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International Tax News

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Launch

Welcome

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.

Featured articles

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Responding to the potential business impacts of COVID-19

COVID-19 can cause potentially significant people, social and economic implications for organisations. This link provides information on how you can prepare your organisation and respond.

In this issue

Legislation

Australia

Australia's offshore banking unit (OBU) regime

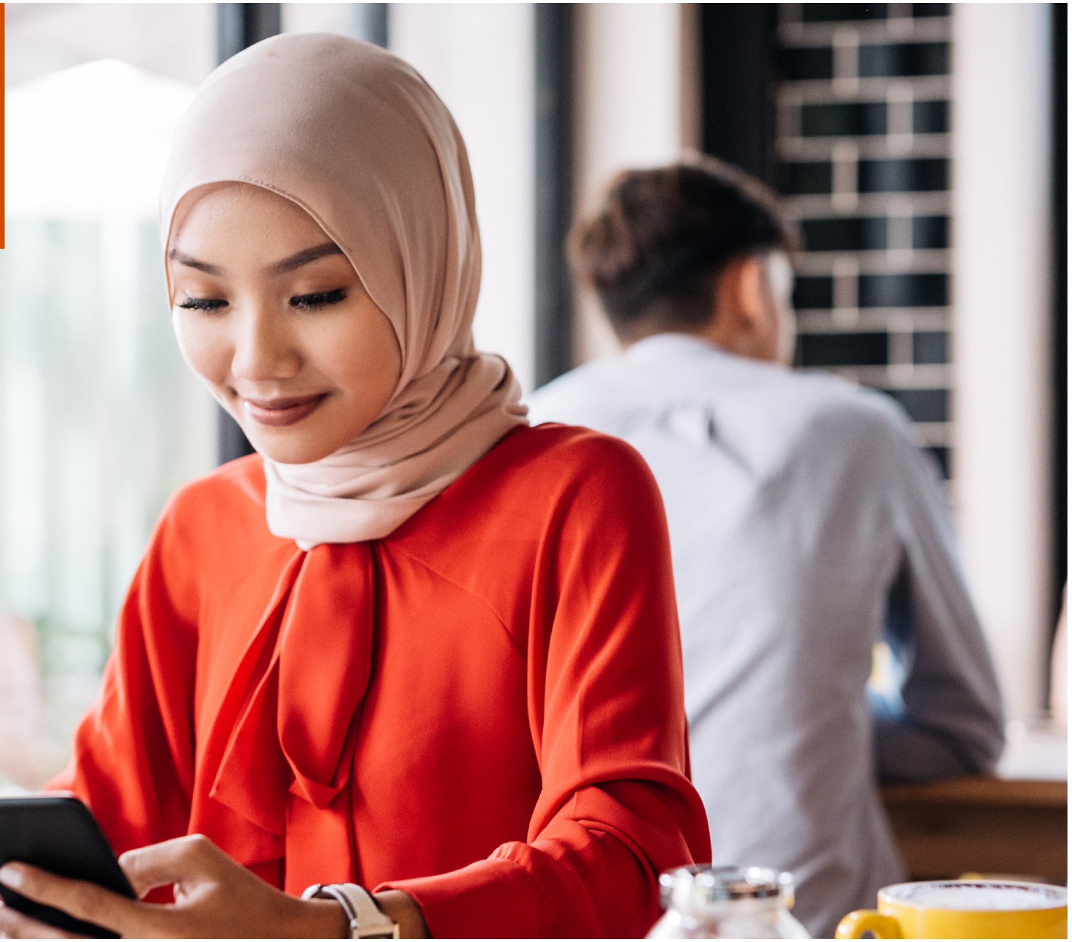
Australia's offshore banking unit regime provides a more attractive tax rate for offshore banking activity conducted by Australian-registered banks. In response to the(OECD's Forum on Harmful Tax Practices, which raised concerns while reviewing the regime, the government decided to amend the OBU to remove the preferential tax rate and close the regime to new entrants.

The amending law (Treasury Laws Amendment (2021 Measures No. 2) Bill 2021) is currently before Parliament. Once enacted it will:

- ensure that OBU income derived from OBU activities are subject to the relevant corporate tax rate in relation to assessments for the 2023-24 income year, and all tax years thereafter
- remove the withholding tax exemption for interest payments (including interest consisting of gold paid) on or after January 1, 2024, on offshore borrowings by OBUs, and remove the Minister's ability to declare or determine that a person or company is an OBU (applicable from the day after the amendments receive Royal Assent).

PwC observation:

Existing participants operating within the OBU regime can continue to access the concessional tax rate up until the end of the 2022-23 income year. In this transitional period, the Australian government is expected to consult on alternative measures to ensure activity remains in Australia.



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Canada

Canada's 2021 budget addresses mandatory disclosure, DST, interest limitation, and hybrid mismatches

The Deputy Prime Minister and Minister of Finance, Chrystia Freeland, presented the Canadian Government's budget on April 19. The budget includes several international tax proposals, in which the budget:

- enhances Canada's mandatory reportable transaction disclosure rules, subject to public consultation, provides further details of a proposed digital services tax, to be effective January 1, 2022,
- limits the deductibility of interest by corporations, trusts, and partnerships to a percentage of tax-basis EBITDA, and
- introduces rules to address hybrid mismatch arrangements.

The budget does not contain any proposed changes to Canadian corporate tax rates.

Mandatory disclosure rules

The government is consulting on proposals to enhance Canada's mandatory disclosure rules to address:

- changes to the Income Tax Act's (ITA's) existing reportable transaction rules
- a new requirement to report 'notifiable transactions'
- a new requirement for specified corporations to report uncertain tax treatments, and
- related rules providing for, in certain circumstances, extension of the applicable reassessment period and the introduction of penalties.

Digital services tax

As previously announced in the November 2020 Fall Economic Statement, the budget proposes to implement a digital services tax (DST) effective January 1, 2022. The DST is a 3% non-income tax introduced as a temporary tax until an acceptable multilateral approach is agreed and implemented by the OECD members and G20 countries. The DST targets large global businesses earning revenue from certain digital services reliant on the engagement, data, and content contributions of Canadian users. The revenue subject to DST is grouped into four categories: revenues earned from online marketplaces, social media, online advertising, and user data ('in-scope revenue').

Interest deductibility limits

The budget proposes a new rule that would limit the net interest expense that a corporation may deduct in computing its taxable income to no more than a fixed ratio of its 'tax EBITDA.' The new rule also would apply to trusts, partnerships, and Canadian branches of non-resident taxpayers.

Hybrid mismatch arrangements

The Action 2 report of the BEPS Action Plan recommended that countries adopt detailed rules to eliminate the tax benefits arising from hybrid mismatch arrangements. The budget proposes to implement rules that are intended to be consistent with the recommendations of this Action 2 report (with modifications for the Canadian income tax context).

For more information see our **PwC Insight**.

PwC observation:

With this proposed budget, Canada is aligning with actions proposed by the OECD, the European Union, and many jurisdictions. Given the global momentum for such provisions, MNCs should understand how the proposals might impact their operations. In addition, MNCs should consider providing feedback on such impact as requested within the proposals.

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China

China's new CIT preferential policies for small and thin-profit enterprises (STEs) and super R&D deduction

For STEs, the corporate income tax (CIT) on the first RMB 1 million of annual taxable income will be further reduced by 50%, with an effective CIT rate of 2.5%, effective from January 1, 2021 to December 31, 2022. Specifically, where an STE's annual taxable income does not exceed RMB 1 million (inclusive), its annual taxable income would be cut by 87.5% and subject to CIT at a rate of 20% (i.e., an effective CIT rate of 2.5%); where the STE's annual taxable income exceeds RMB 1 million, but does not exceed RMB 3 million (inclusive), its annual taxable income would be cut by 50% and subject to CIT at a 20% rate (i.e., an effective CIT rate of 10%), compared with the standard 25% CIT rate in China.

For manufacturing companies, the super deduction ratio of R&D expenses increases from 75% to 100% beginning January 1, 2021. Where R&D expenses incurred have not formed intangible assets, taxpayers can claim an additional 100% deduction of eligible R&D expenses when calculating the taxable income. Where such R&D expenses have formed intangible assets, such assets can be amortized based on 200% of their cost.

PwC observation:

CIT relief for STEs will help to further reduce the tax burden of micro, small and medium enterprises, which took the most direct hit from COVID-19, and help market players stand firmly and thrive.

Additionally, in order to support scientific and technological innovation, China enacted a preferential policy for the R&D expenses super deduction to relieve the tax burdens of enterprises and encourage them to increase R&D spending.

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Cyprus

Cyprus addresses DAC6, prevention of tax abuse, and treaties with Egypt and Germany

The Cyprus Parliament on March 18 approved the draft Bill amending the Law on Administrative Cooperation in the Field of Taxation, implementing DAC6.

In addition, the Cypriot Ministry of Finance (MoF) submitted two bills to Parliament to amend tax legislation to strengthen Cyprus' tax framework for preventing tax abuse, tax evasion, and tax avoidance (the 'bills'). The bills, which currently state that they would be effective July 1, 2021, include the following proposals:

For payments to companies in jurisdictions on the EU 'blacklist' (i.e., companies in jurisdictions included in Annex I of the **EU list of non-cooperative jurisdictions on tax matters**), withholding taxes (WHTs) are introduced (or, in the case of royalties, expanded) as follows:

- for payments of dividends, WHT at a 17% rate
- for payments of passive interest, WHT at a 30% rate
- for payments of royalties, WHT at a 10% rate.

The corporate residency test (currently the 'management and control' test) is expanded with the introduction of a test based on incorporation in Cyprus, for companies that do not have a tax residency anywhere else in the world.

The new tax treaty between Cyprus and Egypt, which was signed on October 8, 2019, and which entered into force on July 31, 2020, is effective as of January 1, 2021, based on a recent Interpretative Directive issued by the Cyprus Tax Authority (CTA). The new tax treaty replaced the existing treaty between Cyprus and Egypt (signed in 1993).

On March 5, Cyprus ratified the amending Protocol to the tax treaty between Cyprus and Germany that was signed on February 19, 2021. Certain legal procedures now need to take place in both states following which the Protocol will enter into force. The Protocol introduces, inter alia, minimum standards of the OECD's BEPS actions.

The amended Protocol includes:

- the replacement of the wording in the treaty's preamble
- the alignment of 'Article 7 Business Profits' with the OECD Model Tax Convention
- the introduction of a Principal Purpose Test through the treaty's pre-existing Article 27 'Entitlement to Benefits.'

For more information see our **PwC Insight**.

PwC observation:

Companies should immediately begin analysing, tracking, and collecting information on potentially reportable arrangements in order to comply with the implemented DAC6 law.

Cyprus reiterates its commitment to prevent tax abuse, tax evasion, and tax avoidance with the introduction of the new bills. The Cyprus MoF notes that the bills align with recent EU Country-Specific Recommendations (CSRs) for Cyprus and the EU guidelines for defensive tax measures to be adopted by EU Member States towards EU blacklisted jurisdictions. The bills do not indicate the applicable effective date of Cyprus WHTs to jurisdictions added to each new version of the EU blacklist, or the disapplication effective date of Cyprus WHTs to jurisdictions removed from each new version of the EU blacklist. The Cyprus authorities are expected to clarify this and other matters after voting on the bills.

The new tax treaty agreed between Cyprus and Egypt will help develop the two-way trade and economic relations between the two States with provisions therein that are fully aligned with the current OECD principles and minimum standards. The main purpose of the Protocol to the existing Cyprus – Germany tax treaty is to introduce minimum standards of BEPS actions.

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France

France updates list of non-cooperative states and territories

France has updated its non-cooperative states and territories (NCST) list in a February 26, 2021 decree (published on March 4, 2021). According to the French tax code, this list should be updated every year. The list was last updated in January 2020.

Transactions with entities established in countries on the French NCST list lead to the application of anti-avoidance measures and potential withholding taxes at the increased rate of 75%.

Bahamas and Oman have been removed from the list effective March 4, 2021. However, Palau and Dominica have been added (this addition will apply effective June 1, 2021). Effective June 1, France's NCSTs will include Anguilla, Panama, British Virgin Islands, Seychelles, Vanuatu, Dominica, Fiji, Guam, American Virgin Islands, Palau, American Samoa, Samoa and Trinidad and Tobago.

The EU Council updated its own NCST list on February 12, 2021. With this update, the French list of NCST matches the EU list with the sole exception of the British Virgin Islands which remain on the French list but not on the EU list.

PwC observation:

Transactions with NCSTs are assessed at the payment date. For instance, a transaction with Palau prior to June 1, 2021, will not be considered to have been made with a NCST. MNEs should be aware of payment dates and watch for future updates to the French NCST list.

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Hong Kong

Proposed relaxation of foreign tax deduction for profits tax purpose

The Inland Revenue (Amendment) (Miscellaneous Provisions) Bill 2021 (the Bill) was gazetted on March 19, 2021. The Bill, among other things, seeks to enhance the foreign tax deduction for profits tax purposes as a means of providing domestic tax relief for foreign taxes paid under the following situations:

1. foreign taxes paid in a treaty jurisdiction by a non-Hong Kong resident on (a) specified interest, gains, or profits and (b) other gross income.
2. foreign taxes paid in a non-treaty jurisdiction by a non-Hong Kong resident on gross income other than specified interest, gains, or profits.
3. foreign taxes paid in a non-treaty jurisdiction by a Hong Kong resident on income other than specified interest, gains, or profits.

In scenarios (1) and (2), the claimant is required to take all reasonable steps to minimize the foreign tax payable and would not be entitled to claim any double tax relief in the jurisdiction of residence.
In scenario (3), the claimant is required to take all reasonable steps to minimize the foreign tax payable.

Currently, foreign taxes paid in a non-treaty jurisdiction by a Hong Kong resident or a non-Hong Kong resident on specified interest, gains, or profits are deductible, provided that the claimant has taken all reasonable steps to minimize the foreign tax payable.

Upon the Bill's enactment, the revised rules on the foreign tax deduction will take effect beginning in the 2021/22 assessment year.

The EU Council updated its own NCST list on February 12, 2021. With this update, the French list of NCST matches the EU list with the sole exception of the British Virgin Islands which remain on the French list but not on the EU list.

PwC observation:

The proposed changes address the double taxation issue that Hong Kong taxpayers face. The proposed relaxation should help develop Hong Kong as a regional intellectual property or service hub.

As the new rules will only take effect beginning in the 2021/22 assessment year, but not retroactively, Inland Revenue could consider allowing a deduction of foreign taxes paid by taxpayers during the transition period as an interim measure.

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Mexico

Mexico approves significant changes for subcontracted services

Mexico's Senate approved legislation on April 20 that significantly modifies the tax and labour laws for outsourcing structures. Outsourcing structures are impacted when a Mexican entity contracts with a related or unrelated legal entity/individual for services and the employees of the service provider are at the disposition and benefit of the service recipient. The labour reform was effective April 24, 2021, and the tax reform will be effective August 1, 2021.

In general terms, subcontracting of specialized services or works not forming part of the purpose or predominant economic activity, if provided by a registered contractor is allowed. Furthermore, subcontracting of workforce is prohibited when it consists of providing or putting personnel at disposal, for the benefit of others.

For more information see our **PwC Insight**.

PwC observation:

Given the tight timeline for compliance, taxpayers should analyse the effect of these new rules on their Mexican operations and determine they warrant changes to their outsourcing framework. Failure to comply with the new rules could result in significant penalties, including potential characterization of tax fraud.

These reforms will impact several areas within Mexican groups, requiring a holistic risk assessment and alignment of actions to the new rules. Some recommended immediate actions include:

- reviewing all services relationships with third and related parties.
- considering restructuring and transfer pricing issues resulting from potential transfer of functions, assets and risks.
- reviewing company bylaws (corporate purpose and predominant activity) from different angles (e.g., from corporate, regulatory, and tax perspective).
- reviewing contracts and evaluating new terms and conditions (e.g., indemnities, etc.).
- implementing compliance tax and other processes and controls considering the use of technology.
- ensuring governance in order to comply and mitigate risks with relevant stakeholders: workers, providers, clients, labour, tax and other authorities.
- determining whether the restructuring falls within the Mexican Mandatory Disclosure Regime for tax purposes.
- considering the US tax implications based on any alignment actions.

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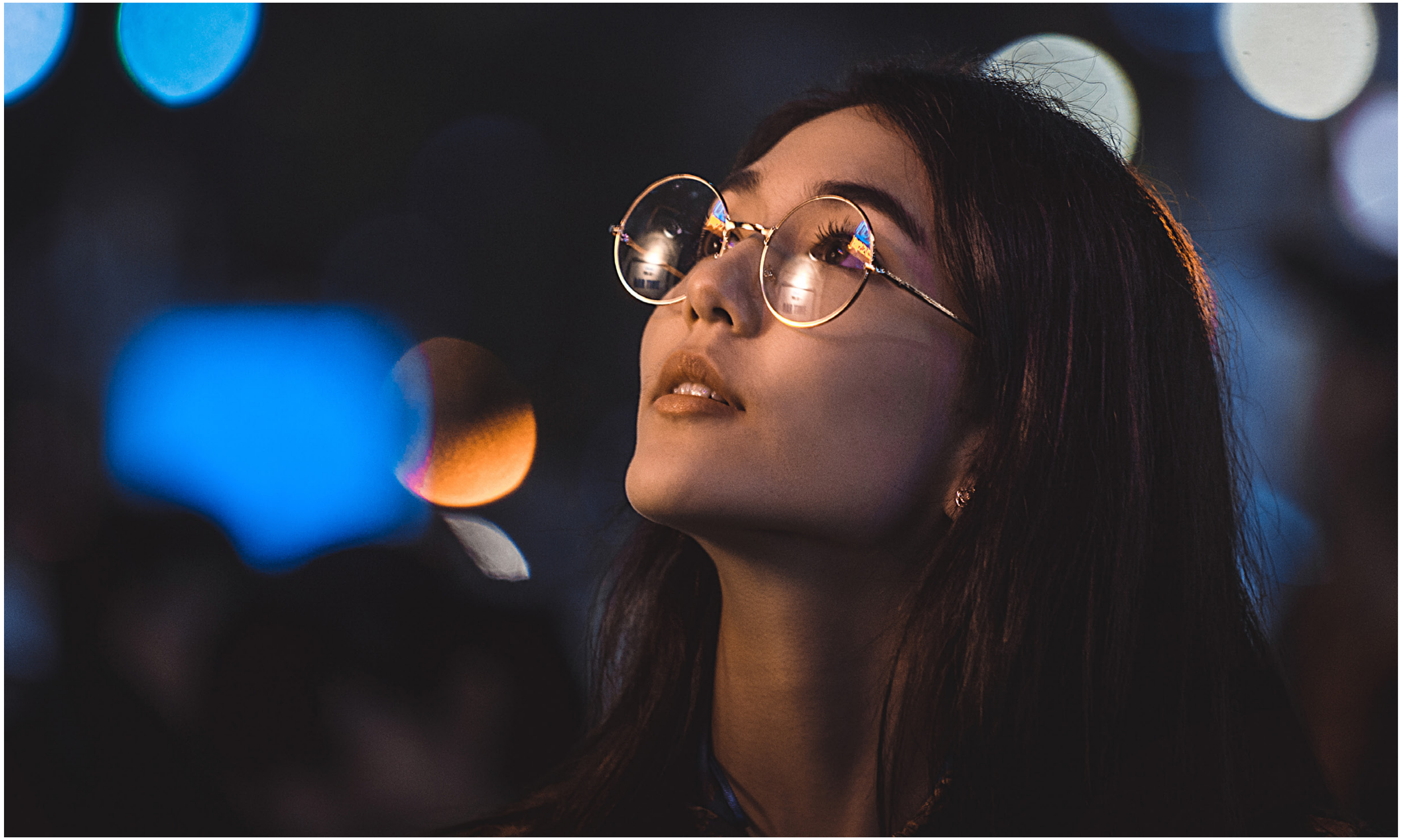
Uruguay

New temporary tax benefits for investment projects

Investment Law No. 16,906 and its regulations offer tax benefits for companies investing in fixed assets. In order to further promote investment, Uruguay issued Decree No. 94/021 on March 23, 2021. It foresees a new temporary increase in the benefits granted.

The Decree includes the following temporary benefits:

i. The computation of 130% for those investments executed between April 1, 2021 and September 30, 2021 when calculating CIT deduction (this benefit is applicable to both new and pre-existing projects).
ii. Incremental benefits previously granted to investments from 2016, 2018 and 2020, may also benefit from this new provision.



PwC observation:

Companies should consider whether current or planned investments could benefit from the new investment project.

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Administrative

Australia

ATO proposes hybrid rules guidance

Australia's hybrid mismatch rules include 'imported mismatch' rules, which may apply more broadly than OECD BEPS Action 2 – compliant hybrid rules implemented in other countries. On April 21, the Australian Taxation Office (ATO) released a draft practical compliance guideline (**PCG 2021/D3**), which provides guidance on how taxpayers practically should apply the imported mismatch rule and what documentation is required.

The PCG provides guidance for taxpayers grappling with these rules in a self-assessment environment, but sets a high bar in terms of the information and documentation required to substantiate Australian deductions. The PCG details the level of supporting information the Commissioner expects taxpayers to obtain prior to filing income tax returns and in order to sustain deductions for payments to offshore related parties.

For more information see our **PwC Insight**.

PwC observation:

Australia's imported mismatch rules can apply to a broad range of taxpayers, and can apply even where there is no Australian tax planning involved. In order to substantiate Australian deductions (including interest, royalties, and purchases of goods and services), MNCs should consider the hybrid mismatch rules.

Accordingly, all taxpayers making cross-border related-party payments will need to consider the draft PCG and the potential work necessary to meet the proposed ATO requirements prior to filing their Australian tax return. This likely will require significant involvement from tax departments in the parent entity jurisdiction, up to and including involvement by the group head of tax.

Although these ATO requirements are not required by law, taxpayers should consider the consequences of not meeting ATO expectations, including the tax return disclosures that may be required (after the PCG is finalized), the impact on penalties in the event a tax shortfall later is identified, and the potential impact on the FIRB approval processes.

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Ireland

Anti hybrid – Irish Tax Authority guidance

The Irish tax authorities published updated guidance with respect to the Irish anti-hybrid legislation, which was introduced and effective for payments made on or after January 1, 2020, and applies to all payments where a tax deduction is obtained after January 1, 2020. The existing published guidance provides helpful examples , and clarifies some on particular areas where the legislation was not necessarily clear, or was open to alternative interpretations.

The most significant update to the guidance includes guidance on the imported mismatch test, and also includes additional helpful wording, to ensure certain updated legislation captured all intended circumstances.

PwC observation:

The Irish tax authorities have continued providing helpful guidance to taxpayers and their advisers to clarify the application of the anti-hybrid rules in Ireland. As the legislation applies to deductions taken post January 1, 2020, MNCs with Irish companies should assess the impact of the latest guidance on the application of the Irish anti-hybrid rules on intra group payments.

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Ireland

Interest limitation rule feedback statement

Interest limitation rules, as required by the EU Anti-tax Avoidance Directive, are set to be transposed into Irish law later this year and take effect January 1, 2022.The Irish Department of Finance has been running a public consultation process on the implementation of ATAD Article 4 Interest Limitation rules. This consultation process closed on March 8, with various stakeholders, including PwC Ireland making submissions to the department, responding to the various questions raised by the department of Finance, and input into how the rules would fit into the existing tax code.

PwC observation:

While the legislation is still draft, it is expected to be effective January 1, 2022, and therefore MNCs with Irish companies should assess the possible impact of the proposed Irish interest limitation rules on interest payments made by the Irish entities in their group. Further guidance addressing other aspects of the rules is expected to be published by the Department of Finance within the next couple of months.

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New Zealand

Imported (indirect) hybrid mismatch rules: New Zealand's draft documentation requirements

New Zealand's Inland Revenue has released an exposure draft with respect to the imported hybrid mismatch rules setting out the steps Inland Revenue expects taxpayers to have undertaken before claiming deductions for cross-border related party payments.

In most scenarios, Inland Revenue expects the New Zealand taxpayer to obtain a written statement from the group's head office tax function, i.e., global head office, confirming the steps required to ensure that there are no imported hybrid mismatches that the New Zealand payer has funded.

The exposure draft outlines that there may be severe consequences if the taxpayer is unable to produce this confirmation, within a reasonable timeframe, upon request. In particular, this could include Inland Revenue simply denying a deduction claimed and the loss of the taxpayer's ability to challenge a deduction denial by Inland Revenue.

For more information see our **PwC Insight**.

PwC observation:

If the exposure draft is finalised in its current form, it would apply beginning with the 2019-2020 income tax years (the due date for these returns was March 31, 2021). PwC has submitted comments on the exposure draft and, in particular, highlighted that the application's timing should be delayed until the 2020-21 income tax year. This would help taxpayers since the due date for the first relevant tax returns has passed yet the requirements are still in draft. In the interim we recommend that taxpayers ensure they have documentation outlined in the exposure draft on file.

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Glossary

Acronym	Definition
ATAD	Anti-Tax Avoidance Directive
ATO	Australian Tax Office
BEPS	Base Erosion and Profit Shifting
CFC	controlled foreign corporation
CGT	capital gains tax
CIT	corporate income tax
CSR	country-specific recommendations
DAC6	EU Council Directive 2018/822/EU on cross-border tax arrangements
DST	digital services tax
DTT	double tax treaty
EBITDA	earnings before interest, tax, depreciation and amortization
ECJ	European Court of Justice
ETR	effective tax rate
EU	European Union

Acronym	Definition
GAAP	generally accepted accounting principles
IF	inclusive framework
IP	intangible property
M&A	mergers and acquisitions
MNC	multinational corporation
NCST	non-cooperative states and territories
NRC	non-resident companies
OECD	Organisation for Economic Co-operation and Development
PCG	practical compliance guidelines
PE	permanent establishment
R&D	research & development
STE	Small & Thin Profit Enterprises
VAT	value added tax
WHT	withholding tax

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