Briefing

International review for October

Speed read

Once again, the challenges of taxing the digital economy dominate the international tax landscape, with updates from the EU, UK, Spain, Mexico and Australia. There have also been various updates from across Europe as countries start to introduce proposals to implement the requirements of the EU's Anti-Tax Avoidance Directive, with draft legislation set out in Ireland, Italy, France and the Netherlands. There have been further developments on the implementation of the OECD's BEPS multilateral instrument, including its entry into force in the UK.

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It seems not a week can go by at the moment without more developments in relation to the taxation of the digital economy. This month, the Committee on Economic and Monetary Affairs of the European Parliament (ECON) discussed the European Commission's (EC) proposals for both the taxation of a digital presence and a digital services tax (DST). European MEP Paul Tang is the rapporteur for the DST proposal for ECON, and previously released a draft report proposing that a number of amendments be made to the EC's proposals. Specifically, the draft report mentioned that the DST rate should be increased from the proposed 3% to 5%, and that the scope should be extended to include taxable revenues from the supply of digital content using a digital interface and the sale of goods or services which are contracted online via e-commerce platforms (for example, film streaming and online retailers).

Discussions of the EC's proposals and Paul Tang's report were extensive but non-conclusive: some stakeholders supported the extension of the DST scope but did not agree on the proposed rate increase to 5% (in particular, if not supported by an impact assessment); others supported both the increased rate and extended scope. There were again calls for an urgent response to the proposals for a temporary solution, to 'level the playing field' and encourage digital companies pay their fair share of tax. However, since the ECON meeting there have been reports of questions being raised by lawyers from the EU Council on the legal basis of the proposed DST, which may prove to be a key development in the discussions: watch this space over the coming weeks.

In the UK, the chancellor has commented twice in recent weeks on the UK's position regarding the challenges of taxing the digital economy: first at the Conservative Party conference where he reiterated a previous message that the UK would be prepared to act unilaterally if necessary; and second at an IMF meeting, with a softened the message that the UK was not looking at an online sales tax at the moment. Most recently, HM Treasury published a call for evidence on competition in the digital economy (see bit.ly/2PaTWpW). Whilst not specifically tax-related, it does further suggest that the UK is gearing up to take action.

There has however been activity elsewhere. As we go to press, Spain's finance minister has announced that the government will propose a DST that would apply to online advertising services, brokering services, and the sale of user data collected over the internet.

Mexico has proposed new legislation to target certain business transactions conducted via the internet, with no or very little physical presence in Mexico.

Also hitting the headlines is a discussion paper released by the Australian Treasury on 2 October, inviting stakeholder comment on possible actions that may be taken to ensure digital services are appropriately taxed. It includes considerations relevant to whether a temporary unilateral measure would be appropriate for Australia. Such a measure could target digital advertising directed at Australian users and/or paid for by Australian businesses.

However, it is recognised that there may be challenges in identifying and enforcing any interim measure, in particular where it is paid for by a foreign business to a foreign advertiser. One possible option to taxing platform fees would be to tax all fees received for a platform service where the customer and/or supplier is located in Australia. Also included in the discussion paper are suggestions for thresholds to ensure that any interim measure would apply to businesses with the ability to pay and would not adversely impact innovation, productivity and business creation. Any interim measure could also be transitioned once international consensus on a longer-term solution is reached, so as to avoid the potential for double taxation.

Australia

Staying briefly with Australia, on 11 October the prime minister announced that the government will be fast tracking the tax rate reduction for companies with a turnover of less than AUD 50m, gradually reducing the rate from the current 30% to 25% by 2026/27.

ATAD implementation

With the deadline for the implementation of the EU Anti-Tax Avoidance Directive (ATAD) pending, we have seen several EU countries implementing legislation to adopt ATAD compliant positions in their domestic law.

Italy

In Italy, proposals have been put forward to replace the current tax rules with ATAD compliant legislation in the areas of corporate interest deductions, exit and entry tax rules, anti-hybrid legislation and controlled foreign company (CFC) provisions. It is considered that Italian law is already compliant with the ATAD's general anti-avoidance rules and no domestic law changes are proposed. Once enacted the new rules are expected to apply from 2019 for calendar year taxpayers.

Ireland

On 9 October, Ireland introduced the 2019 Irish Budget, which confirmed Ireland's adoption of a number of measures under the ATAD in Finance Bill 2018, including the introduction of the EU ATAD exit tax and CFC regime.

The Irish minister for finance announced that the exit tax took effect for deemed disposal events on and from 10 October 2018. Whilst the adoption of the exit tax was earlier than the required deadline for implementation under ATAD, being 1 January 2020, the minister commented that the early introduction of this measure will provide certainty to businesses currently located in Ireland and to those considering investing in Ireland in the future. The regime will tax unrealised capital gains on capital assets where:

- there is a transfer of assets by a company resident in a member state from an Irish permanent establishment to another territory;
- there is a transfer by a company resident in a member state of a business carried on by a permanent establishment in Ireland to another territory; or
- a company ceases to be tax resident in Ireland.

The exit tax is at the same rate as the Irish corporation tax rate on trading profits (12.5%), which will be widely welcomed as this was a key concern raised by industry and practitioners in consultations. There are, however, specific anti-avoidance measures which would deny the 12.5% rate where the charge arises as part of a broader transaction designed to dispose of the asset where a gain would otherwise be taxable at a rate of 33% (the capital gains tax rate).

Ireland has confirmed that it will introduce ATAD complaint CFC rules in Finance Bill 2018 to take effect for periods beginning on or after 1 January 2019.

France

The 2019 France Budget released on 24 September reforms the current French interest deductibility limitation rules in an effort to comply with the ATAD. The proposed reforms would apply to periods beginning 1 January 2019 and would aim to simplify the existing regulations.

The new rules would limit the deductibility of net interest expenses to the higher of €3m or 30% of the company's adjusted EBITDA.

The rules would include a safe harbour provision to allow a deduction of 75% of the net interest expenses exceeding the higher of the abovementioned thresholds provided that the company can demonstrate that its equity-to-asset ratio is at least equal to a similar ratio computed at the level of the consolidated group to which it belongs.

Should the company exceed a specific 1.5 debt-to-equity ratio however, the safe harbour rules would not apply and the net interest expenses would only be deductible to the extent they do not exceed €1m or 10% of the company's adjusted EBITDA.

The Netherlands

On 18 September, the Dutch government presented the 2019 Dutch Budget proposing significant modifications to the taxation of multinational companies. Specifically, the Budget proposed rules surrounding earnings stripping, CFCs, and exit tax. A proposal to abolish the current 15% Dutch withholding tax on dividend distributions as of 1 January 2020 has meanwhile been withdrawn. The Dutch government has reiterated that it may introduce a conditional withholding tax on intercompany interest and royalty payments to related companies which are tax resident in low tax jurisdictions (tax rate less than 7%), countries blacklisted by the EU and artificially imposed intermediary companies as of 2021.

Pursuant to the Dutch proposals for the implementation of earning stripping rules, net interest payable will only be deductible up to 30% of the taxpayer's EBITDA or €1m, whichever is higher. The non-deductible interest can be carried forward indefinitely to subsequent years. Together with the introduction of these rules, several other interest deduction limitation rules will be abolished.

The CFC measures will be introduced to combat tax avoidance via low-taxed controlled foreign companies or permanent establishments, whereby passive income is shifted to these entities. Under the CFC rules, a foreign entity (or permanent establishment) is considered a CFC if the Dutch taxpayer has a direct or indirect interest of more than 50% of the votes or value in that foreign entity and the tax rate in that jurisdiction is less than 7%. The CFC income is included in the Dutch taxpayer's taxable income and taxed on a current basis.

The Dutch government considers the Dutch exit taxation rules to be generally in line with the ATAD guidance. Accordingly, only a minor change is proposed to bring the current ten-year deferral period provided to pay the exit tax, in line with the five-year deferral period prescribed by the ATAD.

Multilateral instrument updates

Following the deposit of their instruments of ratification, the MLI enters into force as of 1 October in respect of New Zealand, Serbia, Sweden and UK.

The OECD announced on 27 September that four more jurisdictions (Australia, France, Japan and Slovakia) have deposited their instruments of ratification or acceptance for the MLI. The MLI will enter into force for all four jurisdictions 1 January 2019.

Geopolitics: Brexit, the US and trade deals

I end this month with a final word on the broader geopolitical landscape and what I anticipate may be a teaser for next month's column. In the UK, we approach (yet another) 'crunch week' in the Brexit negotiations, where we (once again) face the prospect of a 'no deal' Brexit. To the extent that we do have an announcement on the Brexit deal – or lack of – in the next couple of weeks, I will update you on the possible tax implications.

Further afield, Canada and the US have reached an agreement on a trade deal, known as the United States/Mexico/Canada Agreement (USMCA), which should take effect in late 2019 or 2020, replacing the North American Free Trade Agreement (NAFTA). The USMCA provides some clarity on significant trade issues that have been in limbo, particularly for the dairy and automotive industries.

Finally, we are starting to see the release of regulations relating to last year's US tax reform: GILTI regulations were published on 10 October, and in the run up to its first anniversary, further publications are expected. We have heard anecdotal evidence that some multinationals have been waiting for the detail of the regulations before implementing restructuring, so this may now trigger some potentially significant announcements, which I will of course cover in future editions if indicative of broader trends. ∎

For related reading visit www.taxjournal.com

- Tax reform in the digital economy: recent OECD and EC activity (Murray Clayson, 4.4.18)
- The UK's emerging response to the EU's ATAD (James Taylor, 26.7.18)
- Interpreting double tax treaties in light of the BEPS multilateral instrument (Jeremy Webster & Jamie Robson, 31.8.17)