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Briefing

International review for February

Speed read

The US continues to dominate international tax headlines this month, with new executive orders and draft Bills on tax. The EC has published its work programme for 2025, giving an indication of the direction of travel on European tax policy. The CJEU has ruled in favour of the taxpayer in C-601/23 regarding the compatibility of the Spanish dividend withholding tax with EU law. India has presented its Union Budget with proposals impacting Multinational Enterprises and Canada has confirmed that the increase in the capital gains inclusion rate will now be deferred until 1 January 2026.

Tim Sarson
KPMG
Tim Sarson is a Tax Partner at KPMG and the UK Head of Tax Policy. He has worked in the international tax and transfer pricing field since 1998, in both practice and industry. Email: tim.sarson@kpmg.co.uk.

US tax update

Presidential Memorandums on tax

At the time of writing my January 2025 update, President Trump had just issued a Memorandum to the Secretary of the Treasury withdrawing US support from the OECD 'Global Tax Deal' and giving officials 60 days (approximately until 20 March 2025) to draw up retaliatory measures against countries applying levies on US headquartered groups that are 'extraterritorial or disproportionately affect American companies'.

On 20 January 2025 President Trump issued another Memorandum entitled 'America First Trade Policy', that instructs a separate investigation into whether 'any foreign country subjects United States citizens or corporations to discriminatory or extraterritorial taxes pursuant to section 891 of title 26, United States Code'. Section 891 states that when the President declares there is such discrimination, he can double the US tax rates applicable to each citizen and corporation of the foreign country in question, without the need for congressional approval. The Memorandum states that the conclusions of this investigation must be outlined in a report to be delivered to the President by 1 April 2025.

'Defending American Jobs and Investment' Act

On 21 January 2025, House Ways and Means Committee Chairman Jason Smith (R-MO), along with every Ways and Means Committee Republican, introduced H.R. 591, the 'Defending American Jobs and Investment Act'. In a statement alongside the introduction of the Bill, Chairman Smith indicated that it was intended to reinforce President Trump's 'Global Tax Deal' Memorandum. The Bill would impose a 5% addition to the tax rate each year for four years on the U.S income of individuals and entities located in a foreign jurisdiction that imposes a discriminatory or extraterritorial tax, such as an undertaxed payments rule (UTPR) or digital services tax (DST). After four years, the cumulative 20% additional tax would be imposed each year the targeted tax remains in effect.

The Bill is almost identical to H.R. 3665, Bill with the same title introduced by Chairman Smith in May 2023, although the text has now been revised to provide that individuals and entities located in a foreign jurisdiction imposing a targeted tax would also be denied the benefit of reduced withholding taxes under any treaty obligation of the US. Thus, under the revised Bill, the additional tax would be imposed on top of the 30% withholding tax imposed under ss 1441 and 1442 (or 15% under s 1445 on dispositions of interests in US real property).

Note that this latest Bill is in addition to the 'Unfair Tax Prevention Act' (UTPA) that Republican members of the Ways and Means Committee introduced in July 2023. This Bill would increase the US base erosion and anti-abuse tax (BEAT) where foreign countries adopt the UTPR.

Budget reconciliation update

On 13 February 2025, the House of Representatives Budget Committee approved the 2025 budget resolution. The resolution includes instructions allowing the House Ways and Means Committee to increase the deficit by up to $4.5 trillion over fiscal years 2025–2034 in a possible future 'budget reconciliation' Bill.

The budget reconciliation procedure allows tax legislation to be passed with only a simple majority vote in the Senate without being subject to a filibuster, i.e. the process would allow Republicans to pass tax legislation with little or no support from the Democrats in the Senate. Budget reconciliation has been routinely used by both parties to enact tax legislation when one party is in control of Congress and the White House. Recent examples include the Tax Cut and Jobs Act (TCJA) 2017 and the Inflation Reduction Act 2022.

However, a budget reconciliation Bill can only be assembled after both the House and the Senate pass identical budget resolutions. One may think that Republican control of both chambers of Congress would make this a straightforward process: however, the Senate has approved a different budget resolution to the House.

The House resolution would provide for a large reconciliation Bill that could address both the expired TCJA tax cuts and scheduled business tax increases, as well as other border security, defence, and energy initiatives. By contrast, the budget resolution proposed by the Senate Budget Committee provides for more limited reconciliation legislation for non-tax initiatives, leaving the TCJA and other tax issues for a second reconciliation Bill at a later date.

President Trump has stated his preference for a single Bill, but he has largely left Congress to decide on the approach. It remains to be seen which approach will prevail, but we should hopefully not have to wait long to find out. Only one budget reconciliation Bill can be passed per US fiscal year, so Republicans will be motivated to pass a Bill by the 30 September fiscal year end.

European Commission's work programme 2025

On 11 February 2025, the European Commission published its work programme for 2025 outlining its ambition to boost competitiveness, enhance security and bolster economic resilience in the EU.

The work programme suggests that there are currently no specific plans for the EC to put forward new tax proposals: instead the focus seems to be on simplifying existing EU tax legislation and reducing administrative burdens for business. Key takeaways from a direct tax perspective are:

- Establishment of a '28th legal regime': This initiative aims to create a unified legal framework that would apply across the entire EU, operating alongside the 27 national legal systems. It will seek to simplify compliance for businesses, particularly new and growing businesses, and reduce

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administrative burdens of operating across multiple Member States. It will offer a single set of rules in areas such as corporate law, insolvency procedures, labour regulations and tax law. More details are expected to be published in the course of an Innovation Act proposal that the Commission will present later in its mandate.

- Announcement of 'Omnibus simplification packages': These aim to reduce reporting burdens by 25% for all companies and 35% for SMEs. The communication notes that the first two omnibus packages on 'sustainability' and 'investment simplification' are to be issued in the first quarter of 2025, but it does not refer specifically to any direct tax measures in this context.
- Clean Industrial Deal initiative: The work programme announces the Clean Industrial Deal initiative aiming to boost industrial competitiveness while supporting decarbonisation. This will include the development of a new State Aid Framework to accelerate the roll-out of renewable energy, strengthen industrial decarbonisation and ensure sufficient manufacturing capacities for clean tech. The Clean Industrial Deal initiative is expected to be published in the first quarter of 2025.
- Update on proposed Directives: The work programme notes that the proposal for a revised Interest and Royalties Directive from 2011 has been deemed obsolete in light of the EU Minimum Tax Directive.

  Previous Directive proposals including the Directive on Administrative Cooperation (DAC) 9, Business in Europe Framework for Income Taxation (BEFIT), Transfer Pricing Directive, Debt-Equity Bias Reduction Allowance (DEBRA), 'Unshell' (preventing misuse of shell entities for tax purposes), Digital Services Tax proposal, Significant Digital Presence proposal, and the Financial Transaction Tax continue to be listed as pending files.
- Anti-Tax Avoidance Directive (ATAD): Evaluation of ATAD is scheduled to be finalised in the fourth quarter of 2025 (previously expected in the third quarter of 2025).

CJEU decision on withholding tax on dividends

On 19 December 2024, the CJEU rendered a decision in Case C-601/23, addressing the compatibility of the Spanish dividend withholding tax with EU law.

The case concerned a UK-based company with no permanent establishment in Spain (the plaintiff) that received a €2.7m dividend from a company based in the Basque Country. The dividend was initially subject to a 19% withholding tax (WHT) that was ultimately reduced to 10% under the Spain/UK tax treaty.

Prevailing Spanish legislation at the time treated WHT on dividends as a final tax for non-resident companies, with no available reimbursement mechanism in the event the recipient ultimately reported a tax loss for the period. Resident companies on the other hand could treat the WHT as an advance payment on account of corporate income tax (CIT), which would be reimbursed if the company reported a tax loss for the period.

The plaintiff argued that, as a loss-making company, it was unable to offset the tax withheld in Spain against its UK tax liabilities. In light of the difference in treatment compared to a local resident, the plaintiff claimed the Spanish rules constituted a breach of the free movement of capital under Article 63 of the Treaty on the Functioning of the European Union (TFEU).

The CJEU agreed with the plaintiff that the more favourable treatment of dividends for resident companies constituted an unjustified restriction on the free movement of capital under Article 63. The CJEU noted that it is settled case law that a difference in treatment is only compatible with Article 63 if it concerns situations that are not objectively comparable or where it can be justified by an overriding reason in the public interest. The CJEU rejected Spain's justifications for the difference in treatment, including the effective collection of tax, balanced allocation of taxing rights, and maintaining tax system cohesion.

The CJEU's decision is broadly in line with the previous case law on the taxation of outbound dividends, and opens the door for refund claims by loss making non-resident companies subject to WHT in Spain during previous periods.

Indian Budget 2025/26

On 1 February 2025, India presented its Union Budget for 2025/26. Notably the Budget did not propose changes to corporation tax rates, nor provide any update on India's implementation of Pillar Two. The key tax announcements of which MNEs should be aware are:

- Presumptive taxation for non-residents: A presumptive taxation scheme is proposed for non-residents engaged in the business of providing services or technology to a resident company establishing/ operating an electronics manufacturing facility/ connected facility for manufacturing electronic products in India. A sum equal to 25% of the aggregate amount received/ receivable by the non-resident will be deemed as profits of such non-resident chargeable to tax in India. The proposal will also cover the provision of technical personnel by the non-resident.
- Rationalisation of transfer pricing provisions: Taxpayers are to be provided an option to apply the arm's length price determined for a transaction in a given year to the subsequent two years for similar transactions. The scope of transfer pricing safe harbour rules is also to be expanded to provide certainty on arm's length computation of international transactions and reduce underlying litigation. Detailed rules will be released in due course.
- Amendment to 'significant economic presence' (SEP) definition: Broadly, SEP provisions are applicable to non-residents that are engaged in transaction of goods and services in India exceeding c£190,000 in financial year. Effective from FY 2025/26, SEP provisions would not apply to non-residents who are involved in purchase of goods in India for the purpose of export.

Canadian increase to capital gains tax deferred to 2026

Last month, I reported that the prorogation of the Canadian parliament until 24 March 2025 had left taxpayers uncertain regarding the status of various Canadian tax policy proposals. One such measure was the increase in the capital gains inclusion rate from half to two-thirds for corporations, trusts and individuals on the portion of the capital gains realised in the year that exceeded $250,000 that was to take effect from 25 June 2024. On 31 January 2025, Canada confirmed that taxpayers will not be required to account for the proposed capital gains inclusion rate increase in their upcoming 2024 tax filings, and that implementation of this measure will now be deferred to 1 January 2026. ■

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