

Global Tax Accounting Services Newsletter

*Focusing on tax accounting
issues affecting businesses
today*

October – December 2013



pwc

Introduction

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The Global Tax Accounting Services Newsletter is a quarterly publication from PwC's Global Tax Accounting Services Group. It highlights issues that may be of interest to tax executives, finance directors and financial controllers.

In this release we discuss a variety of accounting and reporting developments and the related tax accounting considerations. We also draw your attention to some significant tax law and tax rate changes occurring during the quarter ended 31 December 2013 and some important tax accounting issues to consider.

For questions related to items discussed in this newsletter, for a comprehensive discussion of tax accounting issues affecting businesses today, or for general tax accounting questions, please contact your local PwC team or the relevant Tax Accounting Services network member listed at the end of this document.

Readers should not rely on the information contained within this newsletter without seeking professional advice. For a thorough summary of developments, please consult with your local PwC team.

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Accounting and reporting update

This section offers insight into the most recent developments in accounting standards, financial reporting, and related matters, along with the tax accounting implications.

Financial Accounting Foundation completes review of accounting for income taxes

Outcome

On 19 November 2013 the Financial Accounting Foundation (FAF) completed its post-implementation review of Financial Accounting Standards Board (FASB) Statement No. 109, Accounting for Income Taxes (FAS 109) (codified in Accounting Standards Codification Topic 740, Income Taxes).

The FAF concluded that FAS 109 adequately achieved its intended purposes, while noting that the complexity associated with accounting for income taxes has not been reduced.

Additionally, the FAF concluded that FAS 109 generally provides investors with decision-useful information, noting, however, that investors struggle to assess cash tax effects and find it difficult to understand the potential tax costs associated with foreign earnings considered to be indefinitely reinvested.

The FAF further indicated that preparers have difficulty with ‘intraperson tax allocation’, accounting for intercompany transfers of assets, and indefinitely reinvested foreign earnings.

The FASB’s response

On 3 December 2013, the FASB subsequently released its response to the FAF’s report, indicating that the FASB will follow-up on areas of concern noted in the report by seeking input from financial statement users, preparers, auditors, and others. The response specified that areas for follow-up include intraperiod tax allocation, intercompany transfers of assets, indefinitely reinvested foreign earnings, and income tax cash flows.

The outreach will seek to identify cost-effective solutions to reduce complexity or provide additional decision-useful information, while also considering stakeholders’ views with respect to the priority of addressing those concerns in light of other FASB projects that may be undertaken.

Accounting and reporting update

Highlights of the 2013 American Institute of CPAs (AICPA) conference

Overview

The 2013 AICPA National Conference on current Securities and Exchange Commission (SEC) and Public Company Accounting Oversight Board (PCAOB) developments held in December 2013 included representatives from regulatory and standard setting bodies, auditors, users, and preparers.

The conference highlighted themes of quality and transparency. Topics of quality included financial reporting and auditing, while transparency was discussed in the context of regulatory practices, audits, and disclosures.

SEC representatives emphasised the need for high-quality, concise disclosures, focusing on ways in which registrants can improve communications through their filings.

The SEC and PCAOB also highlighted the continued importance of internal control over financial reporting.

Frequent areas of SEC comments

SEC representatives provided their annual list of areas of frequent comments from filing reviews. The areas noted included income taxes, pensions and other post-employment benefit disclosures, business combinations, goodwill and segment reporting.

In connection with income taxes, frequent comment areas included disclosures related to income tax rate reconciliations, valuation allowances and indefinite reinvestment assertions (see the tax accounting refresher section below for additional discussion regarding valuation allowances and indefinite reinvestment assertions).

Transparency and disclosures

‘Disclosure overload’ was a theme throughout the conference. Various representatives from the SEC and standard setters reiterated that more information is not always better. Preparers should focus on clear, transparent and understandable disclosures that are both relevant and material. While asking for transparency is often interpreted as requiring additional information, good disclosures should be clear and crisp, and written in plain language to effectively reach the financial statement users.

Standard setting update

Representatives of the FASB and International Accounting Standards Board (IASB) discussed current and future standard setting, providing updates on both convergence and individual standard setting projects.

While there was some detailed discussion regarding the convergence projects, there was little discussion about International Financial Reporting Standards (IFRS) becoming an accepted accounting framework for companies regulated by the SEC. This year the topic received significantly less attention than last year’s conference, when it was a frequent and recurring theme.

FASB and IASB provided updates regarding the status of four active convergence projects: revenue recognition, leases, financial instruments (classification and measurement), and insurance contracts.

Although the revenue standard is nearing completion, significant work remains on the leases project. The feedback received regarding the leasing project suggests that many preparers believe the costs of implementation will significantly outweigh the related benefits.

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There was general agreement on the objectives of the classification and measurement of financial instruments project (ie to reduce complexity, provide more decision-useful information, and achieve convergence); however, many do not believe that the current exposure draft adequately achieves those objectives.

Revenue recognition

The revenue recognition project is the furthest along of the joint projects, with a final standard expected before the end of 2014. Once completed, it will impact many industries resulting in either more complex deferred tax calculations or, in some cases an impact on cash taxes.

The conference highlighted concerns about the effort that will be required for the full retrospective and modified retrospective adoption alternatives, as well as the volume of expected incremental disclosures.

Additional disclosures about the disaggregation of revenue, significant judgments made in applying the standard, and changes in contract assets related to costs to obtain or fulfil a contract will add to the burden of adoption. However, the new disclosure requirements are somewhat reduced for non-public entities and interim reporting as compared to what public companies should expect for annual reporting requirements.

There was broad agreement that preparers will need to expend significant effort and resources to understand the new standard and implement process and system changes well in advance of the expected 2017 effective date. Registrants will also need to consider appropriate disclosures related to the expected impact of the standard in the periods after its issuance but before its adoption.

As mentioned above, the final standard is expected to be released during 2014. As such, 2015 would mark the beginning of the comparative periods required to be retrospectively revised in a typical three-year financial statement presentation (ie for most companies filing under US GAAP, the 2017 Form 10-K will show 2017, 2016, and 2015 statements of operations). However, the SEC has yet to determine the manner in which retrospective adoption of the new revenue standard will be treated in the five-year selected financial data table required by Regulation S-K, Item 301.

PCAOB update

PCAOB Chairman James Doty highlighted that the PCAOB continues to examine the role the audit can and should play in enhancing capital formation, investor protection and the economy.

Quality control continues to be at the forefront for the PCAOB. For audit firms, a system of quality control is broadly defined as a process to provide the firm with reasonable assurance that its personnel comply with applicable professional standards and the firm's standards of quality. The PCAOB believes that improvements in the systems of quality control could prevent and detect audit deficiencies and improve audit quality.

Other near- and long-term agenda items include continued outreach to audit committees, identification and tracking of audit quality measures, and focus on inspections and remediation processes, as well as standard-setting initiatives.

Internal control over financial reporting

Internal control over financial reporting continued to be an important theme at the conference, discussed by representatives from both the SEC and PCAOB. It was commented that investors benefited from improvements in the reliability of financial reporting due to the increased focus on internal control.

Accounting and reporting update

To maintain the improvements achieved to date, a continued focus on the internal control over financial reporting is required. Maintaining and evaluating internal control over financial reporting must be an iterative and ongoing process that receives the appropriate level of involvement and support from management.

The SEC noted that as part of their comment letter process, they are also looking for potential indicators of material weaknesses, such as corrections of an error or disclosures regarding material changes in internal controls. They further noted that in instances where the SEC does not agree with a registrant's conclusion on an accounting matter, they may also be interested in a registrant's conclusions regarding the internal control implications.

Takeaway

The above themes of financial reporting and auditing quality, and transparency of regulatory practices, audits, and disclosures are expected to be the key focus areas of the SEC and PCAOB during 2014. Tax accounting matters will also remain high on the agenda as taxes are one of the most common areas of material weakness.

Accounting and reporting update

Country-by-country reporting

In prior 2013 issues of this newsletter we touched on various aspects of tax transparency and country-by-country reporting (CBCR).

In this issue we will give a brief overview of the current CBCR regulations, proposals to extend CBCR to all large companies and groups in Europe and their current status, as well as initiatives from the Organisation for Economic Co-operation and Development (OECD) related to CBCR and their timing.

Overview of the current reporting regulations

Currently there are four CBCR frameworks that are effective or in the process of being implemented:

- Extractive Industries Transparency Initiative (EITI)
- Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act)
- European Union (EU) Accounting and Transparency Directives
- EU Capital Requirements Directive IV (CRD IV)

The EITI applies to companies in the extractive sector ie companies extracting natural resources, including oil, gas, metals, and minerals.

The EITI was originally established in 2003, and then substantially revised in a new standard in May 2013. More than 20 countries are already fully compliant with the requirements of the EITI, with the United Kingdom, United States, and Italy seeking to become compliant in the near future.

Similar to the EITI, the Dodd-Frank Act also applies to companies in the extractive sector. The rules were implemented by the SEC on 22 August 2012, but were successfully challenged in court on 2 July 2013. Therefore, the country-by-country disclosures in the Dodd-Frank Act are currently suspended until the SEC introduces revised rules. There has been no announcement as to when the SEC expects the new rules to be ready, and no timeline has been given for their implementation.

The EU Accounting and Transparency Directives apply to listed and large unlisted EU companies in the extractive sector and those engaged in the logging of primary forests (we discussed these directives in the second-quarter 2013 issue of the newsletter). Each EU member state is now responsible for passing the requirements under these directives into local legislation by 20 July 2015. The directives provide that the requirements will come into effect for financial years beginning on or after 1 January 2016 at the latest.

CRD IV applies to EU banks, other credit institutions and certain investment entities (please refer to the second-quarter 2013 issue of the newsletter for more detail on this directive). The directive is intended to be effective from 1 January 2014 and is being adopted by the EU member states into their local legislation.

Proposals to extend CBCR to large companies and groups

Proposals to extend CBCR to large companies and groups via amendments to the draft directive on non-financial and diversity information emerged in Europe in 2013. The draft directive amends the accounting directives mentioned above and aims at increasing EU companies' transparency and performance on environmental and social matters in order to contribute effectively to long-term economic growth and employment.

These proposals were considered by three EU institutions, namely, Parliament, Council, and Commission, with the Parliament and Council working as EU co-legislators.

In December 2013 the EU Parliament's Legal Affairs Committee (the JURI) decided not to adopt recommendations of the Economic and Monetary Affairs Committee (ECON) in relation to the extension of CBCR to large companies and groups.

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Additionally, a number of the member states in the Council also indicated that they do not support this proposal.

As a result, at this point any future discussion regarding the introduction of CBCR for large companies and groups is effectively postponed until after the directive on disclosure of non-financial and diversity information becomes effective in 2018. However, there is a chance that the EU Parliament, the Council, and the European Commission may bring forward this discussion, as well as consider the alignment of any CBCR initiatives with the OECD's Base Erosion and Profit Shifting (BEPS) project (see below).

OECD's initiatives and timeline

In July 2013, at the request of G20 Finance Ministers, the OECD launched an Action Plan on BEPS that was later fully endorsed by G20 Heads of State at their September 2013 meeting in Saint-Petersburg.

Among other areas, the plan outlined specific actions focused on greater transparency and data and reporting requirements including CBCR to tax authorities.

The timeline of the BEPS project, including CBCR, is extremely ambitious with the first deliverables expected by September 2014 and completion of the project expected by the end of 2015.

In the 2013 third-quarter issue of the newsletter, we discussed the draft memorandum on transfer pricing and CBCR released by the OECD on 3 October 2013 and the subsequent public consultation held by the OECD on 12 and 13 November 2013.

On 3 December 2013, the OECD released a calendar for planned stakeholder input on the BEPS project, including CBCR. The calendar provides a tentative timeline for the release of discussion drafts, deadlines for comments, and public consultations.

In accordance with the timeline, the OECD published a discussion draft on transfer pricing documentation and a template for CBCR on 30 January 2014. The public consultation on these documents is scheduled to take place in March 2014. It should be noted that the deadline for public comments is 23 February 2014, which represents an extremely tight timeframe.

During the webcast on the BEPS action plan on 23 January 2014, the OECD confirmed that the BEPS project is continuing on schedule, consistent with the timeline above.

Takeaway

While the EU proposals addressing the possibility of extending CBCR to all large companies and groups are on hold, the OECD is maintaining momentum as part of the BEPS project. The OECD's specific request for comments, along with corresponding dates for public consultations, has been well received, as the OECD has opened a dialogue with the tax community regarding the BEPS project. Nonetheless, given the short timeline proposed by the OECD, companies with a viewpoint on the draft CBCR template should consider potential feedback now.

Given this timeline, it is also worthwhile to connect with your PwC contacts to consider processes and technology that could be used in relation to the country-by-country data collection and start forming strategies for dealing with the additional compliance and relevant audit requirements.

Accounting and reporting update

European Commission amendments to Parent Subsidiary Directive

On 25 November 2013, the European Commission proposed amendments (2011/96/EU) to the Parent Subsidiary Directive. The historical goal of the Parent Subsidiary Directive has been to prevent the double taxation of group companies based in different EU member states.

The proposed amendments follow the political guidance which was determined in 2009 within the EU's Code of Conduct Group. The group agreed to address mismatches resulting from differences in the tax treatment of hybrid loans between EU member states.

The European Commission also proposed replacing the current anti-abuse provision in the directive with a common general anti-abuse rule based on a similar clause included in its 6 December 2012 recommendation on aggressive tax planning.

The main proposed amendments are as follows:

- The directive will permit the use of domestic or agreement-based rules regarding tax evasion.
- EU member states will withdraw the benefit of the directive in the case of an artificial arrangement put into place with the essential purpose of obtaining an improper tax advantage under the directive if it defeats the object, spirit, and purpose of the tax provisions.
- A transaction, scheme, action, operation, agreement, understanding, promise, or undertaking will be an artificial arrangement or a part of an artificial series of arrangements where it does not reflect economic reality.
- In determining whether an arrangement is artificial, EU member states will consider the following:
 - Whether the legal characterisation of the individual steps of an arrangement is consistent with the legal substance of the arrangement as a whole
 - Whether the arrangement is carried out in a fashion not ordinarily used in a reasonable business manner
 - Whether the arrangement includes elements having the effect of offsetting or cancelling each other
 - Whether the transactions involved in the arrangement are circular in nature
 - Whether the arrangement results in a significant tax benefit which is not reflected in the business risks undertaken by the taxpayer or its cash flows.

If the proposed amendments are implemented, the member states will be required to adopt the amended directive in their local laws, regulations, and administrative provisions by 31 December 2014.

Recent and upcoming major tax law changes

This section focuses on major changes in the tax law that may be of interest to multinational companies. It is intended to increase readers' awareness of the main global tax law changes during the quarter, but does not offer a comprehensive list of tax law changes for all countries.

Some enacted tax rate changes

Country	Prior rate	New rate
Finland (CIT)	24.5%	20% ¹
France (CIT)	33.33%-36.10%	maximum 38% ²
Italy (CIT)	27.5%	36% ³
Norway (CIT)	28%	27% ⁴
Norway (petroleum special tax)	50%	51% ⁴
Portugal (CIT)	25%	23% ⁵
Portugal (CIT – state surcharge)	3%/5%	3%/5%/7% ⁵
Slovakia (CIT)	23%	22% ⁶
Ukraine (CIT)	19%	18%/17%/16% ⁷
Uzbekistan (CIT)	9%	8% ⁸

¹ This change was enacted on 30 December 2013 and is effective from 1 January 2014

² The temporary 5% exceptional surcharge on corporate income tax (CIT) was increased from 5% to 10.7%, leading to a maximum CIT rate of 38%. This change was enacted on 30 December 2013 and is effective for tax years ending between 31 December 2013 and 30 December 2015 (in practice only 2013 and 2014 years will be affected)

³ This change is applicable to banks, insurance companies and financial entities. It was enacted on 30 November 2013 and is effective from the 2013 income period

⁴ These changes were enacted on 5 December 2013 and are effective from 1 January 2014

⁵ These changes were substantively enacted on 26 December 2013 and are effective from 1 January 2014

⁶ This change was enacted on 30 December 2013 and is effective from 1 January 2014

⁷ These changes were enacted on 28 December 2013 and are effective as follows:

- 18% - from 1 January 2014
- 17% - from 1 January 2015
- 16% - from 1 January 2016

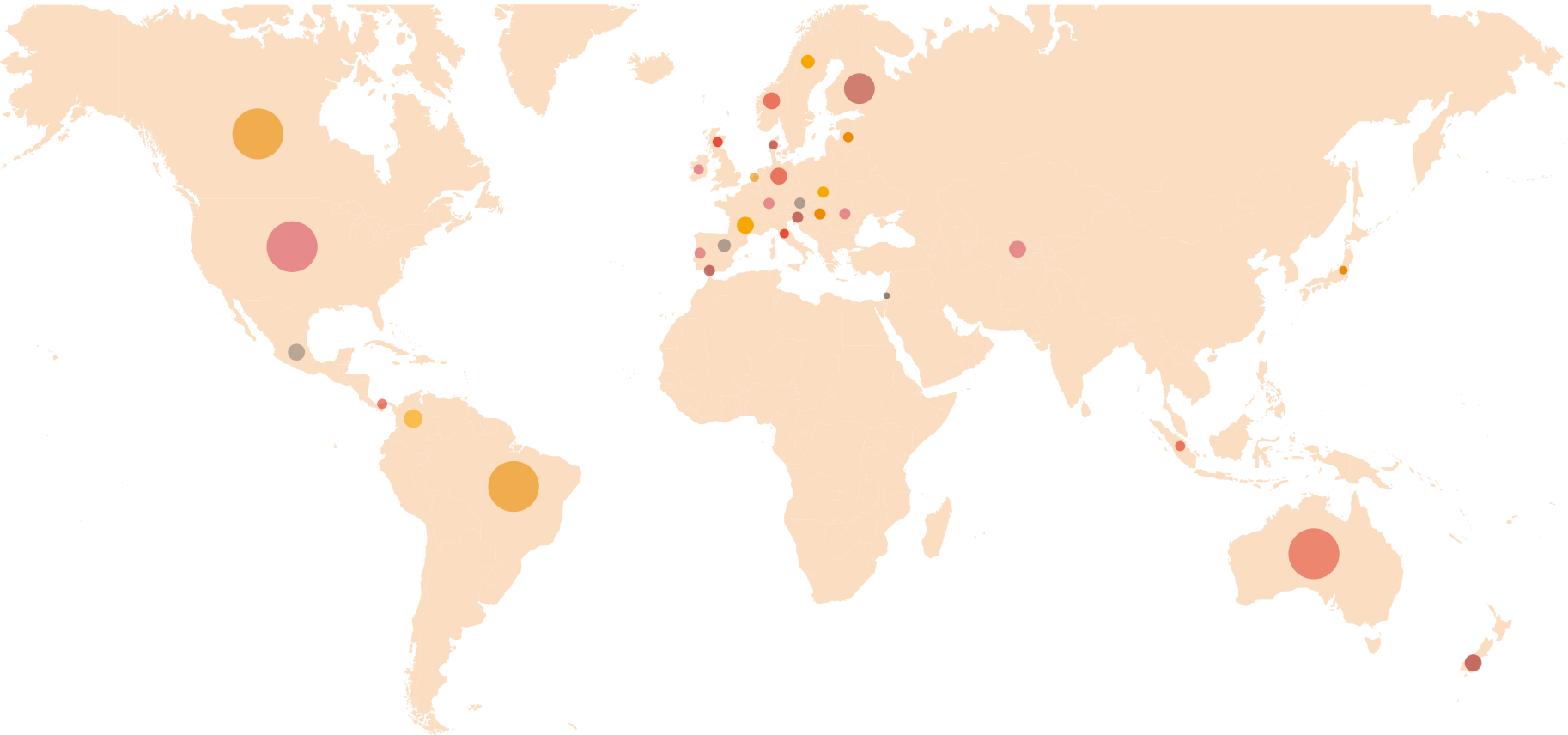
⁸ This change was enacted on 25 December 2013 and is effective from 1 January 2014



Recent and upcoming major tax law changes

Other important considerations in tax law changes

Click each circle to review



Recent and upcoming major tax law changes

Australia

During the fourth quarter of 2013 the new Australian government released its response to previously announced but unlegislated tax measures. In particular, the government will proceed with the following measures:

- Proposal to amend the thin capitalisation rules to reduce the debt-to-equity safe harbour limit from 75% to 60%.
- Proposal to remove the research and development (R&D) concession for large companies with income of AUD 20 billion or more. The R&D concession is currently the Australian government's principal incentive to companies undertaking R&D in Australia.
- Proposal to repeal the loss carry back measures enacted on 28 June 2013 with effect from the 2013–2014 income year.

The new government also announced it will not proceed with the proposal to remove the debt deduction for funding offshore subsidiaries, but will consider an alternative anti-avoidance measure.

Austria

The following proposals were introduced in the fourth quarter of 2013 in Austria:

- Interest payments made to financing companies located in low-tax and offshore jurisdictions will not be deductible.
- The limitation on the use of carry forward losses (currently set at 75% of annual profits) will be abolished.
- Utilisation of foreign tax losses will be limited to 75% of Austrian taxable income.
- Formation of an Austrian tax group between Austrian companies and their foreign group companies will be restricted to companies from EU/EEA and some treaty jurisdictions.
- Goodwill amortisation will be abolished.
- Deductibility of staff provisions will be effectively increased via a reduction in the discount rate applied in calculating staff provisions for income tax purposes.

- Deduction for individual employee salary will be capped at EUR 500,000 per year.
- 'Golden handshakes' (generally, special severance payments made to employees in connection with an early retirement) paid to employees will no longer be deductible (with very limited exceptions).

Brazil

The following measures were enacted during the fourth quarter of 2013 in Brazil:

- Dividends on profits derived between 1 January 2008 and 31 December 2013, and effectively paid before 12 November 2013, will not be subject to withholding tax. For the same period, interest on net equity may be calculated based on the corporate equity.
- New tax rules were adopted which addressed the determination and amortisation of goodwill.
- Gains arising from the fair value revaluation

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of assets or liabilities will be taxed only when realised.

rate for pre-production mine development expenses was reduced.

a place of effective management were amended or clarified.

Canada

The following measures, as we reported in the previous issue of the newsletter, were enacted in Canada during the fourth quarter of 2013:

- The thin capitalisation rules were extended to Canadian resident trusts and to non-resident corporations and trusts that operate in Canada.
- An anti-avoidance measure was introduced which supported restrictions on the deductibility of losses and the use of certain other tax benefits, after certain share acquisition transactions.
- Certain tax benefits relating to two leveraged life insurance arrangements known as 'leveraged insured annuities' and '10/8 arrangements' were eliminated.
- The accelerated capital cost allowance for capital assets used in new mines and certain mine expansions was phased out and the deduction

Colombia

The following measures were enacted during the fourth quarter of 2013 in Colombia:

- Colombia introduced a list of 41 jurisdictions which were considered 'tax havens' under domestic law. From 1 January 2014, all companies that carry out operations with related or unrelated parties located in a 'tax haven' must comply with arm's length principles and support their operations with necessary transfer pricing documentation.
- Payments made to a 'tax haven' will be subject to a withholding tax of 33%, which would not be deductible until paid.
- The new withholding tax rate applicable to payments other than dividends, royalties, and interest was reduced from 3.5% to 2.5% as of 1 January 2014.
- Permanent establishment rules, thin capitalisation rules, and rules which determine

Denmark

The following proposals were introduced during the fourth quarter of 2013 in Denmark:

- Refund of value of tax losses arising from research and development activities, currently available starting from the 2015 assessment year, will also be available for the 2014 assessment year.
- An exit charge arising on the transfer of assets to a foreign permanent establishment or foreign headquarters (domiciled in EU/EEA) could be payable over a period of up to seven years.

Finland

The following measures were enacted during the fourth quarter of 2013 in Finland:

- Deduction for interest paid to related parties will be limited to 25% of taxable EBITDA (instead of previous 30%).
- Entertainment costs will no longer be deductible (previously 50% deductible).
- Deduction for training expenses will be limited

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to 1.5% of annual salary costs, based on a maximum of three training days per employee.

- R&D incentive will be limited to the 2013–2014 tax years only (originally 2013–2015).
- Accelerated depreciation on production investments will be limited to the 2013–2014 tax years only (originally 2013–2015).

France

The following measures were enacted during the fourth quarter of 2013:

- New anti-tax fraud provisions were introduced.
- Simplified transfer pricing documentation will be allowed if provided within six months following the filing of the tax return.
- A 50% tax will be payable in 2013 and 2014 years for individual gross remuneration in excess of EUR 1 million.
- Interest deductions will only be allowed if the French borrower demonstrates that for the current financial year the lender is subject to income tax of at least 25% (see the 2013 third-quarter issue of the newsletter).

Germany

During the fourth quarter of 2013 Germany substantively enacted the following measure:

- Losses from the transfer of certain accruals subject to special tax valuation rules eg pensions, early retirement, contingent liabilities are deductible by the seller over a period of 15 years.
- The buyer has to adjust the fair value of the transferred accruals and consider the special tax valuation rules. Any arising profit can be spread over 15 years.

Gibraltar

Royalties that have been received or are receivable by a Gibraltar company will be taxable at 10%. This measure was enacted in Gibraltar during the fourth quarter of 2013.

Hungary

During the fourth quarter of 2013 the following measures were enacted in Hungary:

- In the case of reported shareholdings, the minimum shareholding requirement decreased to 10% and the reporting deadline will be extended to 75 days.

- Related party taxpayers may split the deduction of R&D costs between each other in an agreed proportion, if certain requirements are met.
- The definition of a real estate holding company has changed in that the proportion of the assets/real estate held by the company must be calculated based on book values as opposed to market values.

Ireland

The following measures were enacted during the fourth quarter of 2013 in Ireland:

- Modifications were made to the calculation of the research and development credit. The limit for subcontracted research and development costs was increased from 10% to 15% of the qualifying spend.
- Modifications were made to certain double-tax relief provisions and corporate tax residency rules.
- The payment of any exit tax arising from the migration of a tax residency of an Irish company may be deferred.

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- The group relief was modified to allow a group to be formed between a parent company that is not a resident of the EU or a country with which Ireland has a Double Tax Agreement and its 75%-owned subsidiaries. The modified rules require the parent company to be quoted on certain stock exchanges.
- Restrictions on the use of carried forward trading losses will be removed for banks that transferred assets to the National Asset Management Agency.
- Relief will be provided for the carry forward of excess foreign tax credits related to lease rental income received by Irish trading entities.

Israel

During the fourth quarter of 2013 Israel enacted the following measures:

- Changes to conditions for certain tax benefits (e.g., entitlement to a reduced tax rate). This measure is retroactive and applies from 1 January 2012.
- Significant changes to the controlled foreign corporation (CFC) regime, including changes to the definitions of a CFC, and passive income, as well as repeal of the deemed credit mechanism.

Italy

The following measures were enacted during the fourth quarter of 2013 in Italy:

- Percentage of notional interest deduction on qualifying new equity (ie the increase in equity over a 2010 base amount) was increased to 4% for tax years that include 31 December 2014, 4.5% for tax years that include 31 December 2015 and 4.75% for tax years that include 31 December 2016. In subsequent years the notional interest deduction percentage will be determined annually by the Ministry of Finance.
- Taxpayers will be able to deduct the 20% municipal tax on real estate starting with the 2013 income year.
- Certain entities may elect to step up the value of certain assets, intangible and equity investments in controlled or connected companies (for both accounting and tax purposes) by paying a substitutive tax.
- Companies increasing the number of employees on long-term contracts will be able to deduct up to EUR 15,000 for each employee for the year in which the employee is hired, as well as the following two years.

Various new measures have been proposed for advance payments payable by taxpayers in financial and insurance business sectors.

Japan

During the fourth quarter of 2013, the Japanese government tabled a proposal for significant tax reform, which will be considered further by the Diet (Japanese parliament) in early 2014. The tax reform package includes the following significant measures:

- The Restoration Corporation Surtax will be terminated one year early (ie from 1 April 2014).
- An incentive (ie special depreciation or a tax credit) for investments in National Strategic Special Areas will be introduced.
- The applicable period for the investment incentive for International Strategic Areas (to assist in rebuilding efforts from the Tohoku earthquake and tsunami and encourage foreign corporate investment into Japan) will be extended.
- The employment promotion incentive will be extended for another two years.
- A 50% deduction for certain entertainment expenses incurred by large corporations will be allowed.

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- Temporary surtax measures on undisclosed expenditures by corporate taxpayers will be amended to become permanent.
- Temporary suspension of the tax loss carry-back will be extended for another two years (small and medium enterprises excluded).
- Temporary suspension of taxation of retirement pension funds will be extended for another three years.
- The Authorised OECD Approach (generally referred to as the functionally separate entity approach) for calculating profits attributed to a permanent establishment in Japan will be adopted.
- Provision of services between certain unrelated parties will be included in the scope of the transfer pricing regime.
- The inhabitants corporate tax rate will be reduced.
- A new local corporate tax at a fixed rate of 4.4% will be introduced. This tax will be earmarked to a special government reserve for allocation to local governments in financial distress.

Latvia

The following measures were enacted during the fourth quarter of 2013 in Latvia:

- Gains on the disposal of real estate in Latvia by a non-resident will be subject to tax at 15%.
- Tax relief allowing application of a 1.5 factor to the cost of new plant and equipment for capital allowance purposes will be extended to 2020. Tax relief for investments made in qualifying investment projects exceeding EUR 10 million will also be extended.
- Tax relief encouraging research and development will be introduced from 1 July 2014.
- Deemed interest relief and group tax loss relief will be cancelled.
- All dividends paid to tax havens will be subject to a 15% or 30% withholding tax. All interest and royalties paid to tax havens will be subject to a 15% withholding tax.

Mexico

During the fourth quarter of 2013 Mexico enacted the 2014 Mexican tax reform package we covered in the 2013 third quarter newsletter.

In summary, the tax reform package repealed the current income tax law, including the flax tax regime and tax consolidation. It introduced changes to the corporate income tax rate and an additional 10% tax on dividends paid by Mexican entities. It also made modifications to various deductions and the maquiladora regime (regime favouring establishment of foreign owned companies to process and / or assemble temporarily imported materials and parts for re-export).

Netherlands

Further guidance was released in the Netherlands in the fourth quarter of 2013 regarding the application of the arm's length principle. The guidance highlights the importance of arm's length terms and conditions and the economic rationale underlying an inter-company arrangement. The guidance also includes specific situations that have led to controversies and audit activities over the past decade.

Netherlands also enacted measures to increase the additional research and development (R&D) deduction to 60% (previously 54%) of the costs (other than wages) directly related to R&D activities.

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New Zealand

The following measure was enacted during the fourth quarter of 2013 in New Zealand:

- A mismatch in the income tax treatment for a person who enters into a foreign currency hedge on assets subject to the Fund Fair Dividend Rate was eliminated.

The following proposal was also introduced during the above period:

- Hedge accounting treatment will be applied on the sale and purchase of properties in foreign currency. This should eliminate forex fluctuations arising under the current rules.

Norway

The following measures were enacted during the fourth quarter of 2013 in Norway that we covered in the 2013 second quarter issue of the newsletter:

- Deduction for interest on intercompany debt will be limited to 25% of taxable income in the relevant year (subject to certain adjustments).
- Deduction for uplift in the petroleum special tax will be limited to 5.5% annually for four years (previously 7.5%).

Panama

On 30 December 2013, Panama introduced a worldwide income tax system effective 31 December 2013. Under the new system Panamanian taxation was to apply to Panamanian residents on any income derived from sources in or outside of Panama.

- However, following strong criticism of the new law, on 10 January 2014, the new system was repealed retroactively.
- As a result of the repealing law being effective retroactively to 31 December 2013, the worldwide tax system is deemed never to have applied for Panamanian tax purposes. Companies should ensure that they have addressed any financial accounting and disclosure implications of the enactment and subsequent repeal for the relevant reporting periods.

Portugal

The following measures were substantively enacted during the fourth quarter of 2013 in Portugal:

- The nominal tax rate will be reduced and the state and municipal surcharges will be abolished.

- The tax loss carry forward period will be extended to 12 years (previously five years).
- Participation exemption will be granted for dividends received from qualified shareholdings of at least 5%, including from countries outside of the EU, subject to anti-avoidance limitations.
- Dividends paid to non-resident shareholders, including residents outside the EU, with at least a 5% stake (previously 10%), will not be subject to withholding tax.
- Capital gains arising on the disposal of shares held for a minimum of 12 months, regardless of the percentage held, will not be taxed.
- Transfer of tax residency from Portugal to other EU or EEA country will be subject to an exit tax, which may be deferred.

In addition, the 2014 Federal Budget enacted in the fourth quarter of 2013 introduced a 10% deduction for retained earnings reinvested by small and medium companies in eligible assets. The deduction is limited to 25% of the corporate income tax liability for the year.

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Romania

In the fourth quarter of 2013 Romania enacted legislation introducing a participation exemption regime for Romanian holding companies. Under this regime, qualifying income eg dividends, capital gains, and liquidation proceeds will not be taxable in Romania.

Singapore

The following measures were enacted during the fourth quarter of 2013 in Singapore:

- A 30% corporate income tax rebate (capped at S\$30,000 per year of assessment) will be available for the 2012 to 2014 tax years.
- Enhancements were made to the Productivity & Innovation Credit (PIC) Scheme.
- Changes were made to the taxation of maritime and financial services sectors.

Slovakia

The following measures were enacted during the fourth quarter of 2013 in Slovakia:

- Capital gain from the sale of shares in Slovakian companies will be taxed in certain circumstances.
- The tax loss utilisation period will be reduced from seven to four years (this change applies retrospectively).

Slovenia

The following thin capitalisation measures were enacted during the fourth quarter of 2013 in Slovenia:

- The definition of related persons who fall under the thin capitalisation rule was extended, in particular, to include sister companies.
- Calculation of average capital was simplified and harmonised with the accounting standards and Companies Act.

Spain

The following measures were enacted during the fourth quarter of 2013 in Spain:

- Temporary measures adopted in 2012 will be extended to 2014 and 2015. The measures include the minimum 12% instalment payment by companies with a turnover in excess of EUR 20 million, the limitation of the tax losses offset and limitation of goodwill amortisation.
- Loss duplication rules will apply on the disposal of a subsidiary of a consolidated group.
- Substantial changes to tax rules were made to conform Spanish law with European legislation regarding the supervision and solvency of financial institutions.
- Spanish law was also amended to adapt European guidance relating to an exit tax arising on the change of tax residency of a Spanish company to another EU state, or transfer of assets of a Spanish permanent establishment to another EU state.

Recent and upcoming major tax law changes

Switzerland

During the fourth quarter of 2013 corporate tax reform was proposed in Switzerland, including introduction of an innovation box regime and a notional interest deduction.

Sweden

During the fourth quarter of 2013 research and development relief in Sweden has been amended to reduce a deduction for employer's contributions for foreign key employees engaged in qualified research or development activities. A deduction is now 10%, capped at SEK 230,000 per month for the group.

United Kingdom

The following proposals were introduced during the fourth quarter of 2013 in the United Kingdom (UK):

- Changes will be made to the grouping rules for the UK debt capitalisation rules.
- Restrictions for utilisation of trading losses due to changes in corporate ownership will be relaxed.
- Significant changes will be made to rules for taxing loans and derivatives.

United States

A number of widely relevant US tax law provisions affecting businesses expired on 31 December 2013. That includes the research and development tax credit, work opportunity tax credit, increased expensing and bonus depreciation allowances, and certain favourable 'subpart F' provisions (ie the look-through treatment on payments between related controlled foreign corporations and exceptions for certain active financing income).

Tax accounting considerations

Accounting Standards Codification (ASC) Topic 740, Income Taxes, requires companies to measure current and deferred income taxes based upon the tax laws that are enacted as of the balance sheet date of the relevant reporting period.

With respect to deferred tax assets and liabilities, that means measurement is based upon the enacted law for the period in which the temporary differences are expected to be realised or settled. Expired tax laws are not considered, nor would they be in statements prepared under IFRS.

Accordingly, some of the more significant effects that should be considered with respect to these expired tax laws include the following:

- In calculating the annual estimated tax rate to be used for interim reporting purposes, benefits such as the research tax credit will no longer be included. The effective tax rate could also be increased if there is a significant effect related to the expired 'subpart F' provisions.
- If the effective tax rate for future periods is expected to be substantially different from the current effective tax rate, disclosure in management's discussion and analysis within SEC filings should be considered. Disclosure of significant potential effects on cash flows or liquidity should also be considered. Because many of these expired provisions have previously been retroactively reinstated, it may be appropriate to offer some forward-looking disclosure inclusive, of course, of the uncertainty with respect to the legislative environment.
- The expiration of the favourable subpart F provisions, applicable to foreign corporations with tax years beginning after 31 December 2013, should be considered in evaluating an indefinite reinvestment assertion. The expiration could result in potential subpart F inclusions that would arise from cross-border dividend (or certain other) payments at lower levels of the company's offshore structure.

Recent and upcoming major tax law changes

A company that has historically asserted indefinite reinvestment with respect to a foreign subsidiary may not be able to maintain the assertion to the extent the difference in the company's book and tax bases in the foreign subsidiary will be taxable under subpart F. For example, without the look-through rule, distributions paid from a lower-tier foreign subsidiary to its foreign parent may result in a deemed dividend (ie subpart F income) to the US parent. Accordingly, the US parent may be unable to assert indefinite reinvestment on the book/tax basis difference related to the unremitted earnings in the lower-tier foreign subsidiary if dividends are expected to be paid after the expiration date of the subpart F look-through exception.

Where the active financing exception applies, it may be necessary to record US deferred taxes for a foreign subsidiary's inside basis temporary differences if their reversals will result in subpart F consequences. See Example 11-17 and 11-18 in PwC's [Guide to Accounting for Income Taxes](#) for an illustration of the interaction of subpart F income and the indefinite reinvestment assertion.

Uzbekistan

The following measures were enacted during the fourth quarter of 2013 in Uzbekistan:

- Income received by non-residents from disposal of property ie real estate or shares in Uzbek companies in Uzbekistan will be subject to withholding tax.
- List of corporate tax benefits and exemptions will be reduced (eg the exemption for income received from the sale or liquidation of fully depreciated assets will be abolished).

Tax accounting refresher

During the 2013 calendar year we saw a continued increase in the number of tax-related comment letters issued by the staff of the SEC. In this section, we will focus on three of the main accounting areas highlighted by these letters: (1) indefinite reinvestment assertions, (2) valuation allowance assessments, and (3) uncertain tax positions. We expect these topics will be continued areas of focus by regulators, investors, and commentators in 2014.

Indefinite reinvestment assertions

The assertion of indefinite reinvestment of foreign subsidiary earnings continues to be one of the more complex and judgmental areas of accounting for income taxes. The continued growth in unremitted foreign earnings; scrutiny from stakeholders, such as the OECD, around base erosion and profit shifting; and the ongoing uncertainty within the global economy has brought heightened attention to the application of the indefinite reinvestment assertion.

Companies should consider a number of factors when evaluating their indefinite reinvestment assertion. Some of these factors are discussed below.

Processes and controls

Coordination and alignment among the multiple business functions within a company's global organisation is imperative. Processes and controls must be in place to ensure that the indefinite reinvestment assertion is consistent with the best information available to the organisation and represents the whole organisation's view, plans, and expectations.

Documentation

A specific, documented plan should lay out items such as the parent and subsidiary's long- and short-term projected working capital and other

financial needs in locations where the earnings are generated. Evidence maintained by management should include documented reasons why any excess earnings are not needed by the parent or another entity in the group.

Consistency with budgeted and actual data

Management should consider the consistency of its assertion with the parent and subsidiary's long- and short-term budgets and forecasts, any past dividends, and the tax consequences of a decision to remit or reinvest. To the extent management can demonstrate that the rate of return on reinvesting foreign earnings exceeds the rate of return on repatriated funds, management should consider documenting that consideration.

Transactions between the foreign subsidiary and the US parent

Management should consider any transactions, such as loans or credit support, provided by the foreign operations to the US parent that may be relevant in assessing whether the indefinite reinvestment assertion can be made. Transactions that present risk of US taxation may suggest that foreign funds or liquidity are needed in the US, thereby possibly preventing an assertion of indefinite reinvestment.

Tax accounting refresher

Management's support

Management must have the ability and intent to indefinitely postpone home country taxation. The assertion needs to be supported by all levels of management with significant decision-making input on plans or transactions that could impact the company's assertion. Where controlling or shared ownership is present, the assertions must be aligned with the expectations of owners who may have governance or decision-making influence.

Financial position and the tax profile of the company

The liquidity and overall financial health of the company must be factored into the assessment of the assertion. If the unremitted earnings may be needed at the parent level to meet existing and anticipated obligations, it may be difficult to support an assertion of indefinite reinvestment. The tax profile of the company should also be considered. For example, if the unremitted earnings were needed to avoid the expiration of foreign tax credit carryforwards, it might also be difficult to support the assertion.

Expired favourable provisions

As mentioned in the section above, certain favourable subpart F provisions (eg the look-through treatment of payments between related controlled foreign corporations and exceptions for certain active financing income) expired on 31 December 2013.

These expired provisions, which may have previously enabled US tax deferral, should be considered, particularly, when evaluating the indefinite reinvestment assertion at the lower levels of a company's organisational structure. This is due to the increased potential for subpart F to arise from cross-border dividend (or certain other) payments.

Recognition of a deferred tax asset

When the outside tax basis exceeds the book basis in a foreign subsidiary, a deferred tax asset (DTA) related to that temporary difference is recognised only when it is apparent that the difference will reverse in the foreseeable future. For example, recognition of a benefit may occur when there is a planned disposal of the subsidiary. However, the expectation of near-term subsidiary profits would not by itself provide a basis for recognising a DTA on the outside basis difference.

Foreign tax credit benefit

We believe there are limited circumstances in which foreign taxes that are expected to become foreign tax credits in the foreseeable future would be recognised as a benefit through the recording of a DTA prior to the actual repatriation event. Among factors to consider, the company must be committed to making the repatriation that triggers the foreign tax credit benefit in the near term.

Disclosures

Due to the significant judgments involved in assessing the indefinite reinvestment assertion, and the potential magnitude of the unrecorded deferred tax liability, transparent disclosure is often critical. For more information, please refer to the recently released PwC Tax Accounting Services publication –[*Income Tax Disclosure*](#).

Tax accounting refresher

Valuation allowances

The valuation allowance assessment on DTAs is an area that has always presented a challenge for financial statement preparers.

The assessment requires significant judgment and a thorough analysis of all positive and negative evidence available to determine whether all or a portion of the DTAs is more likely than not to be realised. In this analysis, the weight given to positive or negative evidence is directly related to the extent to which it can be objectively verified. Accordingly, recently observed financial results are given more weight than future projections which are often inherently subjective.

As companies perform their assessments, the following reminders may be helpful.

Jurisdictional assessment

The valuation allowance assessment needs to be performed on a jurisdiction-by-jurisdiction basis. Further, where the local tax law does not allow for consolidation, the valuation allowance assessment may be at the separate legal-entity level, as opposed to the jurisdictional level.

All available evidence

The accounting standard requires that all available evidence be considered in determining whether a valuation allowance is needed, including events occurring subsequent to the balance sheet date but before the financial statements are released. However, a valuation allowance assessment should not anticipate transactions over which the company does not have control. For example, initial public offerings, business combinations, and financing transactions are generally not considered as part of a valuation allowance assessment until the period the transactions are completed.

Triggering events or changes in circumstances

In assessing potential changes to a valuation allowance (ie establishing or releasing), it is important to consider what triggering events have occurred since the prior assessment and whether a change in conclusion is warranted.

An entity should consider the appropriate timing to release the valuation allowance when circumstances change. Cumulative income (eg on a three-year basis) is not a prerequisite to releasing a valuation allowance. Rather, an entity must consider the totality of all positive and negative evidence when considering whether to release a valuation allowance.

Character of DTAs

The realisation of DTAs is dependent upon the existence of sufficient taxable income of the appropriate source and must create incremental cash tax savings. For example, if tax losses are carried back to prior years, freeing up tax credits (which were originally used to reduce the tax payable) rather than resulting in a refund, a valuation allowance would still be necessary if there are no sources of income that allow for the realisation of the freed-up tax credits. In other words, utilisation does not always mean realisation. The substitution of one DTA for a future DTA, without a source of income for the future DTA's realisation, does not represent realisation.

Outside basis differences

The reversal of an outside basis difference in a foreign subsidiary can only be viewed as a source of taxable income to support recovery of DTAs, when the foreign earnings have not been asserted as indefinitely reinvested.

Taxable temporary differences on equity method investments can be considered a source of taxable income, provided there is an appropriate expectation as to the timing and character of reversal in relation to DTAs.

Tax accounting refresher

Deferred tax liabilities

Taxable temporary differences associated with indefinite-lived assets (eg land, goodwill, indefinite-lived intangibles) generally cannot be used as a source of taxable income. Thus, a valuation allowance on DTAs may still be necessary even when an enterprise is in an overall net deferred tax liability (DTL) position. When the existence of future taxable income is in doubt and the enterprise is in a net DTL position, the timing and nature of reversal of the DTLs must be analysed.

In jurisdictions with unlimited carryforward periods for tax attributes (eg NOLs, AMT credit carryforwards, and other non-expiring loss or credit carryforwards), the related DTAs may be supported by the indefinite-lived DTLs.

Disclosures

Due to the significant judgments involved in determining whether a DTA is realisable, transparent disclosures are often critical. For more information, please refer to the recently released PwC Tax Accounting Services publication –[*Income Tax Disclosure*](#).

Tax accounting refresher

Uncertain tax positions

The assessment of an uncertain tax position (UTP) is a continuous process that does not end with the initial determination of a position's sustainability.

As of each balance sheet date, unresolved positions must be reassessed to determine whether new information exists. The US GAAP accounting standard ASC740, Income Taxes, requires that changes in the expected outcome of a UTP be based on new information, and not on a mere re-evaluation of existing information.

New information

New information can relate to developments in case law, changes in tax law, new regulations issued by taxing authorities, interactions with the taxing authorities, or other developments. Such developments could potentially change the estimate of the amount that is expected to eventually be sustained or cause a position to meet or fail to meet the recognition threshold.

In assessing UTPs, an organisation is required to recognise the benefit of a tax position in the first interim period that one of the following conditions is met:

- The more-likely-than-not recognition threshold is met
- The tax position is 'effectively settled' through examination, negotiation, or litigation
- The statute of limitations for the relevant taxing authority to examine and challenge the tax has expired

Effective settlement

For a tax position to be considered effectively settled, all three of the following conditions must be met:

- The taxing authority has completed its expected examination procedures, including appeals and any required administrative reviews.
- The taxpayer does not intend to appeal or litigate any aspect of the tax position included in the completed examination.
- It is remote that the taxing authority would examine/re-examine any aspect of the tax position.

In jurisdictions like the United States, where the taxing authority can re-examine tax positions that gave rise to a net operating loss or other carryforward in the year those carryforwards are used, the judgment as to whether effective settlement has occurred becomes more complex. If the requirements of effective settlement are met, the resulting tax benefit is required to be reported. In other words, the application of effective settlement criterion is not elective.

Disclosures

Required disclosures related to UTPs are often extensive and can be highly sensitive. For more information, please refer to the recently released PwC Tax Accounting Services publication – [*Income tax disclosure*](#).

Contacts

For more information on the topics discussed in this newsletter or for other tax accounting questions, including how to obtain copies of the PwC publications referenced, contact your local PwC engagement team or your Tax Accounting Services network member listed here.

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