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A STATE OF UNCERTAINTY

Your global tax partner

SESSION OVERVIEW

A STATE OF UNCERTAINTY?

Anne Harvey (Ireland), Andreas Damböck (Austria), Frédéric Teper (France), Okkie Kellerman (South Africa), Jon de Jong (USA)

This session ties together the current state of uncertainty, including BEPS implementation in various countries, recent American changes resulting from the US Tax Cuts Act, as well as national tax developments that are inconsistent with global tax consistency and certainty (including such changes and proposals for digital taxation and European state aid investigations and the risk that they pose for seemingly "ordinary" tax matters such as APAs with European tax authorities and tax assessment settlements).

PANEL INTRODUCTIONS

Panelists

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Andreas Damböck
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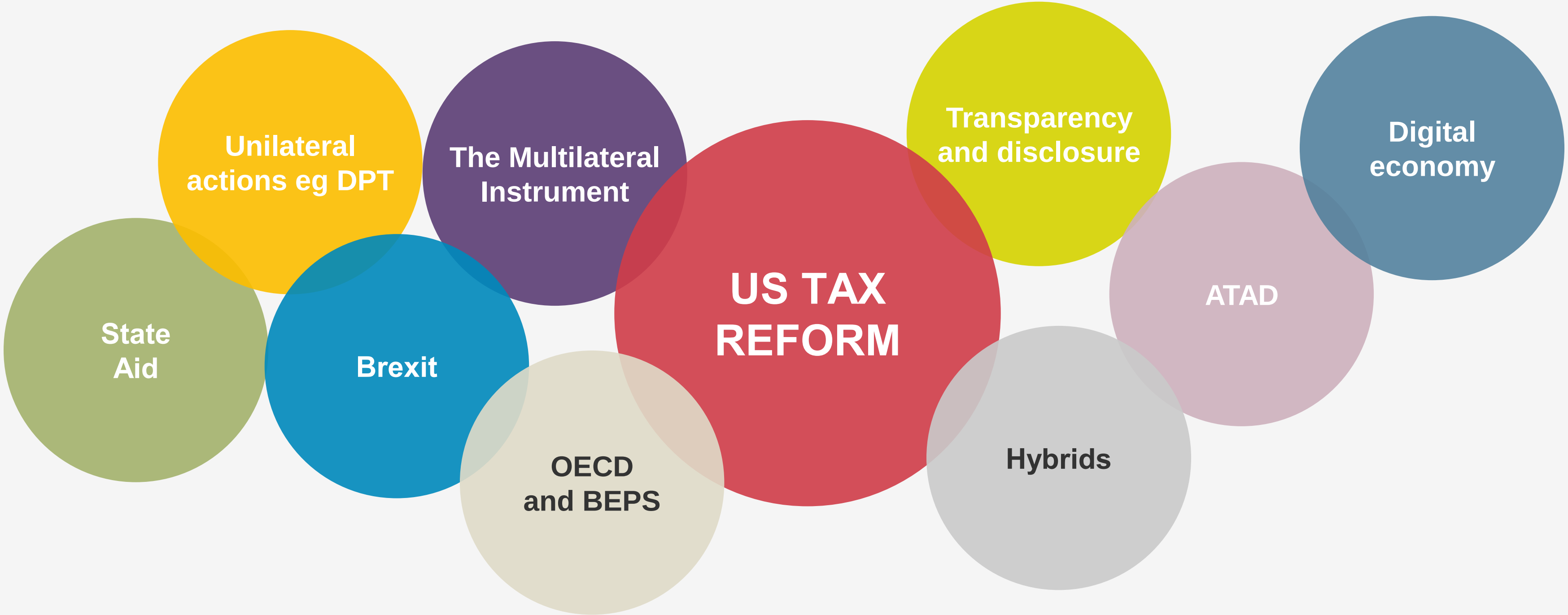
A STATE OF UNCERTAINTY: MANY MOVING PARTS…



THE US SITUATION FOR MNES IN A NUTSHELL

WHAT IS THE US MNE SITUATION NOW?

Although unsurprised by tax reform itself, US taxpayers were taken aback by the scope and haphazard approach undertaken in apparent pursuit of speedy ‘success’

Lowering of the US corporate rate came at a cost of temporary tax savings measures and compromises to raise revenue without regard to thoughtful policy

Contrary to popular reports, the US has **not** transitioned to a ‘territorial’ tax system but is embracing fully its historic system of taxing worldwide profits:

- Ending deferral
- Taxing current non-US earnings at less than the **21%** US corporate rate alongside a partial, current-year crediting regime
- Penalizing transfers of value outside the US

WHERE WILL US MNES BE FOCUSED?

Tax functions of US MNEs will likely be occupied devising strategies to **optimize the consequences** of ‘portable income’ sources in light of a **taxpayer’s business** model and:

In Europe – the uncertain location of income, given traditional economic reality measures, ‘state aid’ challenges to long-standing transfer pricing approaches, questions regarding viability of IP box regimes, BEPS-style focus on human presence, and EU Commission suggestions that revenue might guide income sourcing.

WHERE WILL US MNES BE FOCUSED?

In the US – the expansion of the US tax net, low-rate incentive to earn profits in US, disincentives to repatriate IP (courtesy of the BEAT add-back for amortization and difficulties of anti-churning analysis for established companies), and scepticism over the survival of export tax advantages (FDII).

In both – full interest deductibility and political volatility:

- Local limitations on interest deductibility will require taxpayer and lender creativity (esp. in a rising interest rate-environment)
- Many taxpayers may prefer the political devil they think they know to the one they don't; viable structures will require low-cost, timely exit options to be built-in from the outset.

POLLING QUESTION 1

Do you think that US tax reform is creating a more level playing field for global taxation?

A	Yes
B	No

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POLLING QUESTION 2

Is US tax reform encouraging a global ‘race to the bottom' for corporate taxes?

A	Yes
B	No

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THE IMPACT OF THE EU COMMISSION ON TAX POLICY

THE IMPACT OF THE EU COMMISSION ON TAX POLICY

Anti-tax avoidance directive

Member States must enact laws that largely implement G20/OECD BEPS measures.

Common consolidated corporate tax base

A major legal initiative aiming to harmonize the corporate tax rules in the EU.

Transparency

A specific proposal targeting tax advisers in order to disclose cross-border tax planning.

State aid

Investigations are resulting in behavioural change.

Digital taxes

Two Directives proposed by the Commission.

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EU ANTI-TAX AVOIDANCE DIRECTIVE

ATAD

Directive on fast track	ATAD	Three years (September 2013 – July 2016)
Compared with	Parent-subsidiary directive	21 years (1969 – 1990)
	CC(C)TB	Still pending (first proposal in 2011)

Main regulations

- Interest limitation rule
- Exit tax
- GAAR
- Hybrid mismatches
- CFC

Implementation

- **Jan 1, 2019** Most regulations
- **Jan 1, 2020** Exit tax
- **Jan 1, 2024** Interest limitation rule (if equally effective)

ATAD: LIMITED HARMONISATION WITHIN EU

Minimum standard

Significant **Elections** for Member States

eg, Interest limitation rule

- Czech Rep.: mEUR 3 threshold
- Romania: mEUR 0.2 threshold.

Different interpretations by Tax Authorities

Significant differences in **complexity** of rules implemented

eg, COPY/PASTE implementation of ATAD on minimalistic basis in some Countries.

Different **timing** approaches by Member States

Early birds (Slovakia; all rules implemented) vs Late bloomers (Croatia; none implemented)

Rules partially alread in place for long time in some Member States (eg Germany)

Deferral of implementation planned (subject to EU Commission's approval), eg Austria, Hungary.

Harmonised rules

ATAD: CHALLENGES FOR US MNES

Devising practical, long-term strategies to deduct debt service fully on a global basis while keeping lending arrangements reasonably straightforward

Optimizing the non-US effective rate below the Subpart F/GILTI rates:

- Modelling through each taxpayer's situation under US tax reform
- Building options now for potential future exits not implicating exit taxes
- Re-fighting 'economic substance' outside the US
- Anticipating the scope of each jurisdiction's CFC rules
- Finding suitable replacements to hybrid arrangements.

CCTB/CCCTB

CCTB AND CCCTB: BACKGROUND

2001
Communication of the EU Commission on a common corporate tax base

2011
First directive proposal drafted
Major disagreements on the consolidation issue

2014
Alternative proposal of the EU Council

2015
CCCTB rebooted by the EU Commission

2016
CCTB and CCCTB directive proposals drafted
Two-step approach:
First – harmonized rules
Second – consolidation

2018
Consultative approval by EU Parliament and discussion of the CCTB proposal by EU Council

CCTB OVERVIEW

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Key insights

Targeting **large companies established in the EU** (global consolidated revenues over €750m per year).

Establishes a **common mandatory base for EU companies and EU PE**, without fixing the corporate tax rate.

Main features:

- Amended definitions of taxable base and exempt revenues
- Amended definition of the permanent establishment in the EU
- Super deduction for R&D costs
- Financial expenses deduction cut to the higher of 30% of the EBITDA and €3m
- Allowance for Growth and Investment (AGI)
- Loss relief and recapture rules
- Anti-abuse rules.

CCCTB OVERVIEW

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Key insights

Mandatory regime for **large companies established in the EU** (global revenues over €750m per year).

Optional regime for groups below the €750m per year threshold.

Establishes a **common consolidated base for EU companies and PE**, without fixing the corporate tax rate.

Main features:

- Eligibility for the group based on control (50% of the voting rights) and ownership (75% of profit rights)
- Elimination of intragroup transactions
- Neutrality of business reorganizations
- Apportionment formula to share the tax base between the group members based on sales, labor factors and assets
- Single tax administration in the EU for the consolidated group.

CCTB AND CCTB: WHAT'S NEXT?

Political uncertainty

Main issues:

Approval by **unanimity** by the governments' representatives of the 27 Member States.

Tax **competition through the tax rate** only in the EU.

Compatibility between CCCTB rules and ATAD.

Possible alternative scenario:

Foreseen **enhanced cooperation** between nine member States.

More fragmented corporate tax regime within the EU.

Digital tax could **appear as** a 'temporary' **compensation to a political deadlock** regarding the CCTB/CCCTB.

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TRANSPARENCY

TRANSPARENCY FOR INTERMEDIARIES OVERVIEW

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Key insights

Directive proposal drafted on June 2017.

Mandatory reporting of cross-border arrangements by intermediaries.

Targeting **arrangements designed to obtain a tax advantage**.

Background

- Country by country reports for MNCs; rulings exchange
- Action 12 of the BEPS Plan
- Existing rules in Ireland, UK, Portugal.

Impact on the taxpayers

- Waiver from reporting when the intermediary is entitled to a **legal professional privilege: information relies on taxpayers**.

Current discussion

- Directive agreed by the EU Council on 13 March 2018
- Entry into force forseen on **1 July 2020**.

TRANSPARENCY FOR INTERMEDIARIES OVERVIEW

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Key insights

The arrangement has to be reported if it bears at least one of the indicators – ‘hallmarks’ – outlined in the proposal.

Examples:

Fees linked to the amount of a tax advantage

Cross-border payment which is deductible at source to a recipient resident in a
low-tax country

Involves a jurisdiction with inadequate or weakly enforced anti-money laundering legislation

Circumvent EU information exchange requirements

The same asset benefits from depreciation in more than one country

Arrangements that do not conform to the arm’s length principle.

‘STATE AID’

STATE AID: IT HASN'T GONE AWAY!

State aid is a competition law matter, not a tax law matter.

Business as usual in matters of competition law.

But still used by the EU Commission as an instrument for behavioural change in tax matters…

Limited clarity until the cases are heard by the CJEU.

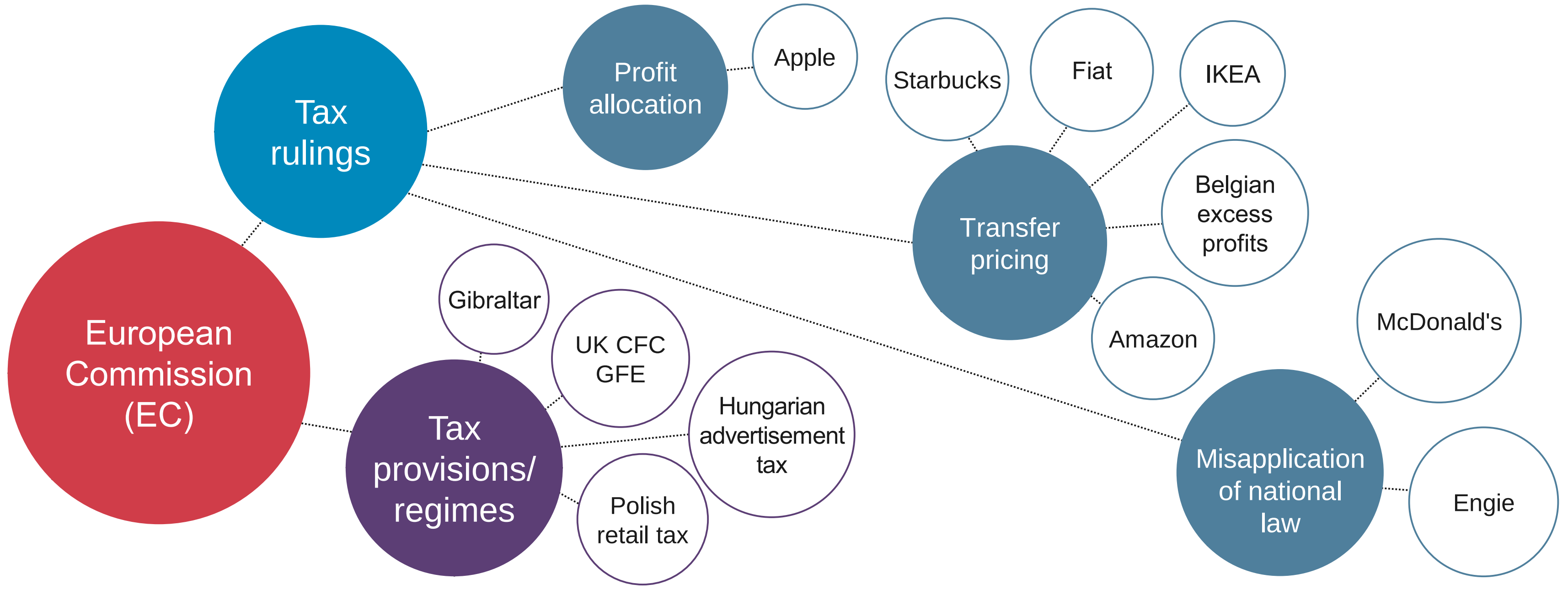
STATE AID: OBSERVATIONS

However, the Commission decisions have resulted in behavioural changes.

Some multinational companies have reorganised their structures, but State aid is not the only factor.

Member States have amended legislation, and Revenue authorities have reviewed and limited their ruling practices.

A RECAP OF THE CASES



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SOME RECENT CASES: INTER IKEA

RECENT CASES: UK CFC REGIME

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THE INITIAL US REACTION (1/3)

"The Commission's actions could threaten to undermine foreign investment, the business climate in Europe, and the important spirit of economic partnership between the US and the EU."

US Treasury

THE INITIAL US REACTION (2/3)

"The Commission has got itself now in a position where it's a bunch of plumbers doing electrical work… The Commission has probably bitten off more than it can chew."

Robert Stack,
(former senior official at US Treasury)

THE INITIAL US REACTION (3/3)

Despite the official ‘noise’, **US taxpayers** generally viewed the **state aid investigations** as attempts by influential EU Member States **to foreclose tax competition** while realizing quick revenue and halting profit-shifting arrangements.

THE CURRENT US REALITY

- Because the US government believed that it had a right to tax the foreign earnings of US-based MNEs, ‘state aid’ claims were considered threats to the fisc because foreign tax credits against US income tax reduced US government revenues
- By ending deferral possibilities for US MNEs, US tax reform has left the US government largely indifferent (economically) to ‘state aid’ results
- US MNEs have simply become more cautious and sceptical in regard to their EU operations, given this increase in tax outcome-uncertainty in countries which have been stable and predictable in the past.

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DIGITAL TAX

DIGITAL TAX: WHAT'S THE ISSUE?

The digital economy is growing…

- Close to the **third** of Europe's overall industrial output is due to digital technologies.

- From 2006 to 2017 the number of digital companies amongst the **top 20** firms by market capitalization increased from **one to nine**.

- The annual average growth of revenues of **top 5** e-commerce companies in 2017: **32%** vs **1%** in the whole EU retail sector.

- From 2006 to 2016 the digital advertising revenue multiplied by **more than five** in Europe.

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DIGITAL TAX: WHAT ARE THE (PERCEIVED) CONSEQUENCES?

- Lack of level playing field.
- Distortion of competition (**between entities, Member States**).
- Loss of public revenue.
- Social fairness.
- Risk of further single market segmentation (unilateral actions).
- Double (multiple) taxation.

DIGITAL TAX: WHAT'S HAPPENING?

- Key area of focus for both the **OECD** and the **EU Commission.**
- Physical presence **no longer key to profit** generation.
- **Proposals from both** – differing approaches.
- OECD in favour of **consensus based approach** with no interim measures.
- **EU Commission** – short and long term objectives.

DIGITAL TAX: A COMPARISON

	Strategy	Long-term proposal	Interim proposal
OECD 16 March 2018	• 113 countries • Outlines positions of three groups of countries • Two year timeline • 2019/2020 – interim and final reports.	Review of • Digitalisation • Nexus • Profit attribution.	• Not recommended • Doesn't favour unilateral measures.
EU 21 March 2018	• Has passed recommendations to Council • Parliament can propose amendments • Requires MS unanimity unless enhanced co-operation invoked.	• Draft Directive re PE thresholds where supply of digital services • Renegotiation of treaties is recommended • CC/CCCTB.	Draft Directive re Digital Services Tax (DST) • **Rate:** 3% • **Threshold:** Turnover >€750m; EU taxable turnover >€50m • **Scope:** Advertising, intermediation platforms, and transmission of user data • **Basis:** Where users (rather than) payer or payee is located • **Application:** 1 January 2020.

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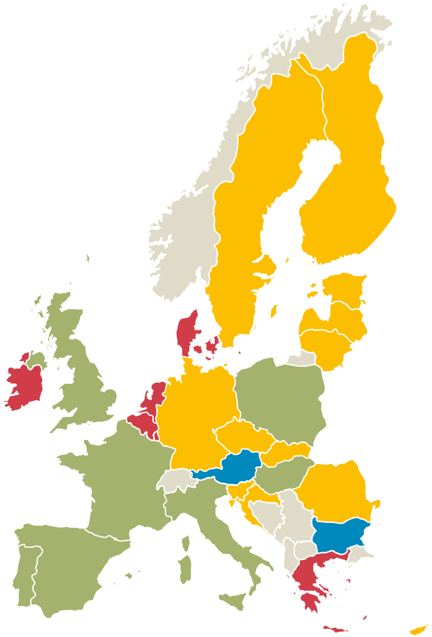
REACTION OF THE MEMBER STATES TO THE EC PROPOSALS



7 countries	Supportive
6 countries	Opposed
12 countries	Undecided
2 countries	Neutral

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POLLING QUESTION 3

Do you feel that the digital tax proposals are realistic?

A	Yes
B	No

A VIEW FROM AFRICA

TAX ON THE AFRICAN CONTINENT

- Tax remains the second-most significant threat for companies doing business on the African continent (after political instability)
- Tax challenges on the African continent

Transfer pricing	Withholding tax	Compliance

TRANSFER PRICING CHALLENGES

TP challenges in Africa:

- Lack of local comparable transactions
- Lack of specialist knowledge and resources
- Value attributable to IP may skew more taxable income to developed countries at the expense of developing countries
- Central bank controls
- Onerous withholding taxes

The use of safe harbours, fixed margins and APA could assist.

TRANSFER PRICING DEVELOPMENTS

African Tax Administration Forum (ATAF)

- Transfer Pricing Project – assist in building capacity of ATAF members.

No African country is currently a member of the OECD

- BEPS Action Plan provide further support for many African tax authorities'.

A growing number of African jurisdictions have transfer pricing regimes

- More than general anti-avoidance provisions
- Based on the arm's length principle.

TRANSFER PRICING REGIMES

- **South Africa** – OECD Guidelines
  - Comprehensive documentation requirement
  - No APAs
- **Kenya** – established TP regime
  - No APAs
- **Tanzania** – recognises OECD Guidelines
  - APAs.

TRANSFER PRICING REGIMES

Angola – TP regime for all domestic and cross-border commercial transactions

Ghana – recognizes OECD Guidelines

- Implementation of the general anti-avoidance provisions
- Full documentation requirement

Nigeria – based on OECD Guidelines and UN Manual

- APAs

Zambia – recognises OECD Guidelines.

TRANSFER PRICING REGIMES

- **Uganda** – recognises OECD Guidelines
  - Make provision for APAs
- **Botswana** – no transfer pricing regulations
- **Uganda** – recognises OECD Guidelines
  - Make provision for APAs.

WITHHOLDING TAX ISSUES

- Rates from 5% to 30% of the gross amount of the transaction
- WHT increasing (i) in number (ii) tax rate
- Levied even on:

Professional and consultancy services (Tanzania)

On branch profit repatriations (Zambia)

Technical services (Botswana)

- Goals:

Raising extra tax revenue

Obtaining more information

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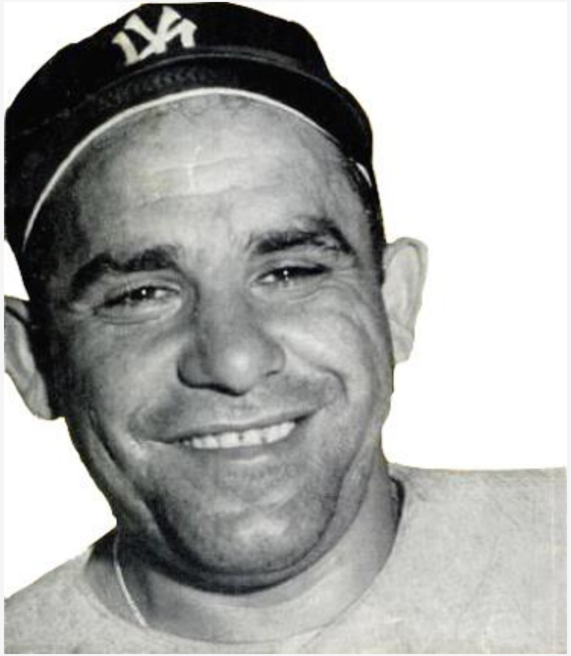
APPLICATION OF WITHHOLDING TAX

Example

	SA – only if the source is in SA – so really information gathering (PE reviews?).
	Tanzania – a source-based system – sourced in Tanzania if 'results of activities are directed to/utilised by a resident – so WHT generally applies.
	Ghana – similar in practice – no specific guidance on how to interpret the laws.
	African countries notorious for not implementing the provisions of a DTA, leading to double taxation even with a DTA.

IF WE HAD A CRYSTAL BALL…



- US reform here to stay regardless of politics
- Adjustments expected at the regulatory and judicial levels, and US-based MNEs will be working hard to contain non-US taxes
- EU Commission driving tax reform via Directives and State aid
- Changes are happening – we must be increasingly agile in our thinking…

> “It’s tough to make predictions, especially about the future.”

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SPEAKER PROFILES

SPEAKER PROFILE

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Anne Harvey is a partner of William Fry Tax Advisors, Taxand Ireland. She specialises in international corporate tax having previously worked in a Big Four practice. Anne has over 20 years' experience in advising multinational companies on the corporate tax aspects of reorganisations, acquisitions, financing and IP planning and inward investment.

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Andreas Damböck is a partner at LeitnerLeitner, Taxand Austria. He is a tax advisor and auditor, and his main areas of focus are transaction services (including private equity transactions), corporate and group tax law reorganisations and international tax law. As an author, Andreas contributes to many publications and is editor of the books “Verrechnungspreisrichtlinien – Kommentar” (Transfer Pricing Guidelines – Commentary) and “Gruppenbesteuerung” (Tax Consolidation).

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Jon de Jong joined Alvarez & Marsal Taxand's Colorado office on 1 May 2018. This follows 20+ years of work for Koch Industries, one of the world's largest private corporations (and a Taxand client), most recently in the areas of global M&A, private equity, internal structuring and matters unique to closely held companies. Jon led Koch's M&A Tax practice, as well as the group responsible for implementing transactions, and served as Tax Director for one of Koch's business divisions.

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Okkie Kellerman is an executive at ENSafrica, Taxand South Africa. He is a qualified CA (SA) and specialises in international tax with an emphasis on inward and outward investments and the funding of restructurings, take-overs, mergers and acquisitions. He is also experienced in transfer pricing, thin capitalisation, international double tax agreements and exchange control regulations. Okkie has in depth knowledge of the construction, mining, energy, manufacture, distribution and services industries.

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Frédéric Teper is based in Paris where he is a partner with Arsene, Taxand France. Frédéric has developed specific expertise in group taxation of French and international companies. He has been working for international groups and private equity houses for many years on acquisition/development projects to address optimal tax conditions (structuring, acquisition due diligence, vendor due diligence, and financial flows dividends, interest, royalties and license fees, etc).