Keeping up with the constant flow of international tax developments worldwide can be a real challenge for multinational companies. International Tax News is a monthly publication that offers updates and analysis on developments taking place around the world, authored by specialists in PwC’s global international tax network.

We hope that you will find this publication helpful, and look forward to your comments.

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Australia

Government releases exposure draft legislation implementing technical tweaks to hybrid mismatch rules

The government released exposure draft legislation implementing changes to Australia’s hybrid mismatch rules.

The draft legislation contains a number of technical amendments first announced in the 2019/20 budget which would:

- clarify that the rules apply to multiple entry consolidated (MEC) groups in the same way as consolidated groups
- change the definition of ‘foreign income tax’ to exclude foreign municipal or state taxes
- clarify the operation of the hybrid mismatch rules for trusts
- change the interaction between the low tax lender and other OECD compliant hybrid mismatch rules and
- clarify the operation of the dual inclusion income on-payment rule.


PwC observation:

The hybrid mismatch rules commenced on January 1, 2019. Taxpayers should fully understand how the rules may apply to them, consider restructuring possibilities, and document any positions that they take.
Barbados / Bermuda / UAE

Bermuda, Barbados and the UAE adopt new rules, guidance on economic substance requirements

The government of Bermuda, on December 20, 2019, passed the economic substance amendment No. 2 act (2019) which entered into effect on December 24. The Minister of Finance also issued updated regulations which took effect on December 24, along with final guidance notes. Following a review by the OECD and the European Code of Conduct Group (the ‘CoCG’), and several months of further consultations with both organizations, the Barbados government repealed the business companies (economic substance) Act, 2018-41, and replaced it with the recently enacted companies (economic substance) Act 2019-43 (‘the Barbados Act’) and the economic substance guidelines Version 1 (‘the Barbados guidelines’). The United Arab Emirates (UAE) Ministry of Finance, on January 5, 2020, published Frequently Asked Questions (the ‘FAQs’) with respect to the UAE economic substance regulations. The FAQs clarify certain aspects of applying the economic substance regulations and the guidance on the regulations. Although the FAQs provide additional clarity on certain key areas, other areas may require further clarity.

Please see our PwC Insight for more information.

PwC observation:

Multinationals should determine whether the substance requirements apply to their business/entities and begin planning how they can demonstrate the required economic substance requirements in various jurisdictions. In Bermuda, companies should complete and submit their economic substance declarations.

In Barbados, all resident companies (other than those being grandfathered) must comply with the economic substance rules as of the fiscal period commencing on or after January 1, 2020. As the Barbados government goes through this transition period, various government agencies are expected to announce additional measures and guidelines clarifying the scope and application of the Act.

In the UAE, entities should assess whether and which of their activities fall within the scope of the economic substance regulations and what steps to take in order to meet the economic substance test with respect to each relevant activity. This is both a qualitative and quantitative assessment that involves consideration of operational, financial, tax/transfer pricing, legal, and governance matters.
Belgium corporate tax updates

Below is a summary of several recent corporate tax developments in Belgium:

- **Royal Decree 30% EBITDA rule:** A royal decree has been published with respect to the economically equivalent interest concept, the allocation of negative EBITDA, and the allocation of the EUR 3M threshold.

- **Belgian implementation of DAC 6:** Belgium implementation closely follows the Directive's scope.

- **Tax reform:** The last tax reform step entered into force in FY2020, including changes related to the permanent establishment (PE) definition, the use of (non-final) losses of foreign PEs and the limitation on certain business expense deductibility.

- **Dividend received deduction (DRD):** The Court of Justice of the EU (CJEU) ruled that Belgium’s participation exemption (the 'DRD') is not in accordance with EU law because of the order of deductions.

**PwC observation:**

Companies should consider modeling in order to determine the impact of the interest limitation and other tax reform provisions.

Taxpayers and intermediaries need to be aware of the new reporting obligation for cross-border arrangements should they fall within the hallmarks. Companies should assess whether the tax reforms impact them.

Taxpayers also should assess whether the DRD’s application in any year resulted in the loss of another tax deduction (because of a time limit). If so, taxpayers could file an ex officio relief request or protest letter to safeguard their rights.
Colombia passes tax reform

The Colombian Executive Branch, on December 27, 2019, signed into law the tax reform that the Colombian Congress passed in late December (Law 2010 of 2019). The law became effective on January 1, 2020 and mirrors most of the provisions contained in the 2018 tax reform that was ruled unconstitutional by the Colombian Constitutional Court, including the following provisions:

- progressive corporate income tax (CIT) rate reduction from 33% to 32% for FY 2020, 31% for FY 2021, and 30% beginning in FY 2022
- the presumptive income tax regime’s progressive elimination (alternative mechanism to determine tax basis for CIT purposes) from 1.5% to 0.5% for FY 2020 and 0% for FY 2021 and onward
- temporary increase of the CIT rate for financial institutions (an additional 4% for FY 2020 and 3% for FY 2021 and FY 2022)
- limiting application of the thin-capitalization rules to related-party debt transactions (local and cross-border) and observing a 2:1 debt-to-equity ratio
- holding entity regime creation
- controlled foreign company (CFC) regime adjustments
- taxation of indirect transfers of Colombian assets (including shares), including provisions related to step-up in basis and relief in specific cases where indirect transfer results from foreign merger/spinoff transactions
- increase in income withholding tax rate on cross-border payments related to administrative services to 33%
- withholding tax rate on dividend payments to foreign parties increased to 10% (from 7.5%)
- reduced statute of limitations for amended income tax returns filed in 2020 and 2021 that show an increase in tax liability and
- creation of a net wealth tax applicable to individual taxpayers (not applicable for resident companies and nonresident companies except under certain limited exceptions) that had net equity of at least COP 5,000,000,000 (Approx. 1,520,000 USD) as of January 1, 2020. The net wealth tax will apply at a rate of 1% for FY 2020 and 2021.

Please see our PwC Insight for more information.

PwC observation:
Since the tax reform law passed prior to December 31, 2019, the provisions (mostly mirroring the previously ruled unconstitutional 2018 tax reform law) were made effective as of January 1, 2020.
France

France implements anti-hybrid provisions of ATAD 1 and ATAD 2 directives into law

The 2020 finance law implements into French law the anti-hybrid provisions included in the ATAD 1 and ATAD 2 directives. The objective of the new regulations is to combat tax optimization schemes between related companies that are based on the differences between the laws of two States as to the characterization of a financial entity or instrument or the allocation of a payment. This covers operations that give rise to a tax deduction in one State without giving rise to corresponding taxation in another State. The new regulations also cover situations in which the same charge or loss gives rise to a deduction in more than one State. The official commentaries from the French tax authorities have not yet been published, but implementation of the above directives does not appear, at first sight, fully compliant.

Moreover, the finance law for 2020 abrogates the previous anti-hybrid provisions which prohibited the tax deduction of interest when the related company (whether or not established in France) having loaned the funds, was not subject on the corresponding interest to a tax at least equal to a quarter of the French tax determined under common law conditions. At the time these provisions were adopted, doubts appeared on their conformity with European Union law since the CJEU sanctions texts which are a priori of general application but which de facto discriminate between internal operations and cross-border operations.

Please see our PwC Insight for more information.

PwC observation:

The scope of the former and the new French anti-hybrid provisions is very different and companies should conduct a complete review of their intragroup financing in order to determine whether the reform impacts them. Multinational companies operating in France should consider the impact of the Finance Act with respect to their international flows, structure, and tax obligations. ATAD II provisions require a thorough understanding of the interactions and conflicts between foreign tax regimes with respect to the same structures or flows.

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Significant changes enter into force in the Hungarian corporate income tax legislation

Hungarian corporate income tax (CIT) legislation enacted significant changes effective on January 1, 2020.

Introduction of exit taxation rules

The Hungarian corporate income tax regime introduced exit taxation provisions aimed at complying with the EU's anti-tax avoidance directive (ATAD I) harmonization requirements.

Accordingly, a Hungarian taxpayer is subject to 9% CIT at the time that its assets exit, on an amount equal to the positive difference between the fair market value of such assets (to be determined in line with general transfer pricing guidelines) and the tax book value of those assets, in the following cases:

- upon transferring its assets from its domestic PE to a foreign PE, or to its foreign head office insofar as Hungary will no longer have taxation rights on those assets following the transfer, and
- upon transferring its domestic PE's business to another jurisdiction, insofar as Hungary will no longer have taxation rights on the underlying assets following the transfer.

The exit taxation under the above rule is only triggered if the underlying transaction would not otherwise be subject to the same tax burden in Hungary.

Finally, the new rules prescribe that transactions regarding securities financing, assets provided as collateral, complying with prudential capital requirements, or transactions necessary for liquidity management purposes are out of scope from an exit taxation perspective, provided that the related assets are set to be reverted to Hungary within 12 months.

Implementation of hybrid mismatch rules and related anti-avoidance provisions

Also as of January 1, 2020, Hungarian CIT legislation incorporated the respective provisions of the ATAD II (EU Directive 2017/952) regarding hybrid mismatches in order to meet the implementation requirements as set out in the Directive.

Notably, the implemented provisions are in substance parallel with those enacted in ATAD II with respect to the scope [Paragraph (9) of Article 2], anti-avoidance provisions regarding hybrid mismatches (Article 9), and tax residency mismatches (Article 9b).

The new rules do not include provisions on reverse hybrid mismatches (as detailed within Article 9a), as these are expected to be incorporated in the Hungarian legislation only when the corresponding deadline of December 31, 2021 approaches.

PwC observation:

The latest legislative changes are significant, as they intend to meet EU law harmonization measures. At the same time, in certain aspects, the new rules are not completely straightforward and give room for differing interpretations. As such, companies should review existing and contemplated new structures.

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Italy adopts digital services tax and reintroduces notional interest deduction

Italy recently adopted Law n. 160 of 2019, implementing its Budget Law for 2020 (the Law). The adoption follows the Law’s approval on December 27, 2019 and the Law’s publication in the Official Gazette on December 30, 2019. The Law contains several corporate tax provisions, including a digital services tax and reintroduction of a notional interest deduction for capital injection.

Reintroduction of the notional interest deduction (NID)

The NID benefit was reintroduced effective for fiscal year 2019 at a 1.3% rate. The benefit seems to have been reintroduced without any effective interruption of the deduction – the measure was repealed effective in 2019 with the 2019 Budget law and now is reinstated retroactively to 2019. Italian lawmakers clarified that this aspect of the provision was intended to avoid any ‘temporal gaps’ in the benefit’s application. Accordingly, all relevant capital increases and decreases (including also those deriving from the application of anti-abuse provisions) that occurred since December 31, 2010 should be considered when calculating the benefit.

Digital services tax (DST)

The DST is effective as of January 1, 2020. Its entry into force was not dependent on any further legislation. The DST appears to target revenues from digital services that underpin ‘user participation,’ such as the:

1. channeling of advertisements on a digital platform targeting the users of the same platform (‘targeted online advertising’)
2. availability of online platforms and multi-sided digital interfaces that allow user interaction and may facilitate the sale of goods and services among them and
3. transmission of user data generated from their activities on digital interfaces.

The DST applies to revenues generated during the calendar year that result from providing the above-described digital services by businesses that meet both of the following conditions (individually or group-wide) in the prior calendar year:

- total worldwide revenues of at least € 750 million
- revenues of at least € 5.5 million obtained in Italy from providing digital services (as described above). The tax does not apply to goods and services provided between affiliated companies.

Tax credits for investments in new assets replacing the amortization benefits

The new ‘Industry 4.0 Plan’ provides for a new tax credit on the investments made in 2020, repealing the hyper and super depreciation benefits in force up to 2019. The tax credits will be determined as follows:

- investments in the new capital goods functional to the digitalization and technological transformation (i.e., the same assets covered by the hyper amortization benefit) will benefit from a tax credit equal to 1) 40% of the investment cost up to € 2.5M and 2) 20% of the investment cost up to € 10M
- investments in the other new tangible assets (i.e. the same assets covered by the super amortization benefit up to 2019) will benefit from a tax credit equal to 6% of the investment cost up to € 2M.

Revaluation of the business assets

Companies adopting Italian GAAP may elect for the revaluation of tangible and intangible assets (excluding goods for selling), shareholdings in subsidiaries and associated companies already booked in the FY 2018 financial statements by paying a substitutive tax for CIT (i.e., IRES and IRAP) purposes equal to 12% (in case of non-depreciable assets) or 10% (in case of non-depreciable assets) on the revaluation.

Please see our PwC Insight for more information.

PwC observation:

The Italian Budget Law includes several important measures, introducing both ‘new’ tax benefits (for example, the NID), credits, and also adopts new taxing measures such as the DST. These new opportunities and challenges will impact multinationals significantly.
Announced 2020 Japan tax reform proposals

The ruling parties in Japan published their 2020 tax reform proposals (‘2020 tax proposals’) on December 12, 2019. Most of the provisions in these proposals are expected to be passed into law this March.

Abolishment of consolidated tax system and introduction of group tax relief system

The introduction of group tax relief would allow domestic corporations to allocate profits and losses between companies within a 100% Japan-parented group. The new law would be effective for fiscal years beginning on or after April 1, 2023. The proposals introduce measures to transition from the current consolidated tax system. The basic rules for applying group tax relief essentially would be the same as under the current consolidated tax system. However, under the new system for group tax relief, the parent corporation and each subsidiary would file their own (blue form) corporate tax return. These tax returns also would need to be e-filed.

Under group tax relief, proposed measures would provide for calculating, among other items, 1) the allocation of current profit and loss and losses carried forward to the group member corporations; 2) adjustments to the book value of subsidiary corporations, and 3) the valuation of assets owned and (dis)allowance of losses carried forward, upon entry or exit from the group or beginning or termination of group tax relief. In contrast to the current consolidated tax system, under group tax relief, certain income or tax credits would be calculated on a stand-alone entity basis to reduce the administrative burden on group corporations. On the other hand, certain tax measures would be determined on a group basis (such as the amount of R&D credits). To align with the proposed changes, the current rules of the ‘group taxation regime’ would be reviewed, including the dividend income exclusion, donation expenses, bad debt allowances, and capital gain deductions arising from the intra group transfer of assets.

International taxation

a. Measures to prevent tax avoidance through the payment of dividends and subsequent transfer of shares in subsidiaries. If the dividend received from an affiliated subsidiary (i.e., a subsidiary with a specified control relationship on the date of the dividend resolution) exceeds 10% of the book value of the shares of that affiliated subsidiary, the book value of the affiliated subsidiary would be reduced. That is, any capital gain on the transfer of the shares cannot be reduced through dividend payment.

b. Calculation of a CFC’s income with partial income aggregation Interest received from suppliers to whom financing was provided would be excluded from a CFC’s aggregated taxable income.

c. The scope of creditable foreign tax payments under the foreign tax credit regime would be reviewed.

d. Non-deductible interest under the earnings stripping rules would exclude certain interest paid by a Japanese corporation to a Japanese permanent establishment of a foreign corporation.

e. The reporting system for automatic exchange of country-by-country reports of non-residents would be reviewed.

Please see our PwC Insight for more information.

PwC observation:

Multinational enterprises currently investing in Japan should review their existing structures and determine the impact of the proposed rules. Specifically, corporations should analyse the potential effects related to the earning stripping rules and dividends received modifications.

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Luxembourg

Luxembourg passes law implementing ATAD 2

The Luxembourg Parliament on December 19, 2019 voted to approve the law implementing the EU ATAD regarding hybrid mismatches with third countries into Luxembourg domestic law (ATAD 2 Law).

The ATAD 2 Law follows the text of ATAD 2 rather closely, adapting it mainly to integrate with the structure and terminology used in the Luxembourg Income Tax Law (LITL).

Note that the reports of the State Council and the Budget and Finance Commission left the text of the legislation largely unaltered from the bill submitted to Parliament in August 2019.

However, the Budget and Finance Commission stated that further guidance, potentially in line with what is emanating from the State Council, may be appropriate in the form of a tax authority Circular or a Grand-Ducal decree addressing various points. Unfortunately, there is no certainty over when, or even whether, such a Circular or Grand-Ducal Decree might be issued.

Please see our PwC Insight for more information.

PwC observation:

In general, the ATAD 2 Law will apply to tax years beginning January 1, 2020, with the additional ‘reverse hybrid’ measures applicable as of the 2022 tax year (i.e., to tax years closing in 2022 – fiscal year taxpayers may see these ‘reverse hybrid’ measures applicable in 2021). Taxpayers should assess the potential impact of the ATAD 2 law.

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Mexico tax reform: Fiscally transparent entities

The recently enacted 2020 Mexico tax reform significantly modifies the taxation of income earned through foreign fiscally transparent vehicles; such legal structures are common in the private equity space. Investment funds often consolidate investments through a foreign fiscally transparent vehicle that does not have legal personality in its jurisdiction of formation ('Foreign Transparent Vehicle'), which, in turn, invests in Mexican entities. The tax reform affects the tax treatment of Mexican-source income received by the Foreign Transparent Vehicle, as well as the deductibility of the cross-border payments made by the Mexican entity. In contrast to the reform’s general effective date of January 1, 2020, the changes to Foreign Transparent Vehicles are effective January 1, 2021.

Effective January 1, 2021, Article 4-A of the Mexican income tax law provides that a Foreign Transparent Vehicle will be taxed as a separate entity for Mexican income tax purposes if it is not a tax resident in either its jurisdiction of formation or the location of its effective seat of management. This law change directly conflicts with the pass-through rule, and upon its effective date, the new law will override the look-through treatment provided by the pass-through rule. On its own, this statutory change would increase significantly the tax burden of many investment funds that have a presence in Mexico.

However, as part of the legislative discussion leading up to the tax reform, Congress included Article 205. This article provides that a Foreign Transparent Vehicle is eligible for pass-through treatment for Mexican tax purposes if the vehicle meets three requirements: 1) it manages private equity; 2) it invests in Mexican entities; and 3) it is fiscally transparent in its jurisdiction of formation. The fiscal transparency provided in Article 205 for Mexican tax purposes will apply only for specific categories of passive income: interest, dividends, capital gains, and lease payments for immovable property. Article 205 provides a narrower benefit than the pass-through rule, which allows for fiscal transparency in determining the withholding tax on all Mexican-source income and is not limited to private equity investments.

PwC observation:
Mexican investments structured through a Foreign Transparent Vehicle may no longer benefit from fiscal transparency, effective January 1, 2021. The statutory exception provided for private equity funds requires that controls be put in place to gather and file with the Mexican government information regarding the individual fund members. Furthermore, the fund structure should be assessed before and after the change to fiscal transparency under the Article 28 non-deductibility rule to understand any impact to the effective tax rate of the Mexican entities. For new investments into Mexico, funds should consider structures that meet the new requirements for fiscal transparency and the deductibility of payments by the underlying Mexican entities.

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Spanish coalition parties announce significant tax reform

The Spanish Parliament on January 10 re-elected the socialist prime minister, Pedro Sánchez. A coalition government between two left-wing parties – Socialist Party and Unidas Podemos is expected to form in Spain. These parties already have released a political agreement containing significant tax measures. The proposals would impose a significant tax burden on both corporations and individuals. The political agreement includes a significant increase in income taxation and the introduction of new levies. Some of the announced tax measures were included in the draft Budget Bill for 2019, which was not enacted.

Even though the prospective coalition government will not have a majority in the Chamber of Deputies, socially driven bills, including the proposed tax reform bill, could pass with the support of small left-wing regional parties. The tax reform likely will be legislated during 2020. Some of the measures may be effective retroactive to January 1, 2020.

The political agreement contemplates several corporate income tax measures. A minimum corporate income tax rate of 15% generally would be established for large corporate taxpayers. However, financial institutions and oil and gas companies would be subject to a higher rate of 18%.

The agreement also calls for a reduction from the current full participation exemption on dividends and capital gains from qualifying shareholdings to a 95% exemption. The 5% taxable portion would qualify as nondeductible expense related to managing the shareholding. If the proposal is passed, dividends and capital gains from qualifying shareholdings would be subject to an effective tax rate of 1.25%. The partial exemption would apply to both foreign source and domestic dividends and capital gains. This measure would have a significant impact on Spanish holding companies ('ETVEs').

The agreement includes other tax measures that would align with other EU jurisdictions’ reforms. These include a digital services tax, which would align with the EU guidelines; a tax on financial transactions on the purchase of Spanish shares by players in the financial industry; and environmental taxes. The agreement also indicates a new tax on empty dwellings as well as on large real estate holdings, but it provides no details.

PwC observation:
If the proposed tax measures are enacted, they could have a significant impact on both Spanish corporations and individuals. Multinational enterprises with either operations in Spain or with Spanish holding companies should review how the proposed changes could affect their Spanish investments.

It remains to be seen whether the tax reform also will affect the 0% withholding tax on dividends distributed by ETVEs consisting of foreign source dividends and the capital gains that they generate.

Please see our PwC Insight for more information.
Turkey

Turkey enacts digital services tax

Turkey’s law accepted in December 2019 introduces three new taxes in 2020, in addition to implementing several other revenue-generating measures. Among the new taxes is the implementation of a 7.5% digital services tax. This tax would apply to revenue resulting from the supply of certain digital services that are characterized by user value creation. The new tax is intended to have a narrow target, only applying to big businesses with global revenue of over EUR 750 million and local revenue of TRY 20 million. The new tax will be effective on March 1, 2020.

Included among the revenue-generating measures are the doubling of the exchange tax from 0.1% to 0.2% for foreign currency sales and

- introduction of a new dispute resolution mechanism, which enables taxpayers to settle with the tax authority after commencing with court proceedings.

PwC observation:
The tax measures accepted for 2020 and following years introduce new taxes and rules that increase tax revenues. Taxpayers should evaluate the potential impact and monitor implementation guidance that tax authorities expect to release.

Uruguay

Incentives to promote entrepreneurship

The Uruguayan Congress approved Entrepreneurship law (Law No. 19.820), which entered into force on October 7, 2019.

The law’s aim is to facilitate entrepreneurship development, giving accessible tools and modern mechanisms that will provide competitiveness to ventures in Uruguay. The law created a new type of legal entity, a simplified stock corporation (SAS), which may be incorporated by a single person and does not require certain publication approvals requested of corporations. In addition, the principle of party autonomy will govern the SAS.

From a tax perspective, an SAS is incorporated as a taxpayer of income tax (IRAE), property tax (IP) and value added tax (VAT). Nevertheless, a temporary tax exemption regime applies when certain conditions are met.

Finally, the law recognizes crowdfunding as an entrepreneurship funding mechanism delegating the establishment of limits and setting up to the Uruguayan Central Bank.

PwC observation:
The introduction of this new type of legal entity is a way to attract new investments, improving the development of business in a fast, simple and low-cost legal framework.

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The ATO updates corporate residency guidance

The ATO updated its Practical Compliance Guideline (PCG) 2018/9 on corporate residency.

In 2017, the ATO dramatically altered its residency test approach for companies not incorporated in Australia under the 'central management and control' test and provided transitional relief, until June 30, 2019, designed to give taxpayers time to adjust to this new ATO approach. This update extends the transitional relief period for companies that are taking active and timely steps to change their governance arrangements to align with the new ATO approach. Generally, the transitional period has been extended until December 31, 2020 (for December 31 tax year ends) and until June 30, 2021 (for June 30 tax year ends).

In addition, the PCG now indicates that “it is unlikely the Commissioner would apply resources to review the residence” of a foreign company that “has its operating business wholly offshore.”

The Board of Taxation is conducting a review of the operation of Australia’s corporate tax residency rules. The purpose of the review is to ensure that the rules are operating appropriately in light of modern, international and commercial board practices and international tax integrity rules. Further details are expected later this year.

PwC observation:
While the extended transitional period and new ‘operating business wholly offshore’ concession are welcomed, Australian taxpayers with offshore activity should consider the PCG in detail, review existing governance protocols and, if required, make necessary changes with respect to foreign incorporated companies.

ATO releases guidance on treaty anti-abuse rules

The ATO released draft law Administration Practice Statement PSLA 2019/D2 which deals with the administration of general anti-abuse rules, such as a principal or main purposes tests, included in any of Australia’s tax treaties. The provisions include:

- the Principal Purpose Test (PPT) under paragraph 1 of Article 7 of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) and
- a Main Purpose Test (PPT in an Australian tax treaty that is yet to be, or will not be, modified by the MLI).

Comments were due February 14, 2020.

PwC observation:
The MLI adoption has resulted in a large number of Australian tax treaties being subject to the PPT. The framing questions and document indicators provide helpful guidance for taxpayers considering its application.
Dutch Supreme Court rules on interpretation of Dutch anti-abuse rules

The Dutch Supreme Court, in a January 10, 2020 judgment, ruled that a dividend payment by a Dutch company to a foreign corporate shareholder constitutes Dutch taxable income of that shareholder under the so-called ‘substantial interest taxation rules.’ The Court concluded that the structure was abusive.

In the case at hand, a Dutch company – originally a holding company of a Dutch insurance firm – distributed a dividend to its Luxembourg shareholder X (a company incorporated under Dutch law but effectively managed in Luxembourg). X did not have an office at its disposal, did not have any employees and merely incurred various legal and administrative expenses. The shares in X were ultimately held by one Swiss individual. At the time of the dividend distribution, the Dutch company had sold its activities and merely held the cash proceeds from that sale (i.e., it was a so-called ‘cash-box’ company).

In order for the dividend distribution to constitute Dutch taxable income of X under the substantial interest taxation rules, it had to be confirmed that:

a. X held its shareholding in the Dutch company with the main purpose, or one of the main purposes, of avoiding the levy of Dutch personal income tax or dividend tax at the level of the Swiss individual (subjective condition); and that
b. The shareholding in the Dutch company could not be functionally allocated to X’s business (objective condition).

According to the Supreme Court, both tests were satisfied.

As to the subjective condition: if X had not been ‘interposed’, the Netherlands could have taxed the dividend distribution to the Swiss individual. Furthermore, based on the facts, X had no relevant function within the group and no economic activities and therefore constituted a wholly artificial arrangement in the meaning of various European Court of Justice cases.

In reaching its conclusion as to the objective condition, the Supreme Court in addition took into consideration that, at the time of the distribution, the Dutch company was a mere ‘cash box’ and as such could not be allocated to the business of its shareholder X. It follows from both conclusions that the Supreme Court tested the abuse conditions at the moment of the dividend distribution and hence has confirmed that the anti-abuse rules are a continuous test.

PwC observation:

The judgment sheds an important light on the Dutch Supreme Court’s interpretation of the Dutch anti-abuse rules and confirms that these rules are a continuous test. Similar anti-abuse rules are implemented in the Dutch dividend withholding tax act and will be implemented in the 2021 withholding tax act regarding interest and royalties. Furthermore, the Dutch State Secretary of Finance is of the view that the (PPT also needs to be interpreted in line with these anti-abuse rules. Taxpayers should carefully consider the judgment in light of these developments.

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No slowdown in unilateral tax measures targeting digital activities in 2020

2020 started with new digital services taxes (DSTs) coming into effect in Italy and Austria, with more on the horizon in the coming months, including agreed legislative provisions from Turkey beginning in March. The pace of countries considering DSTs continues to accelerate, even as discussions by the OECD Inclusive Framework move forward, driven in part to mitigate the rationale for DST implementation.

France (which retroactively applied its law to the beginning of 2019) and Italy mark the most active DSTs currently in effect. Modelled in part on the paused European Commission directive regarding a DST, both countries target large technology firms with more than €750 million in global sales and local revenues thresholds with a 3% tax. Activities considered in-scope include online advertising services and the provision of digital intermediation (such as online marketplaces, dating services, and app stores). Austria chose a limited measure in only subjecting online advertising revenues to a 5% tax (an extension of its traditional advertising tax). However, Turkey has arguably enacted the strongest DST to date, which begins on March 1, 2020 – at 7.5%, its scope goes beyond the French version to capture transmissions of digital content services (such as streaming services) and internet of things (IoT) sensor data.

Each of these measures places new, substantial compliance burdens on affected companies (or those likely to be affected), requiring not only administrative filing with tax authorities but implementation of new data systems to collect information on the location of purchasers/users to substantiate the various revenue thresholds used.

The United Kingdom is also committed to introducing a 2% DST as of April 2020 (based on deemed revenues attributable to certain activities rather than specific revenue streams). The UK Budget will be announced in March 2020. Spain has expressed strong interest in an EU-inspired DST and is likely to move forward on this measure in with its newly installed government.

Please see our PwC Insight for more information.

PwC observation:
Continued uncertainty and global adoption of DST measures make 2020 an important year for carefully monitoring tax legislation and policies.
**Tax Treaty between China and Botswana enters into force**

The China-Botswana tax treaty, which was signed on April 11, 2012, entered into force on September 19, 2019. The tax treaty is applicable to income in China derived in any taxable year beginning on or after January 1, 2019. For income derived in Botswana, the tax treaty applies to the amount subject to tax withholding at source on or after October 19, 2018, and taxable income subject to other taxes derived on or after July 1, 2019. The important features of the China-Botswana tax treaty include:

- The time threshold for constituting a construction permanent establishment (PE) is 12 months, while that for constituting a service PE is 183 days within any 12 month period.
- For passive income, the restricted withholding tax rates are as follows: dividends, 5%; interests, 7.5% (except for interests received by the government, a local authority, the Central Bank or any financial institution wholly owned by the government, which is exempted from tax); royalties, 5%.
- The taxing right on capital gains arising from the transfer of property-rich shares rests with the source state. In other cases of share transfers, the taxing right lies with the residence state.
- Principle purpose test: provision in each of the article of dividends, interest, royalties, and other income, to deny the granting treaty benefits if the main purpose or one of the purposes of putting in place any arrangement is to take advantage of the treaty benefit.

**Mainland China and Macao sign fourth protocol to the tax treaty**

The China mainland and Macao signed the fourth protocol to the Mainland-Macao tax treaty on November 28, 2019. The fourth protocol will enter into force upon completion of ratification procedures and notification by both sides. Highlights include:

- **Article 4:** China and Macao tax authorities shall endeavor to determine the tax residency status of a person by mutual agreement by taking into account its place of effective management, the place where it is incorporated, or otherwise constituted.
- **Article 5:** Introducing a stricter definition for Agency PE by widening the scope of Agency PE to those who habitually play the principal role leading to the conclusion of contracts, which is also in line with BEPS Action 7.
- **Article 21:** Adding a new government investment article providing tax exemption treatment for income derived from funds for government invested livelihood projects.
- **Article 26:** Adding a new PPT article, under which a benefit under the Mainland-Macao tax treaty shall not be granted if obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit.

**PwC observation:**

The twelve-month threshold for constituting a construction PE is not commonly seen in tax treaties concluded by China (usually six-month). It indicates Botswana's will to encourage cross-border construction activities.

The fourth protocol to the China-Macao tax treaty indicates China’s intention to put it on par with other tax treaties concluded or re-negotiated by China in recent years, especially with Hong Kong, the other Chinese Special Administrative Region.

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<tr>
<th>Acronym</th>
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<tr>
<td>ATAD</td>
<td>Anti-Tax Avoidance Directive</td>
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<td>ATO</td>
<td>Australian Tax Office</td>
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<td>BEPS</td>
<td>Base Erosion and Profit Shifting</td>
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<td>CFC</td>
<td>controlled foreign corporation</td>
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<td>CIT</td>
<td>corporate income tax</td>
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<td>CJEU</td>
<td>Court of Justice of the European Union</td>
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<td>CoCG</td>
<td>Code of Conduct Group</td>
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<td>DRD</td>
<td>Dividend received deduction</td>
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<td>DST</td>
<td>digital services tax</td>
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<td>DTT</td>
<td>double tax treaty</td>
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<tr>
<td>EBITDA</td>
<td>Earnings before interest, tax, depreciation and amortization</td>
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<td>Multinational corporation</td>
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<td>PCG</td>
<td>Practical Compliance Guideline</td>
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<td>Principal Purpose Test</td>
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