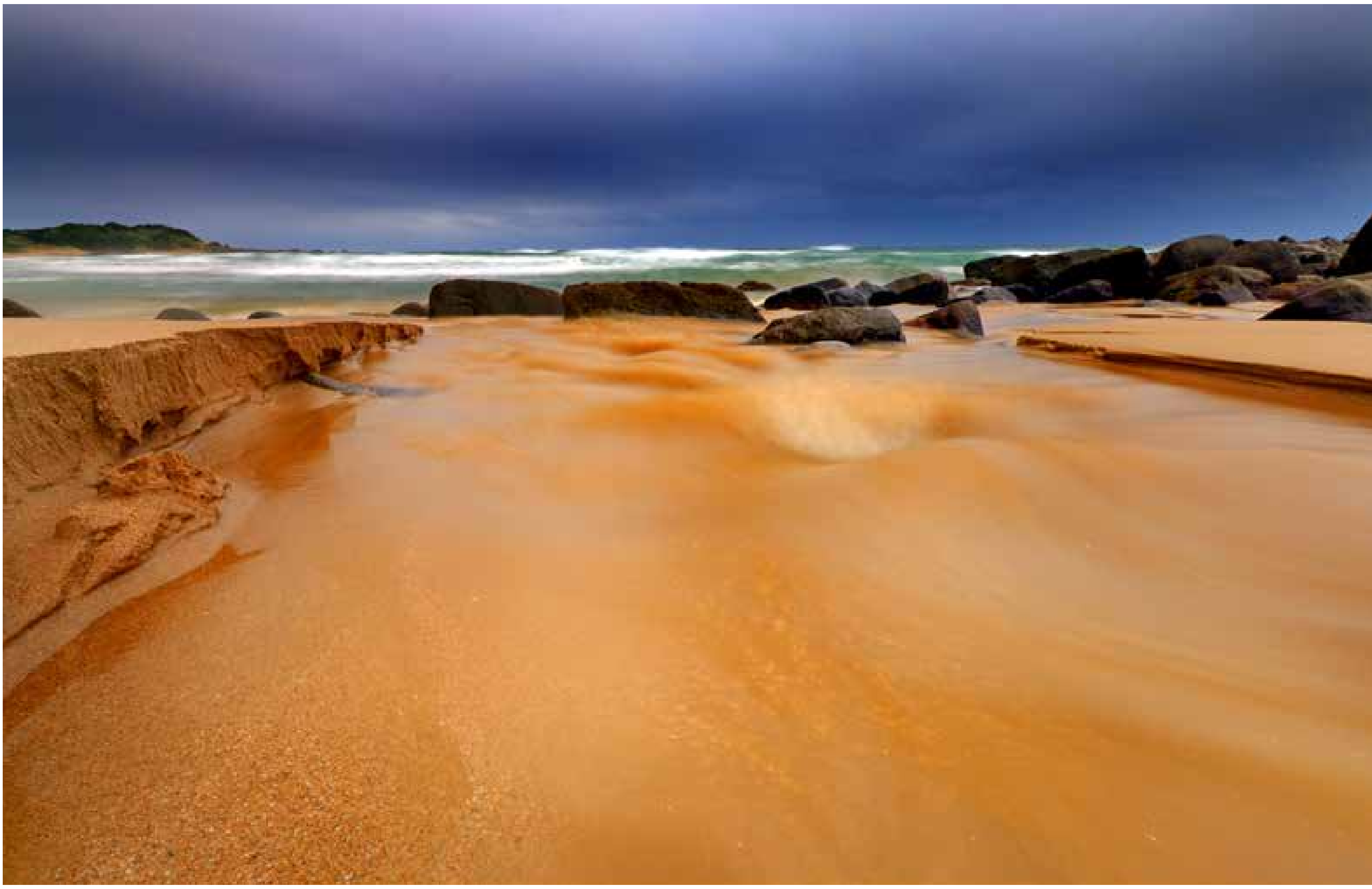
SOUTH AFRICA

NEW WITHHOLDING TAXES



New withholding taxes on interest and royalties paid to or for the benefit of non-South African residents will come into effect on 1 March 2014.

The new rules will apply to non-residents who spend up to 183 days in the country or who do not have a permanent establishment, such as a branch in South Africa. Non-residents who are physically present in South Africa for more than 183 days, or who have carried on business through a permanent establishment in the country, in the aggregate 12 months before the interest or royalties were paid, will be exempt from the withholding taxes, but would be subject to income tax in the normal way.

The taxes on both interest and royalties have been set at a 15% rate, subject to double taxation rates. This is in line with the withholding tax on dividends that came into effect on 1 April 2012, and it will apply to interest or royalties that either accrue, are paid, or become due and payable on or after 1 March 2014. In the case of interest, this includes the payment of interest to a South African resident as a collection agency for a non-resident creditor. Specifically, interest accrued before that date, but only paid after 1 March 2014, will attract the new tax.

There will be some exemptions, depending on how the interest is earned. *Inter alia*, any interest paid in respect of any government debt instrument, any listed debt instrument, any debt owed by any bank, the South African Reserve Bank, and any interest arising from the import of goods, will be exempt.

The responsibility for deducting and remitting the withholding taxes will be that of the entity making the payments, but the ultimate liability is that of the recipients of the payments. Payments to SARS will have to be made by the last day of the month following that in which the interest or royalty payment has been paid.

Refunds will be entertained if the recipient was unable to present the relevant declaration forms to the payer in time.

These amendments to South Africa's laws close the near-blanket exemption for local interest earned by non-residents subject to exceptions in limited instances.

Some elements of the new laws will have to be tested in the courts for clarity. Beneficial ownership is likely to cause concerns, given there is no international consensus on a definition. For example, interest could be paid to a South African trust with non-resident beneficiaries, posing the question as to who the beneficial owner was. One solution may be to establish whether or not the trust had discretion in its payments or whether it was bound to pay only the non-residents.

Another issue could concern what portion of a loan repayment constitutes interest. A ZAR 100 million loan may incur annual payments of ZAR 25 million, of which perhaps ZAR 20 million represented interest, with the balance being capital. However, it may be possible to treat the whole amount as a capital repayment if that was defined in the loan terms. The law does not clearly define the issue.

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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 14 May 2013.

Currency unit	Value in euros (EUR)	Value in US dollars (USD)
Euro (EUR)	1.00000	1.29735
British Pound (GBP)	1.18231	1.53403
Canadian Dollar (CAD)	0.76208	0.98880
Hong Kong Dollar (HKD)	0.09929	0.12884
Indian Rupee (INR)	0.01407	0.01826
Singapore Dollar (SGD)	0.62118	0.80598
South African Rand (ZAR)	0.08434	0.10946
US Dollar (USD)	0.77071	1.00000

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