

6th Annual IBA Tax Conference: Current International Tax Issues in Cross-Border Finance and Capital Markets

London, 31 January 2017, 9 am to 11 am

Panel on

Tax Controversy

Panellists:

Francesco Capitta, Macchi di Cellere Gangemi, Rome, Italy

Sam K. Kaywood, Jr., Alston & Bird, Atlanta, GA, USA

Margriet Lukkien, Loyens & Loeff, Amsterdam, Netherlands

Peter Reinartz, Bär & Karrer, Zurich, Switzerland

Jean Schaffner, Allen & Overy, Luxembourg, Luxembourg

Jonathan Schwarz, Temple Tax Chambers, London, United Kingdom

Chair:

Wilhelm Haarmann, Linklaters, Frankfurt/Main, Germany

Tax Controversy CbC and Exchange of Tax Rulings

BÄR
& KARRER

6th Annual IBA Tax Conference, London

31 January 2017

Peter Reinarz

Spontaneous Exchange of Rulings

Overview

The final report on BEPS Action 5 recommends to introduce the spontaneous cross-border exchange of tax rulings that relate to harmful tax practices or potentially contradict the principles of BEPs.

Currently, the OECD-member states around the world are amending their regulations in this regard.

Based on the OECD the following categories of tax rulings might be subject of a spontaneous exchange of information:

- Rulings relating to the taxation as a holding company, a domicile company, a mixed company, with a principal allocation or a patent/license box;
- Unilateral tax rulings covering cross-border transfer prices;
- Cross-border rulings providing for an unilateral downward adjustment of the taxable income in a country, that is not directly reflected in the financial statements;
- Cross-border rulings concerning the existence or absence of, and / or the attribution of profits to, a permanent establishment;
- Cross-border rulings related to conduit structures (as channelling via hybrid entities / hybrid flows).

Spontaneous Exchange of Rulings

Questions for local counsels

1. What is the status of signing and implementation of the Convention on Mutual Administrative Assistance in Tax Matters in your specific country?
2. What is the expected timeline for the application of the spontaneous exchange of rulings in your country?
3. Rulings with regard to which type of taxes will be exchanged?
4. What will happen with received information based on the spontaneous exchange of rulings? Shall it be expected that in your country the information will be systemically reviewed?
5. How will your government ensure that the received information is secure (trade secret)?
6. Will the government in your country be legally entitled to use such type of information in (i) legal proceedings or (ii) assessment process retroactively?

Spontaneous Exchange of Rulings

Questions for local counsels

1. What is the status of signing and implementation of the Convention on Mutual Administrative Assistance in Tax Matters in your specific country?
 - Italy: Convention is effective
 - Netherlands: Convention is effective
 - Switzerland: Convention and domestic implementing legislation in effect (since 1/1/2017)
 - UK: Convention and 2010 Protocol signed
UK is bound the exchange rulings under EU Directive on Administrative Cooperation and does so under OECD BEPS Action 5.
 - Luxembourg: Convention and 2010 Protocol signed
 - US: Convention signed but not 2010 Protocol.
 - Germany: Convention and 2010 Protocol signed and effective

Spontaneous Exchange of Rulings

Questions for local counsels

2. What is the expected timeline for the application of the spontaneous exchange of rulings in your country?
 - Italy: Rulings are not expressly mentioned in the Convention. In principle, “rulings” could be included within the notion of “information” under Art. 7, para. 1. On 14 December 2016, the Italian Government approved a draft decree implementing EU Directive No. 2015/2376, which regulates the automatic mandatory exchange of rulings for direct taxes (social security contributions, VAT and other indirect taxes are excluded). The decree is not effective yet.
 - Netherlands: NL is working on exchanging information on rulings. Some information was exchanged already by 31 December 2016 and it will make sure that the remainder of the information on existing ruling is exchanged before 31 December 2017. Further, the Netherlands amended its legislation **as per 1 January 2017** to implement EU Directive No. 2015/2376 to exchange information on rulings between EU Member States. The scope of the term rulings in the Directive is broader than in OECD Action 5.
 - Luxembourg: Start date **for exchange 1/1/2017 (BEPS 5: as of 2010; Cooperation directive as of 2012)**
 - Switzerland: Ruling information will be collected as from 2017 and be exchanged with participating foreign tax authorities in 2018 for the first time.
 - Germany: Germany has introduced an automatic exchange of information on tax rulings. In general, tax rulings are to be disclosed which have been issued, reached, amended or renewed after 31 December 2016.

Spontaneous Exchange of Rulings

Questions for local counsels

3. Rulings with regard to which types of taxes will be exchanged?

- Italy:

The Convention applies to income taxes, indirect taxes, mandatory social security contributions and all other taxes of every kind. Custom duties collected on behalf of a party are excluded.

- Netherlands:

Rulings concerning direct taxes

- Luxembourg:

Rulings concerning direct taxes

- Switzerland:

OECD ruling categories --> i.e. rulings granting preferential regimes, APA's, rulings with transfer pricing angle, PE rulings, conduit rulings, other rulings with potential BEPS implications

- Germany:

Generally, rulings with regard to all taxes will be exchanged, excluded are e.g. VAT and custom duties

Spontaneous Exchange of Rulings

Questions for local counsels

4. What will happen with information received from the spontaneous exchange of tax rulings? Do you expect that such information will be systematically reviewed by your country's tax authorities?
- Italy: Yes
 - Luxembourg: No
 - Switzerland:
Yes. Information will be collected by the Federal Tax Administration and be shared with the cantonal tax authorities, which are in charge of assessing all direct taxes.
 - Germany:
Yes. Information from the automatic exchange will be reviewed by the Federal Tax Administration and shared with the competent local tax authorities.

Spontaneous Exchange of Rulings

Questions for local counsels

5. How will your government ensure confidentiality of the received information (protection of trade secrets etc.)?
 - Italy:
See Art. 22 of the Convention
 - Switzerland:
Strict legal provisions concerning data security/protection and professional and trade secrets are applicable
 - Germany:
See Art. 22 of the Convention

Spontaneous Exchange of Rulings

Questions for local counsels

6. Will the government in your country be legally entitled to use such type of information in (i) legal proceedings or (ii) assessment process retroactively?
 - Netherlands:

Yes, taking into account the regular statute of limitations
 - Italy:
 - (i) Yes.
 - (ii) Yes, within the terms under the Statute of Limitations.
 - Luxembourg:

Information could be considered as „new facts“ enabling a tax reassessment on 10-year period.
 - Switzerland:

In scope are tax rulings issued on or after 1/1/2010 that are still in force on 1/1/2018. Thus, such information could be used retrospectively, however, subject to statute of limitation (WHT: 5 years) and qualification as relevant „new facts“ for direct tax purposes, when assessment has already become final.
 - Germany:

Yes, subject to the applicable rules of procedure.

Country-by-Country Reporting Overview

Previous OECD Approach

Masterfile

Countryfile

BEPS Action 13

Master File (MF) *

Local File (LF) *

Country-by-Country Report (CbC) **

* OECD: Required for group entities that have a turnover exceeding an annual threshold of EUR 50 million.

** OECD: Required for multinationals with an annual turnover of a minimum of EUR 750 million.

Country-by-Country Reporting

Questions for local counsels

1. Has the "Multilateral Competent Authority Agreement on the exchange of Country-by-country reports" already been signed by local authorities?
2. What is the deadline regarding the implementation of the local guidelines?
3. What is the scope of the local implementation (Master file, Local File and CbC reporting vs. CbC reporting only ?)
4. What is the deadline for the submission of the respective files?
5. Is there a fixed date or are the files to be submitted upon request of tax authorities?
6. Are there any penalties, if not submitted on time?
7. Is English language accepted, or must the files be in local language?
8. Are there any facts for a criminal offence fulfilled in case a company officer provides foreign countries with such (tax relevant) information?

Country-by-Country Reporting

Questions for local counsels

1. Has the "Multilateral Competent Authority Agreement on the Exchange of Country-by-Country Reports" already been signed by local authorities?
 - Italy: Yes
 - Netherlands: Yes
 - UK: Yes
 - Luxembourg: Has approved Council Directive 2016/881 of 25 May 2016 amending the EU cooperation Directive 2011/16
 - Switzerland: Yes – on 27 Jan. 2016 Switzerland signed without reservation. This requires ratification by Federal Parliament and implementation in Swiss law (draft ALBA Act). Message of the Federal Council on MCAA-CbC and draft ALBA Act was published on 23 November 2016. Once approved by the Federal Parliament, the package will be subject to a facultative referendum. The package might enter into effect by the end of 2017 at the earliest.
 - US: Has not signed MCAA – CbyC, but has promulgated regulations that impose CbyC reporting starting with tax years of ultimate parent beginning on or after June 1, 2016.
 - Germany: Yes

Country-by-Country Reporting

Questions for local counsels

2. What is the deadline regarding the implementation of the local guidelines?
 - Italy: CbCR has been firstly regulated under Art. 1, para. 145-147, Law No. 208/2015. However, the implementing regulations have not been issued yet.
 - Netherlands: NL introduced legislation in accordance with Action 13 as per 1 January 2016
 - Luxembourg: CbCR applies as of 1 Jan. 2016
 - UK: UK reports all accounting periods starting on or after 1 January 2016
 - Switzerland: Assuming the new rules will enter into force by 31/12/2017, local guidelines should be pulished in the course of 2017. CbC reports will be required to be prepared for 2018 for the first time, first exchange taking place in 2020.
 - US: Filing of tax return for first tax period beginning on or after June 1, 2016.
 - Germany: Germany reports all accounting periods starting on or after 1 January 2016

Country-by-Country Reporting

Questions for local counsels

3. What is the scope of the local implementation (Master File, Local File and CbC reporting vs. CbC reporting only?)
 - Italy: N/A
 - Netherlands: NL implemented obligations for MF, LF and CbC
 - UK: UK resident ultimate parent companies report on consolidated group; entities of MNEs with UK connection to report where specific conditions are met.
 - Switzerland: Draft legislation adopts only *the minimum standard* pursuant to BEPS Action 13. Only the CbC Report (excluding master file and local file) will be required from (MNEs). Only Swiss head-quartered MNEs having consolidated group revenues exceeding CHF 900mn would need to provide CbC reports to Swiss tax authorities. Swiss based subsidiaries of foreign head-quartered MNEs may be required to file such a report, if the foreign based parent is not resident in a Partner State, or if there is a systemic failure in the foreign headquarter jurisdiction.
 - US: CbC reporting only.
 - Germany: Germany implemented obligations for MF, LF and CbC

Country-by-Country Reporting

Questions for local counsels

4. What is the deadline for the submission of the respective files?

- Italy:
N/a
- Netherlands:
12 months from the end of the relevant accounting period. So CbC file for calendar book year 2016 needs to be submitted before 31 December 2017.
- UK:
12 months from the end of the relevant accounting period.
- Luxembourg:
31 March n+2
- Switzerland:
The CBC report of a Swiss MNE will be due within 12 months after the finalization of the respective accounting year.
- US: file Form 8975 with filing of tax return, 9½ months after tax period of ultimate parent closes.
- Germany: 12 months from the end of the relevant accounting period

Country-by-Country Reporting

Questions for local counsels

5. Is there a fixed date or are the files to be submitted upon request of tax authorities?
 - Italy:
N/a
 - Netherlands:
The MF and LF should be available in the administration of the taxpayer by the due date of filing the tax return, but do not need to be submitted unless requested for by the DTA.
 - Luxembourg:
Fixed date
 - UK:
12 months from the end of the relevant accounting period.
 - Switzerland:
Same as UK.
 - File Form 8975 with tax return.
 - Germany: same as UK

Country-by-Country Reporting

Questions for local counsels

6. Are there any penalties if not submitted on time?
 - Italy:
EUR 10,000-50,000
 - Netherlands:
Yes
 - Luxembourg
EUR 250k
 - UK:
GBP 300, plus GBP 60 per day
 - Switzerland:
Draft legislation provides for penalties of CHF 200 per day
 - US: No specific penalty but tax return may not be complete without proper Form 8975.
 - Germany: max. EUR 10,000

Country-by-Country Reporting

Questions for local counsels

7. Is English language accepted or must the files be in local language?

- Italy:
N/a
- Netherlands:
Dutch or English
- UK:
No language specified
- Luxembourg
Yes
- Switzerland:
English, German, French, or Italian
- US: English
- Germany: In general German, exceptions allowed

Country-by-Country Reporting

Questions for local counsels

8. Are there any facts for a criminal offence fulfilled in case a company officer provides foreign countries with such (tax relevant) information?
- Italy: N/a
 - Luxemburg: Information transits via Luxembourg Revenue
 - UK: No criminal offenses specific to CbCR
 - Switzerland
 - Proactive compliance with CbC Reporting duties pursuant to BEPS Action 13 might be qualified as forbidden acting for a foreign state, according to Swiss Penal Code, art. 271.
 - Background model case: CH HoldCo owns a CH and, say, a NL subsidiary. Unlike CH, NL implements the full scope of CbCR, including local files and master file. The CFO of the NL Sub requests copies of the CH tax rulings pertaining to HoldCo, providing inter alia for a transfer pricing for group-internal management services provided by HoldCo based on cost + 10%. Against that background, CH corporate officers are recommended to obtain prior approval from the federal authorities. Notably, CH draft rules provide for CbC Reports and relevant tax rulings to be provided to the Swiss Federal Tax Administration, which will subsequently exchange the information automatically with relevant foreign tax authorities.*
 - US: N/A
 - Germany: No criminal offenses specific to CbCR



6th Annual IBA Tax Conference:

Introduction of GAAR and EU Anti-Tax Avoidance Directive

31 January 2017, 9 am to 11 am

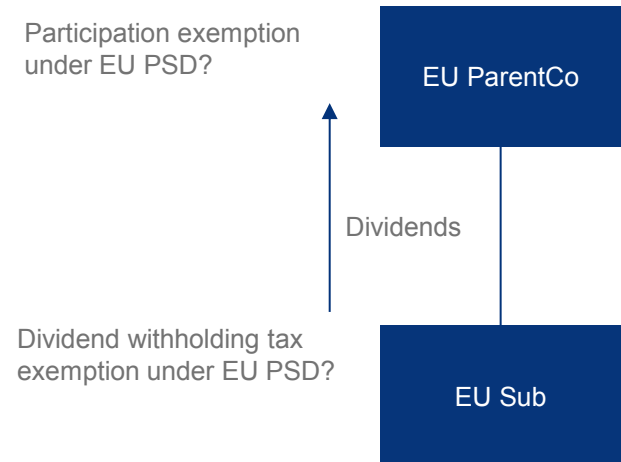
Margriet Lukkien – tax partner Loyens & Loeff NV Amsterdam

EU PSD GAAR

- Introduction of mandatory general anti-abuse rule (**EU PSD GAAR**) in EU Parent Subsidiary Directive (**EU PSD**)
- Implementation required by the Member States before 1 January 2016. Hence a reality as per 1 January 2016!
- Diverging approaches in the 28 Member States, despite the EU wish to apply a common approach
- Possibly also an EU GAAR in EU Interest & Royalty Directive with a minimum effective taxation clause
- More pressure on entitlement to tax exemptions for EU dividends, EU interest payments and EU royalties

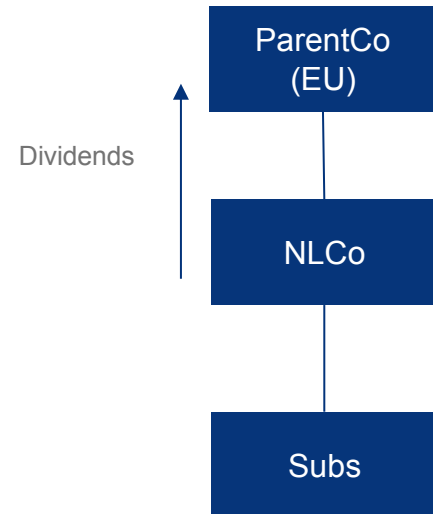
EU PSD GAAR

- **Purpose:** not to grant EU PSD benefits for EU dividends in abusive situation
- But what is an abusive situation?
 - **Tests:**
 - What is the main purpose or one of the main purposes of the structure?
 - Does it defeat the object or purpose of the EU PSD?
 - Is the structure genuine, i.e. has it been put into place for valid commercial reasons which reflect economic reality?



Dutch implementation of EU PSD GAAR

- Not in dividend withholding tax act, apart from specific anti-abuse rules for cooperatives
- Not in Dutch participation exemption regime for corporate income tax (**CIT**) purposes
- Only amendments in Dutch non-resident CIT rules as per 1 January 2016
 - Covers:
 - EU and non-EU situations
 - Dividends **plus** other sources of income
- In practice generally possible to comply with these amendments in order not to trigger Dutch non-resident CIT



EU PSD GAAR – implementation in other jurisdictions

- Change of legislation; as per when and how?
- Changes in practice due to the EU PSD GAAR?
- EU policing?
- (Recent) court judgments

EU Anti-Tax Avoidance Directive

- EU Anti-Tax Avoidance Directive (**ATAD**):
 - Adopted on 20 June 2016
 - To be implemented by the Member States in principle as per 2019
 - EU policing?

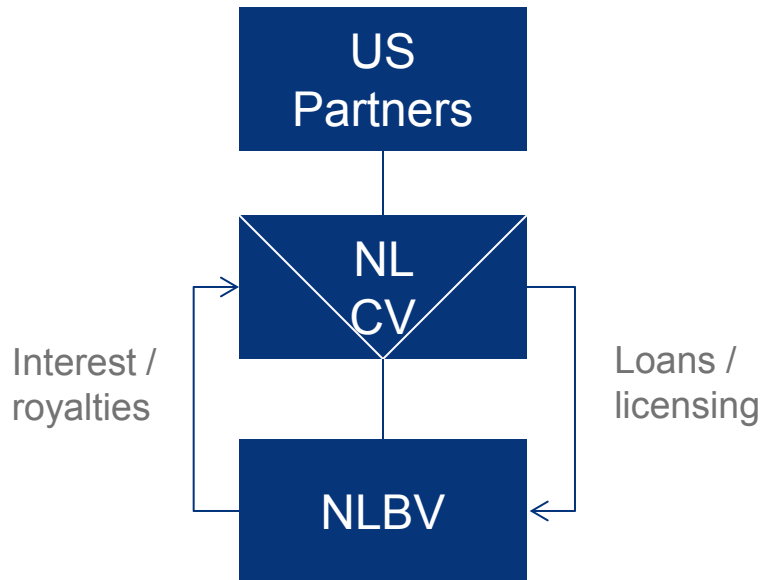
EU Anti-Tax Avoidance Directive

- ATAD requires all Member States to have certain provisions on:
 - Controlled foreign company (**CFC**) rules; 2 options:
 - (i) tax non-distributed passive income or
 - (ii) profits derived from non-genuine arrangements
 - Hybrids; limited to intra-EU hybrid mismatches
 - Interest deductibility limitation based on earnings stripping rule;
 - Limits deduction of net borrowing costs to in principle 30% of taxpayer's EBITDA
 - Exit tax; due over hidden value in assets upon migration and possibly deferral of tax due
 - General anti-abuse rule (**GAAR**); to attack non-genuine arrangements

EU Anti-Tax Avoidance Directive

- Upgraded version of ATAD was proposed on 25 October 2016 (**ATAD 2**)
 - To neutralize hybrid mismatch structures involving third (non-EU) countries
 - Content and implementation date still under discussion

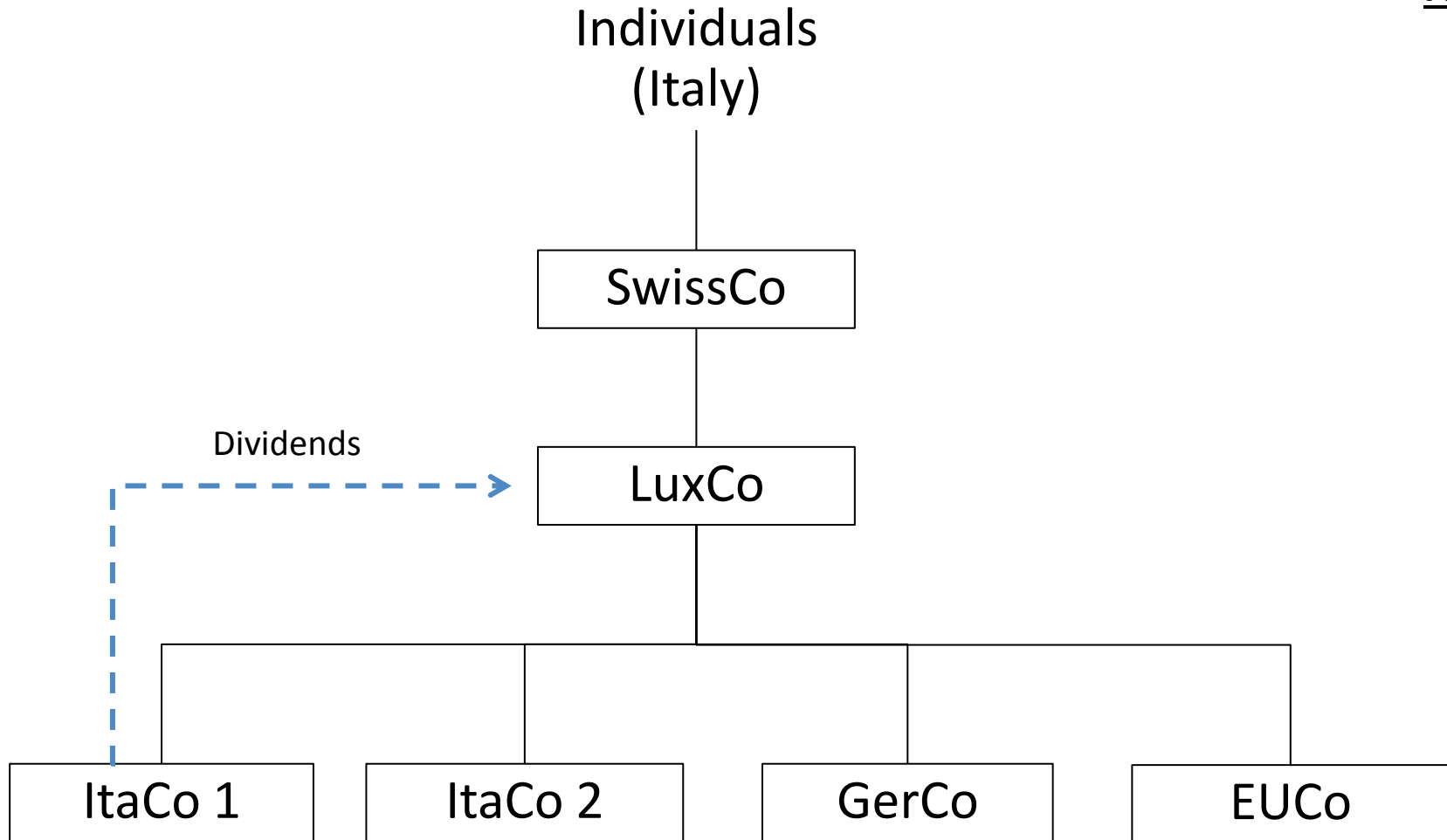
EU Anti-Tax Avoidance Directive



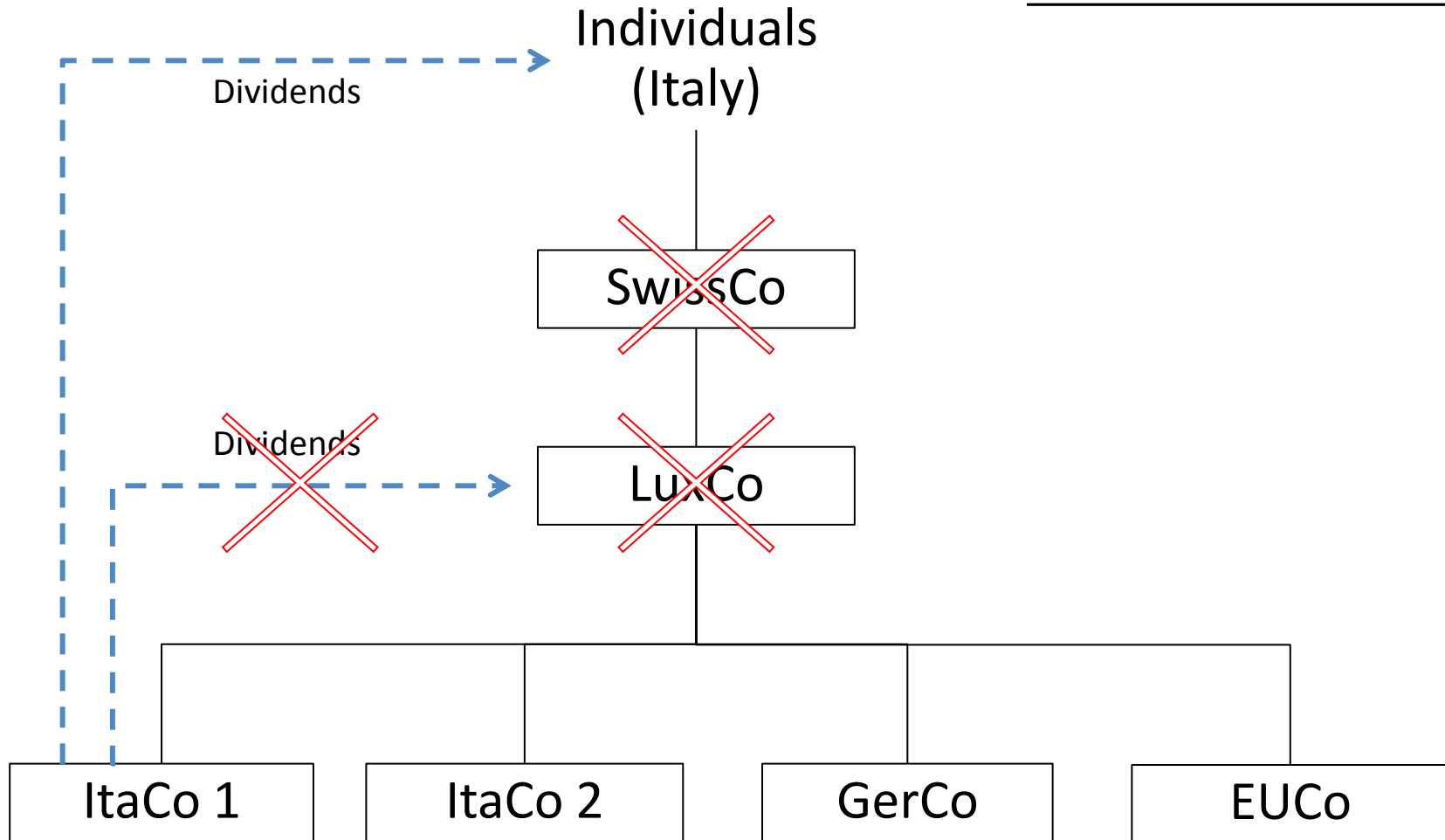
- CV/BV structures not covered by ATAD
- Still works from a Dutch tax and US tax perspective
- But it is a hybrid mismatch covered by ATAD 2

Holding Companies Under Attack

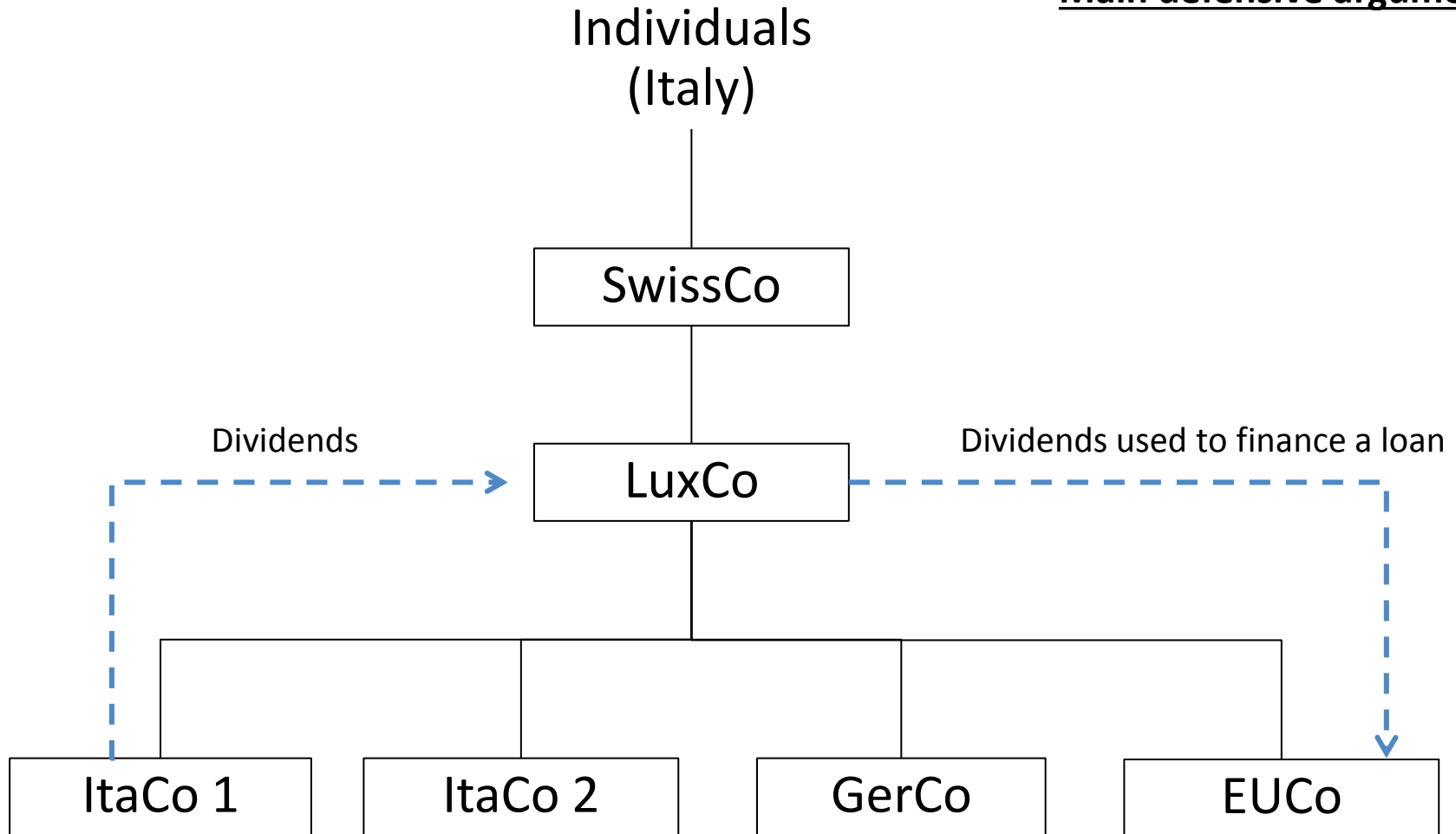
Facts



Italian Tax Authorities' claim



Main defensive argument



- Decision of the Regional Tax Court (2nd level of litigation)
 - First level of litigation favourable to the taxpayer
 - Regional Tax Court upheld the claim of the Italian Tax Authorities based on the following reasons:
 - LuxCo has been established for the sole purpose of avoiding taxation on dividends
 - The Italian Tax Authorities proved that LuxCo was a sham used by the Italian individuals since LuxCo was indirectly controlled by the Italian individuals and they are the beneficial owners of the dividends distributed
 - The Parent-Subsidiary Directive is not applicable because LuxCo's purpose was used to cash dividends and then let them flow to SwissCo whose only purpose was to distribute the dividends to the real beneficial owners with no taxation.

- Increase of tax assessments regarding cross-border structures
 - The focus is on dividends, interest and capital gains
 - Another important field of challenge is transfer pricing
- Arguments used by the Italian Tax Authorities:
 - The foreign company is effectively managed in Italy (Dolce & Gabbana case)
 - The foreign company has a permanent establishment in Italy (especially in private equity structures)
 - The latest trends have been illustrated in Circular Letter No. 6/2016: focus on economic substance of foreign intermediate holding companies. In particular, there is no economic substance if any of the following cases occurs:
 - Light organisational structures with no effective activity and no actual decision power
 - Conduit financial arrangements

- The approach of the Italian Tax Courts
 - General disfavour towards cross-border structures
 - Development of the “abuse of law” doctrine
 - Finance transactions are regarded with higher severity (Italian Supreme Court decision No. 1372/2011)

- Luxembourg
 - Typically a holding jurisdiction
 - Structures without substance are disappearing / issue is to have decision power in Luxembourg
- Netherlands
 - Typically a holding jurisdiction
 - Structures without substance are getting less common / substance needed at holding company level depends to large extent on source countries involved
- Switzerland
 - Corporate perspective: Taxation of SwissCo not affected by Italian measures (effectively tax-free dividend in-flow, dividend out-flow subject to 35% WHT, Italian resident shareholders may reclaim 20%, face 15% residual Swiss WHT)
 - Individuals' perspective (if CH resident):
 - Holding structures based in tax treaty countries usually respected
 - Dividend benefits of reduced income tax (40/50% exemption), if participation is at least 10%
 - Holding structures based in offshore tax havens could be challenged (POEM in CH; look-through only exceptionally, based on general tax avoidance or sham doctrine)

- Litigation vs settlement
 - Italy offers interesting incentives for tax settlements
 - Reduction of penalties
 - Possibility to reduce the amount of taxes requested (further to technical discussion on the legal basis of the claim)
 - Italian Tax Authorities are often happy to settle
 - Netherlands
 - Tax settlement is used in practice and can be effective
 - Switzerland
 - Settlement not excluded, but difficult especially in cases of principle; tax authorities tend to launch "pilot cases" to provoke "leading case" court decisions in their favour, which they can then use on a broad scale
 - Example: "Dividend stripping" cases of two Danish banks, which failed to obtain tax treaty-based refunds of Swiss WHT (Fed. Supreme Court rulings of 5 May 2015)

- Italy - The “tax crime leverage”
 - Tax audits or tax assessments may very easily give rise to a notice of criminal offence to the public prosecutor (except for claims based on the “abuse of law”).
 - Obligation for the Italian Tax Authorities to transmit the notice if certain thresholds of unpaid taxes are exceeded
 - Happened often in case of cross-border structures
 - Two main consequences:
 1. For past years (up to 2015), in case of notice of criminal offence, the terms under the Statute of Limitations are doubled
 2. Incentives to settle
 - In case of tax settlement, criminal penalties are reduced by operation of law.
 - Once tax is settled, the criminal court/public prosecutor may adopt a softer approach

- Switzerland
 - General distinction:
 - Legitimate tax planning/optimization
 - Tax avoidance → recharacterization based on substance over form -> re-assessment of tax, late interest (WHT: 5% p.a.), but: no penalties
 - Tax evasion: Criminal (minor) offense, pursued by Tax Office, gives rise to penalties (1/3rd to 3 times the evaded tax), penalty comes on top of the (evaded) tax and late interest
 - Tax fraud: Serious tax offense/evasion qualified by use of forged/falsified documents or "fraudulent" conduct (indirect taxes including WHT); pursued by criminal prosecutor, sanctions include jail sentence up to 3 years or monetary penalty; comes on top of penalty for the underlying (simple) tax evasion!
 - Punishment for tax evasion and/or tax fraud requires individual culpable conduct, directed towards concealing objectively taxable elements
 - Risk of tax crime (evasion/fraud) is not usually considered in tax planning (but may be in future, due to increasingly aggressive stance of tax authorities upon audits!)

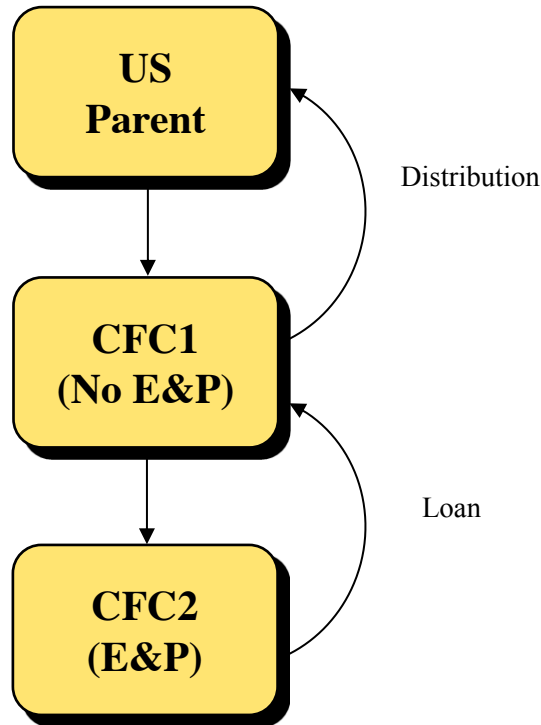
6th Annual IBA Tax Conference

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Sam K. Kaywood, Jr.
Alston & Bird LLP
One Atlantic Center
1201 West Peachtree Street
Atlanta, Georgia 30309-3424
USA
+1 (404) 881-7481
+1 (404) 881-7777
sam.kaywood@alston.com

Basis Repatriation Illinois Tool



Facts

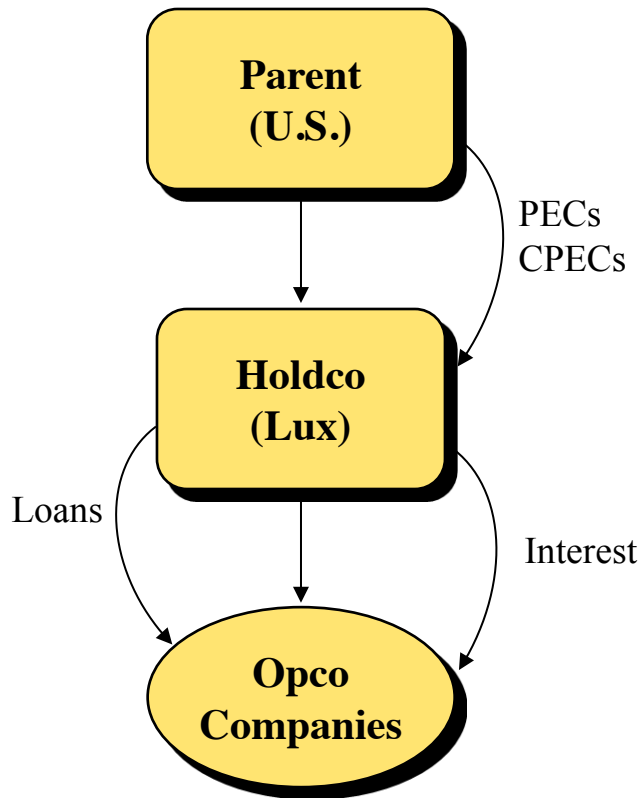
- CFC2 has E&P and lends \$100 to CFC1 which has no E&P.
- CFC1 distributes \$100 as a return of basis.

Results

- Falls within the funding rule – loan is treated as stock, but that does not affect repatriation
- Currently being litigated in Illinois Tool.
- Can use third party debt.

Financing Structures

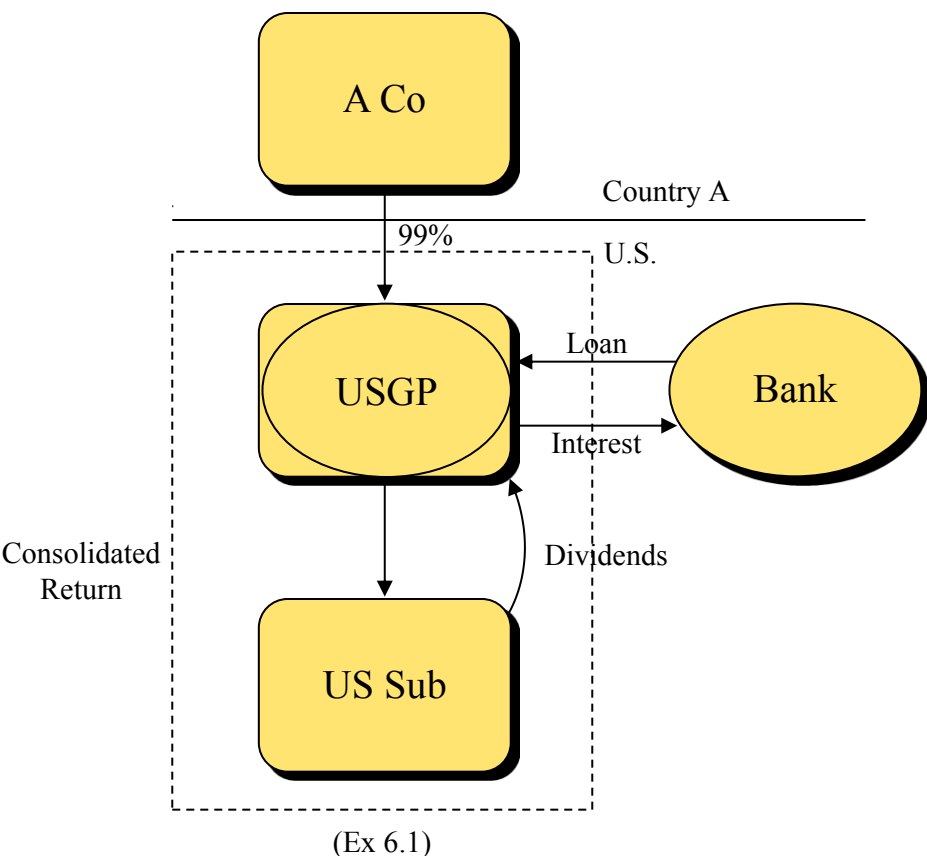
Use of Hybrid Debt



- Lux HoldCo accrues “interest” expense on PECs/CPECs to offset against interest income from Opcos
- Can defer paying interest as long as desired
- When paid, interest can be treated as dividend for U.S. purposes, carrying out foreign tax credits
- APB 23 considerations

Action 2 – Hybrid Entities

Reverse Hybrid – Double Deduction



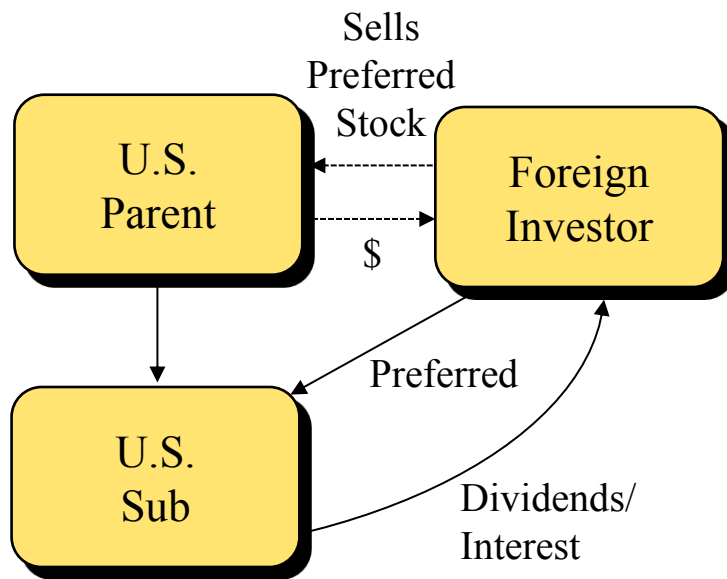
- US General Partnership (USGP) transparent for A purposes but a corporation for US purposes (check-the box).
- A Co deducts interest paid to Bank under consolidated return rules
- A Co also deducts interest on foreign tax return.
- US anti-hybrid rules n/a.

BEPS Recommendation

- **Primary Rule:** Country A should disallow a double deduction.
- **Defensive Rule:** U.S. should disallow deduction if primary rule is not applied.

Action 2 – Hybrid Instruments

Sale/Repo Agreements (D/NI)

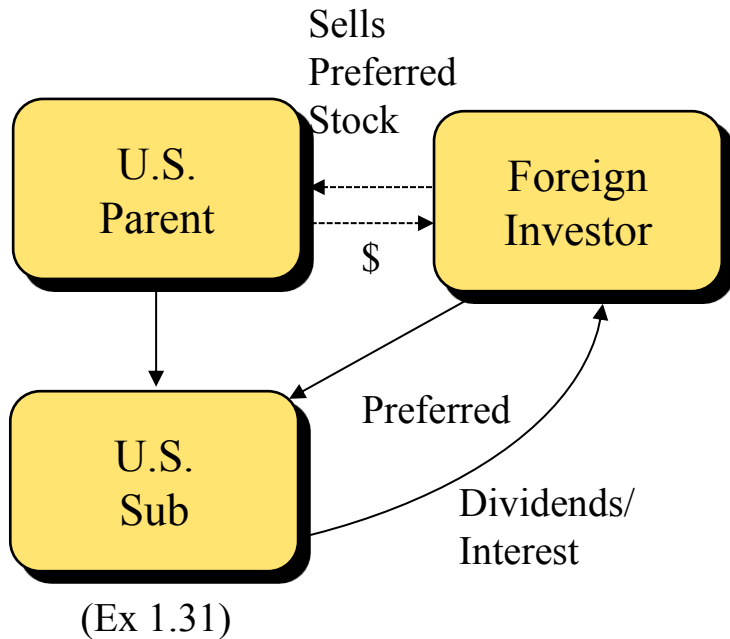


U.S.

- U.S. Parent treated as borrowing money and pledging preferred stock in U.S. sub.
- Dividends paid to Foreign Investor on preferred stock treated as paid to U.S. Parent, followed by U.S. Parent paying interest to Foreign Investor.

Action 2 – Hybrid Instruments

Sale/Repo Agreements (D/NI)



Foreign

- Dividends paid by U.S. Sub to Foreign Investor exempt under participation exemption regime

BEPS Recommendation

- **Primary Rule:** U.S. should deny deduction
- **Defensive Rule:** Investor jurisdiction should deny participation exemption.

New Debt/Equity Regulations

Documentation Requirements

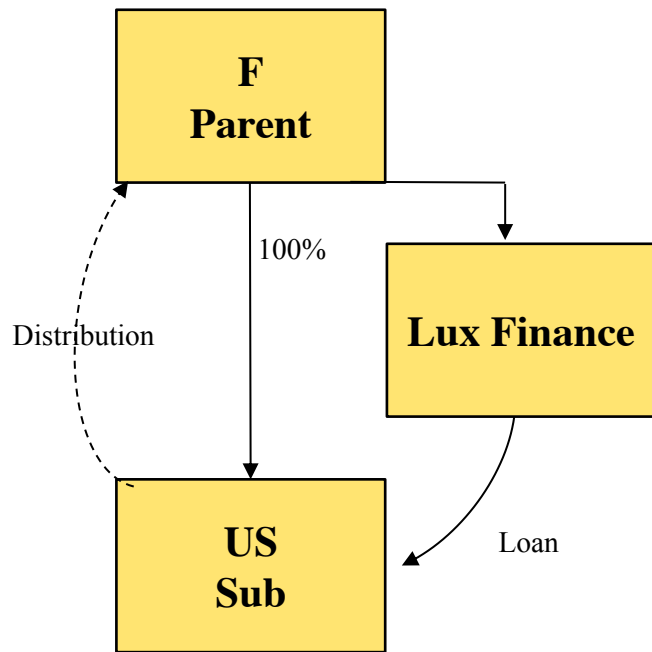
- Written promise to pay, fixed maturity date, etc.
- Must abide by covenants.
- Must enforce payment.
- Ability to repay, documented with projections, financial analysis, etc.

General Rule & Funding Rule

- Distribution of a note.
- Leveraged distributions – 72 month rule.
- Intercompany sale of stock in exchange for a note
- CFC to CFC transactions exempt.

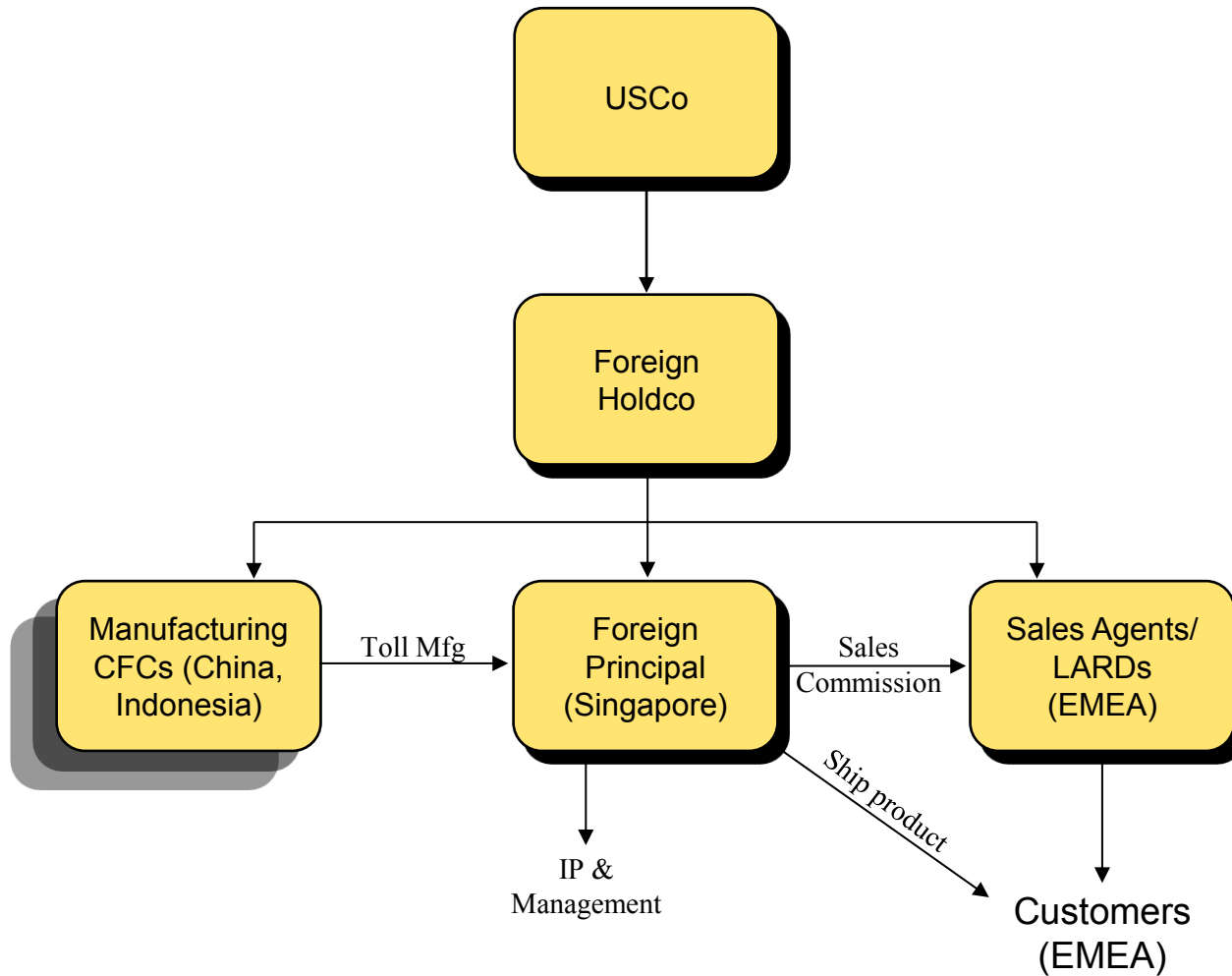
New Debt/Equity Regulations

Leveraged Distributions – Inbound



- This rule attacks loans designed to increase leverage in the U.S. where there isn't an acquisition of new assets
- The loan followed by the distribution is recharacterized as stock under the funding rule
- Per se rule: The loan is tested for distributions that occur 36 months before the date of the loan and 36 months after
- A loan on 2019 could be combined with a distribution in 2017 such that the loan would be treated as stock
- Interest paid would be recharacterized as non-deductible dividends
- 15% withholding likely since treaty voting thresholds not satisfied

Offshore Principal Structure



Offshore Principal – Tax Issues

U.S. Tax Issues

- Foreign Base Company Sales Income
 - Contract manufacturing needs to qualify as “manufacturing” under Reg. §1.954-3(a)(iv)
 - Foreign principal must make “substantial contribution” to manufacturing process
- Foreign Base Company Services Income
 - LRDs sell products in their country of incorporation
- Transfer Pricing
 - Migrating IP to Foreign Principal subject to §367(d), §482, etc.

Foreign Tax Issues

- Foreign principal may have a “permanent establishment” in local markets if LRDs have too much authority as “dependent agents”
- LRD transfer pricing

ALLEN & OVERY

6th Annual IBA Tax Conference



Jean Schaffner

31 January 2017

Context of State aid investigations

Definition of State aid: advantage granted with State resources, which favours certain undertakings or products, and thus distorts competition and affects trade among member States.

Only selective advantages: TPI of 7 November 2014 and ECJ of 21 December 2016 (Autogrill & Santander): the fact that in practice a measure benefits only to certain economic actors (in this case deduction for foreign participations) could potentially make it selective: certain undertakings are favoured.

Link with non-discrimination: conclusions of AG Kokott in Linz case C-66/14

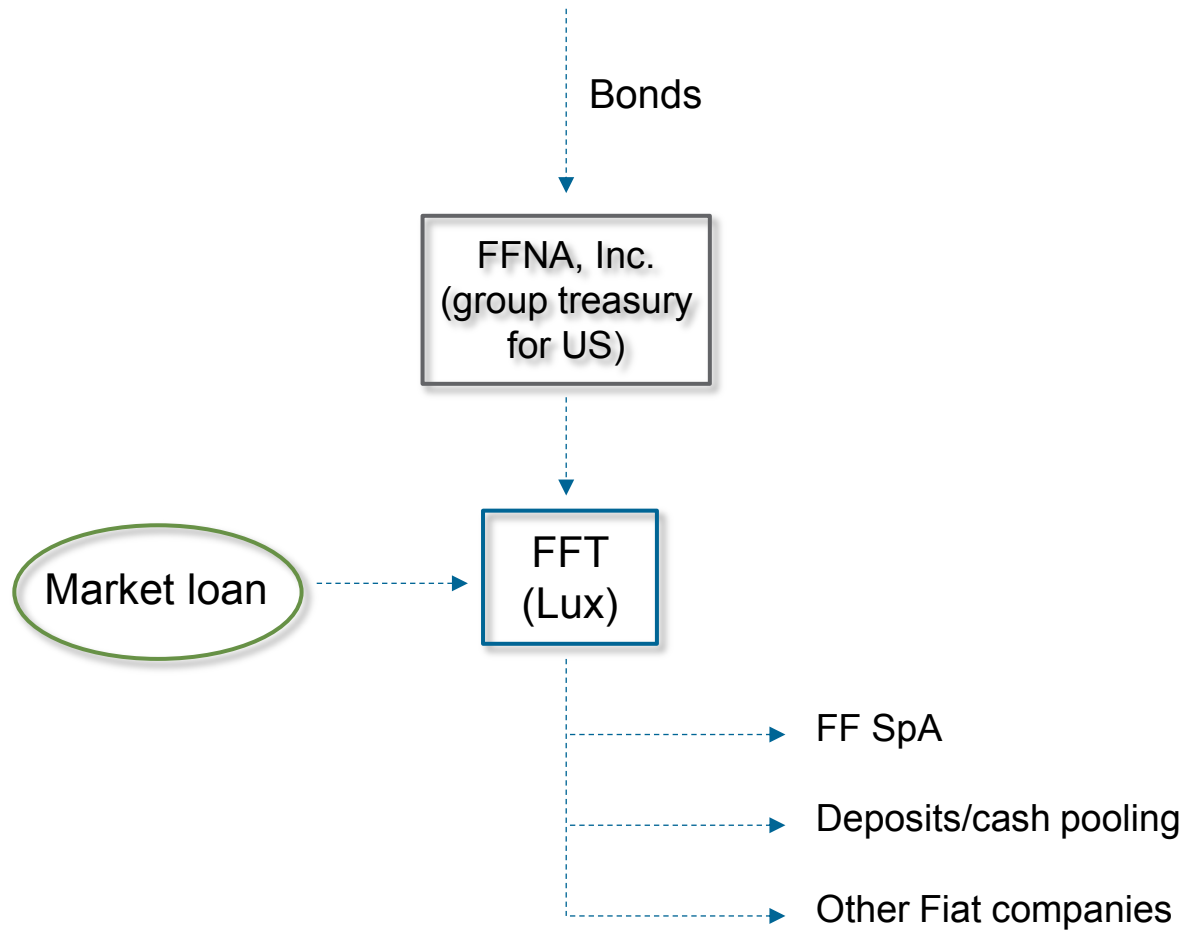
Luxleaks/Formal and informal investigations (more than 20 big household names)

Several cases: FFT/Amazon/McD/Engie /forex neutralisation

Indirect means for tax harmonisation, interference with tax competences of EU Parliament and Council, and fiscal sovereignty.

Solely economic activities

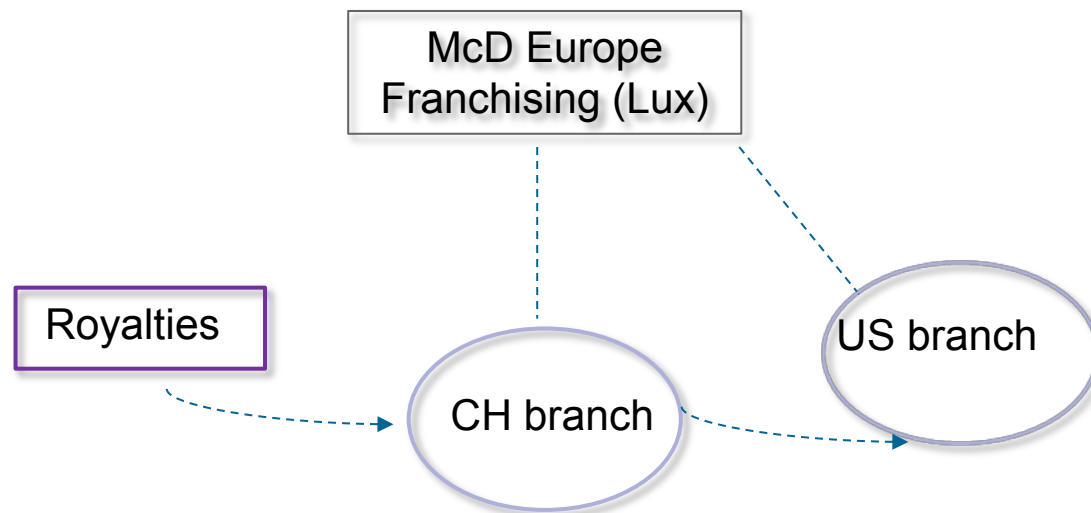
Example: FFT (financing)



Example: FFT (financing)

- ✓ Discussion on TP methodology and equity at risk, on comparables and on the return on equity (parallell with Starbucks)
- ✓ Comparison between the financial sectors and the automotive sector (different credit ratings)
- ✓ Taxable profit not sufficiently related to actual activity
- ✓ Inappropriate credit risk assessment
- ✓ No information regarding profit shift
- ✓ No information regarding the deduction for the counterparties (group as a whole)
- ✓ No precisions regarding the link of tax balance sheet to commercial accounts (« white » income)
- ✓ Selectivity
 - ❖ Group finance companies
 - ❖ Comparison with other rulings
- ✓ Proposed tax reassessment

McDonald's (US branch exemption, applicable DTT)



McDonald's (US branch exemption, applicable DTT)

➤ Luxembourg company with a US permanent establishment

➤ Different tax criteria in the US and in Luxembourg

➤ Luxembourg pure application of DTT :

- 2 subsequent rulings (1 first ruling wrongfully referred to taxation in the US)
- no subject to tax or switch-over clause in DTT
- proposed amendment of treaty (US MC)
- solution similar under OECD MC in other jurisdictions

➤ +/- 25 rulings in Luxleaks based on same conclusions

Outlook

- Rulings are valid if solely interpret law, BUT...
- Rulings for a too long duration or without time limit
- No control of implementation and ongoing monitoring
- New TP rules in Luxembourg; link with BEPS and OECD methods
- No notional methods (such as 1% risk capital)



International Tax Dispute Resolution and the BEPS Multilateral Convention

Jonathan Schwarz

www.taxbarristers.com



BEPS Multilateral Convention

- Scope and interpretation
- Pt II Hybrid mismatches (Action 2) –optional
- Pt III Treaty Abuse (Action 6)
 - Chose LOB or PPT
 - Dividend Transfer Transactions, immoveable property interests, 3rd state PE, own residents - options
- Pt IV PE Avoidance (Action 7)- options
- Pt V Dispute resolution (Action 14)

TEMPLE TAX CHAMBERS

3 TEMPLE GARDENS LONDON EC4Y 9AU





Elements of Minimum Standard

- Article 16 – Mutual Agreement Procedure
Taxpayer may present a case to competent authority of either Contracting Jurisdiction.
- Article 17 - Corresponding Adjustments
incorporated from OECD Model, Article 9(2)
- Reservations that these do not apply because the state intends to apply Action 14 minimum standard



BEPS Action 14 – More Effective Dispute Resolution

- Elements of minimum standard to ensure timely, effective and efficient resolution: Articles 16 and 17
- MAP arbitration Articles: 18 - 26



MAP Arbitration (Part VI)

Article 18 – Choice to Apply Part VI

Article 19 – Mandatory Binding Arbitration

Article 20 – Appointment of Arbitrators

Article 21 – Confidentiality of Arbitration Proceedings

Article 22 – Resolution Prior to Conclusion of Arbitration

Article 23 – Type of Arbitration Process

Article 24 – Agreement on a Different Resolution

Article 25 – Costs of Arbitration Proceedings

Article 26 – Compatibility



Time Limit Extensions

- Optional extension from 2 to 3 years
- Extension until information requested by a CA is provided (plus information process on presentation of case)
- CA suspends MAP because a case with respect to one or more of the same issues is pending before court or administrative tribunal



Let-Outs From Arbitration

Reservations

- Decision on the issue has been rendered by a court or administrative tribunal of either Contracting Jurisdiction
- CA of the Contracting Jurisdictions reach a mutual agreement before arbitrators deliver a decision
- No matching adoption of arbitration type



Binding Arbitration

Arbitrators' decision is binding on the states unless

- Taxpayer does not accept the decision
- Arbitration is held to be invalid
- Taxpayer pursues the issues through the judicial process of the contracting states



Further Information

Jonathan Schwarz:

Schwarz on Tax Treaties (4th Ed)

www.cch.co.uk/content/schwarz-tax-treaties-4th-edn

Blog: Kluwer International Tax

<http://bit.ly/1Dm2hcZ>