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International Tax News

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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.

Featuered articles

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Costa Rica

Costa Rica tax reform includes new VAT and capital gains tax on share transfers in Costa Rican entities

Law No. 9635, which recently was approved and published in the Costa Rican Official Gazette, provides major tax reform. Among other tax measures, the Law replaces the existing sales tax with a new value-added tax (VAT) and introduces a new capital gains tax on the transfer of shares in Costa Rican companies. The entry into force of the provisions in this Law varies, but most occur on July 1, 2019.

Please see our **PwC Insight** for more information.

PwC observation:

Multinational entities (MNEs) with current or planned operations in Costa Rica should consider how they might be impacted by the new VAT and capital gains tax on share transfers. MNEs still have time to assess that impact and respond, since generally most provisions do not enter into force until July 1, 2019.

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France

France introduces additional GAAR regulations

Under current tax provisions, the French domestic general anti-abuse rules (GAAR) disregards any legal arrangement which is ‘artificial’ and/or seeks to benefit from a literal application of legal provisions or decisions while contradicting the objective of such provisions. Such an arrangement is considered to be motivated by the sole purpose of avoiding or alleviating the taxpayer’s tax burden. The domestic GAAR applies to all kinds of transactions and taxes.

The corresponding tax reassessments could be subject to an 80% penalty for abuse of law. In this case, the audit file would be automatically transferred to the office of the public prosecutor based on a new law against tax fraud, which was enacted at the end of October 2018.

In addition to the introduction of the EU anti-tax avoidance directive (ATAD) GAAR, the Finance Bill for 2019 extends the domestic GAAR which would also apply to fraudulent arrangements if their main purpose, or one of the main purposes is tax-driven (i.e., artificial arrangements should not be covered by this new rule). In this particular case, the 80% penalty would not apply. The new domestic GAAR should apply for operations carried out as of January 1, 2020.

PwC observation:

Whether the definition of abuse used in the EU ATAD GAAR, in the OECD’s multilateral instrument (MLI) and the French domestic GAAR will be unified has not yet been clarified. Furthermore, the guidelines from the French Tax Authorities on this issue have not been published yet.

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Germany

German government passes 2018 tax bill

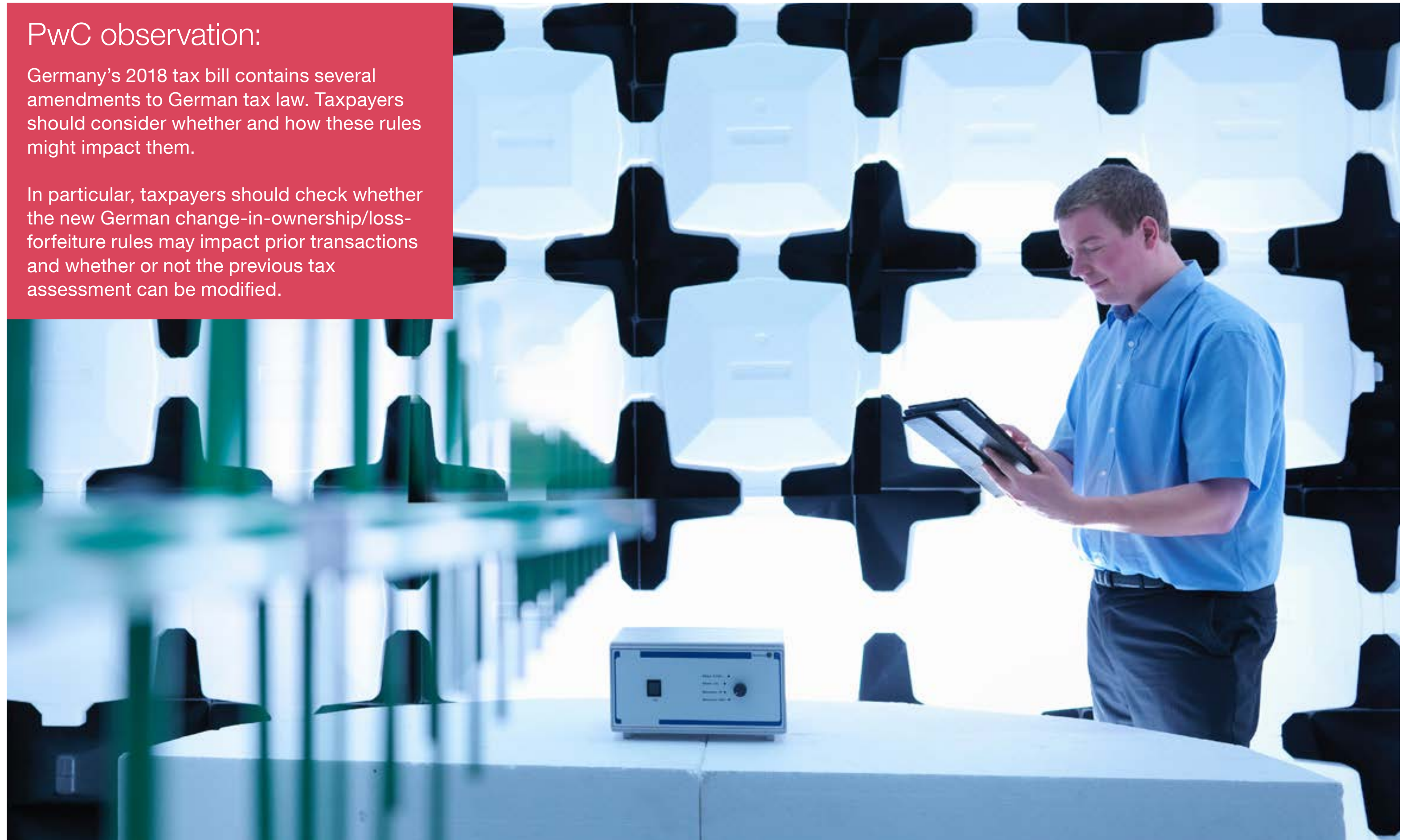
The German Federal Parliament and the German Federal Council recently passed a tax bill that is commonly referred to as the '2018 tax bill.' The 2018 tax bill includes the following changes in German tax law: (i) extending non-resident capital gains taxation treatment to shares in foreign 'real estate-rich' corporations; (ii) narrowing the German change-in-ownership rules/loss-forfeiture rules; and (iii) the acceptance of variable compensatory payments for outside shareholders in a German organschaft subsidiary based on the subsidiary's profits.

Please see our **PwC Insight** for more information.

PwC observation:

Germany's 2018 tax bill contains several amendments to German tax law. Taxpayers should consider whether and how these rules might impact them.

In particular, taxpayers should check whether the new German change-in-ownership/loss-forfeiture rules may impact prior transactions and whether or not the previous tax assessment can be modified.



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Gibraltar

Income Tax Act 2010 - Taxation of movable property

Following the publication of the Income Tax (Amendment) Act 2010, on November 22, 2018, any non-trading rental income arising from movable property located outside Gibraltar is automatically deemed to accrue in and derive from Gibraltar, and is therefore taxable under the Act if the income has been received or is receivable by a company that is registered in Gibraltar.

The amendment was enacted under a new Class 3B of Schedule 1 Heads of Charge.

The amendment applies immediately and was introduced for the purposes of satisfying EU requirements.

PwC observation:

Multinational entities (MNEs) with companies registered in Gibraltar should assess any impact, since the amendment is already applicable.

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Hong Kong

Ordinance related to (1) environmental protection installations and (2) qualifying debt instruments gazetted

Inland Revenue (Amendment) (No. 9) Ordinance 2018 (the 'ordinance') was gazetted on November 23, 2018. The Ordinance proposes, among others, the following tax measures:-

1. 100% immediate deduction for specified capital expenditure on environmental protection installations (EPIs)
   The tax deduction period for capital expenditure incurred on EPIs will be changed to allow for a 100% immediate deduction in the year of acquisition. Previously, the tax deduction period for capital expenditures incurred on EPIs was over five consecutive years from the year of purchase. The accelerated tax deduction is effective from the year of assessment 2018/19.

2. Expansion in scope-of-profits tax exemption for qualifying debt instruments (QDIs)
   In order to promote the development of the Hong Kong bond market, the scope-of-profits tax exemption for QDIs will be expanded to cover:

- QDIs with any maturity period that are issued on or after April 1, 2018; and
- QDIs listed on the Hong Kong Stock Exchange that are issued on or after April 1, 2018.

The ordinance also contains new/amended sections that address the treatment of loss sustained from a transaction with or related to QDIs.

PwC observation:

The passage of the ordinance reflects the Hong Kong government's continuous effect in encouraging the wider use of environmental friendly installations by businesses and strengthening the development of the bond market in Hong Kong.

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Hong Kong

Proposed changes to Hong Kong's profits tax exemption for funds

The Inland Revenue (profits tax exemption for funds) (Amendment) Bill 2018 (the bill) was gazetted on December 7, 2018. The bill clarifies some initial uncertainties, for instance the impact of the changes to non-fund entities (their tax treatment will remain unchanged and the previously applicable profits tax exemption regime will continue to operate separately), and Hong Kong privately offered open-ended fund companies.

In summary, the bill introduces the following provisions:

1. unification of the profits tax exemptions for privately offered funds (onshore or offshore, regardless of their structure, location of central management and control, their size, or the purpose they serve) into one comprehensive regime

2. wider application scope of the profits tax exemption to put Hong Kong in a much more competitive position as a regional and international asset and fund management center

3. removal of the 'tainting' effect where a profits tax exemption would still be available for the 'good' transaction of the fund, even if the fund carries out 'bad' transactions.

Upon passage of the bill, the proposed changes to the Hong Kong's profits tax exemption for funds will be effective on April 1, 2019.

PwC observation:

The bill fundamentally changes Hong Kong's profits tax exemption for funds and significantly reduces the current tax uncertainty faced by the private equity, venture capital and real estate funds.

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Ireland

ATAD implementation

Ireland recently issued draft legislation to implement two ATAD measures, CFC rules and an exit tax. Additionally, Ireland has taken steps to determine the manner in which the remaining two ATAD measures (interest limitation and anti-hybrid rules) will be implemented through launch of a public consultation. The public consultation closes on January 18, 2019. Ireland is already compliant with the final ATAD measure as wide-ranging general anti-abuse rules (GAAR) are contained within existing legislation. We have included a high-level overview of some of the developments below.

CFC rules

Detailed in Finance Bill 2018, the aim of the CFC regime is to counteract base erosion and profit shifting by multinational groups that use group companies located in low- or no-tax jurisdictions and where a significant part of the business is carried on in Ireland. The Irish CFC rules effectively treat a CFC company's income as taxable in Ireland regardless of whether there was an actual distribution to the Irish company. The impact of the CFC charge is to ensure tax is paid where the significant people functions are located.

Exit tax

Ireland introduced an exit tax with an October 10, 2018 effective date. The introduction of the tax was not included in an advance publication prior to Budget day (the Corporation tax Roadmap) and its introduction was not expected until January 1, 2020. Under the new rules, an exit tax charged at a 12.5% rate will apply to many situations including:

- where assets are transferred by an Irish PE to its foreign head office or foreign PE
- where a business is transferred from an Irish PE to its foreign head office or foreign PE
- where a company migrates its residence out of Ireland.

This represents an expansion on the previous exit tax rules. The tax will apply to gains on deemed disposals arising in these scenarios. Additional guidance is expected to be issued on the exit tax's operation in early 2019. Helpfully, the exit tax has been set at 12.5%, rather than the standard capital gains tax rate of 33%.

Interest limitation rules - existing rules being regarded as 'equally effective'

Article 4 of the ATAD requires Member States to introduce interest limitation rules that must be transposed into national law by December 31, 2018. However, under Article 11 of the ATAD, Member States that have existing rules for preventing base erosion and profit shifting risks which are 'equally effective' to the interest limitation rule set out in ATAD may continue to apply these targeted rules until the earlier of:

- the end of the first full fiscal year following the date of publication of the agreement between the OECD members on the official website on a minimum standard with regard to BEPS Action 4, or
- January 1, 2024.

The European Commission, on December 7, 2018, published a notice regarding which Member States are considered to have existing interest limitation legislation in place that is deemed 'equally effective' to the rule as set out in the ATAD. That notice included Greece, France, Slovakia, Slovenia and Spain.

The Irish government has previously stated that it regards the existing interest limitation rules as 'equally effective' to the proposed ratio-based rules under ATAD. The government notified the European Commission of its intention to avail of the derogation to the introduction of the BEPS Action 4 minimum standard or at the latest, until 2024. Ireland's omission from the December 7 notice means that the Irish Department of Finance will continue negotiations with the European Commission. Ireland aims to demonstrate that their interest limitation rules are 'equally effective' as the rules as set out under ATAD Article 4. Despite no further clarity on the timing of the introduction, MNEs should consider modeling the impact of a new interest limitation rule before 2024.

PwC observation:

The ongoing evolution of the international tax landscape has necessitated the implementation of various new rules as outlined under the BEPS project. The ATAD and has resulted in updates to existing Irish tax legislation. Ireland is committed to targeting base erosion and profit shifting as evidenced by its participation in the debate on the agreement of the proposed rules and their implementation. As expected during the implementation phase, the creation and introduction of new rules has resulted in additional discussion. However, by launching a consultation process to consider views on the implementation, the Irish government seems to be seeking a fair implementation of the new rules.

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Japan

Japan FY2019 tax reform proposals

The FY2019 tax reform proposals submitted by the government's ruling party were issued on December 14, 2018. These proposals will be submitted to the Japanese parliament (Diet) in early 2019. With regard to international taxation, the tax reform proposals include:

1. expansion of the earnings stripping rules to restrict interest deductions in accordance with BEPS Action Plan 4
2. revisions to the transfer pricing rules in accordance with BEPS Action Plan 8 and
3. revisions to the CFC rules.

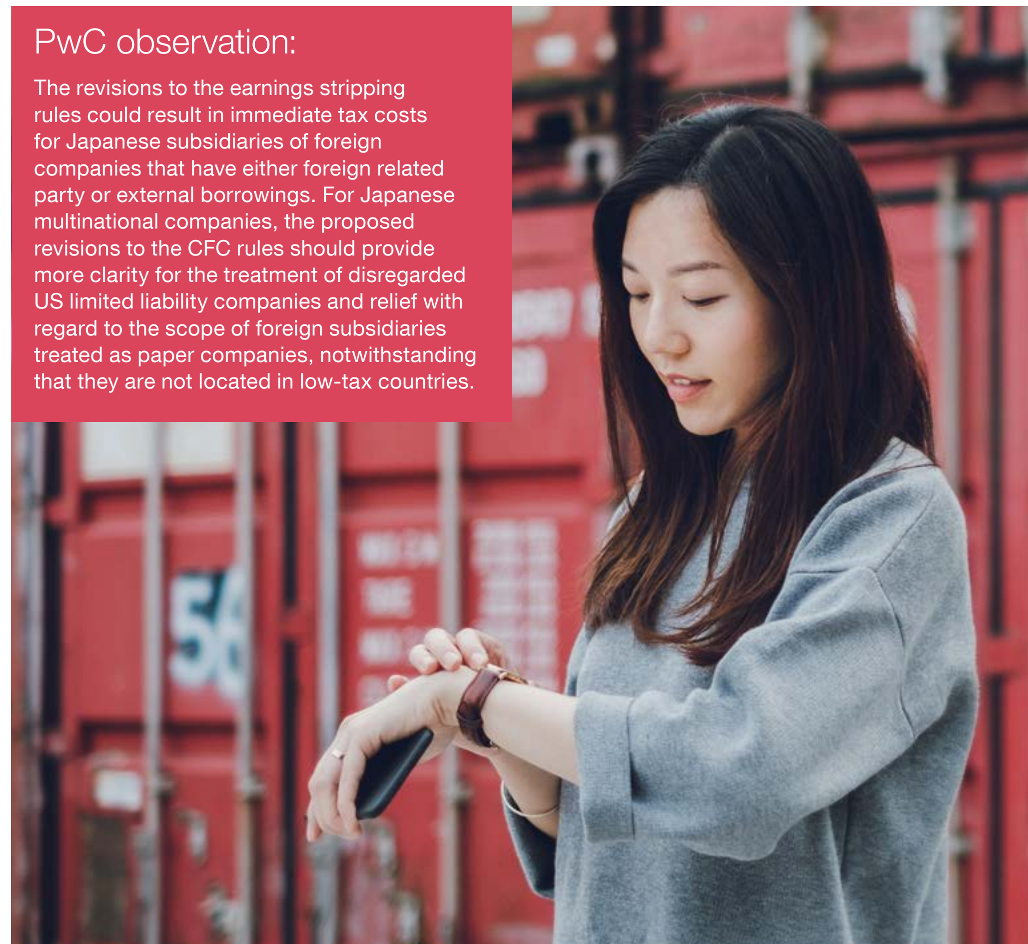
Under the existing earnings stripping rules, if net interest expense to related parties exceeds 50% of (as defined) adjusted income, the excess is treated as non-deductible (although it may be carried forward for up to seven years). Under the 2019 tax reform proposals, the scope of interest expense will be expanded to include interest paid to non-related parties. However, interest expense, either subject to Japanese taxation in the hands of the income recipients, or where paid to qualifying public service corporations, is specifically excluded. Specific rules will apply to interest on bonds and interest expense arising from back-to-back repos. Further, the threshold ratio will be significantly reduced from 50% to 20% of adjusted income. These revisions are scheduled to apply to fiscal years beginning on or after April 1, 2020.

The transfer pricing rules will be revised to (i) mandate the use of the discounted cash flow method for the valuation of intangible assets where no comparable unrelated pricing is available, and (ii) introduce a 'commensurate with income' concept for purposes of determining the arm's length price for hard-to-value intangibles. These revisions are scheduled to apply to fiscal years beginning on or after April 1, 2020.

Under the current CFC rules, the treatment of a foreign subsidiary that is a member of a consolidated tax group or treated as a pass-through entity under local tax law is unclear. In addition, as a result of the FY2017 and FY2018 tax reforms, all income of a foreign subsidiary that falls within the definition of a 'paper company' (in general, a company without business substance) is subject to CFC taxation unless its effective tax rate is 30% or more. The CFC rules will be revised to (i) clarify the calculation of the effective tax rate of a foreign subsidiary that is a member of a consolidated tax group or treated as a pass-through entity, and (ii) exclude certain foreign subsidiaries from the definition of 'paper company.' These revisions are scheduled to apply to fiscal years of a Japanese company ending on or after April 1, 2019 with respect to foreign subsidiary fiscal years beginning on or after April 1, 2018.

PwC observation:

The revisions to the earnings stripping rules could result in immediate tax costs for Japanese subsidiaries of foreign companies that have either foreign related party or external borrowings. For Japanese multinational companies, the proposed revisions to the CFC rules should provide more clarity for the treatment of disregarded US limited liability companies and relief with regard to the scope of foreign subsidiaries treated as paper companies, notwithstanding that they are not located in low-tax countries.



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Korea

South Korea tax law changes

On December 8, 2018 the Korean National Assembly approved changes to Korean tax laws. The changes were mainly consistent with the government's proposals announced in August 2018. The main tax law changes that Korean inbound investors should be aware of include:

- **Extension of statute of limitation period**: The statute of limitation period for tax purposes (except for cases of fraud) is generally five years for under-reporting and seven years for non-reporting. Under the revised tax laws, the statute of limitation period has been extended to 10 years for offshore transactions that include cross-border related party transactions.
- **Changes to the permanent establishment definition:** Consistent with the recommendations made by the OECD as part of the BEPS Action 7, changes were made to the domestic definition of PE to narrow the scope of the preparatory or auxiliary exemption and broaden the scope of the dependent agent PE concept. The scope now includes situations where an agent repeatedly plays a principal role in the course of concluding contracts that are routinely concluded without material modification by the foreign company.
- **Limitation on the utilization of tax losses by branches**: Under previous changes to the tax law the amount of tax losses carried over from prior years that can be utilized by a Korean company for fiscal years starting on or after January 1, 2019 is limited to 60% of the company's current year taxable income. The latest tax law changes mean that the same 60% restriction will apply to Korean branches of foreign companies.
- **Changes to the taxation of Korean source income of overseas investment vehicles (OIVs):** Changes have been made to improve the taxation of Korean-source income of OIVs, including changes to the definition of 'foreign corporation' for Korean tax purposes, rules to clarify the characterization of Korean-source income received by investors in OIVs, and new rules to clarify when an OIV is not viewed as the beneficial owner of Korean-source income when investors receive Korean-source income through an OIV.
- **Abolishment of tax exemptions for foreign direct investment:** Certain qualifying foreign direct investments could previously benefit from individual and corporate tax exemptions for certain high-technology businesses and foreign investors in specially designated areas such as foreign investment zones and free economic zones. Such exemptions have been abolished to be consistent with the OECD BEPS initiative.
- **Expanded scope of electronic services subject to VAT:** If a foreign company provides electronic services to customers in Korea, it should comply with a simplified VAT registration and compliance regime. The latest tax law changes expand the scope of electronic services to include cloud computing, advertising and brokerage services for goods or services. The changes apply to services provided on or after July 1, 2019.

PwC observation:

The tax law changes confirm the Korean government's commitment to drive tax policies that facilitate job creation and innovative growth and also narrow income inequality. The changes also demonstrate the government's commitment to implement the recommendations of the OECD under the BEPS project.

Foreign-invested companies in Korea should assess how the changes may impact them since most of the changes are effective on January 1, 2019. Some supporting details related to the tax law changes are still to be finalized in relevant Enforcement Decrees.

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Luxembourg

Changes proposed to Luxembourg draft law implementing ATAD 1 effective January 1, 2019

Under the EU ATAD 1 published in July 2016, EU Member States have until December 31, 2018 to transpose ATAD 1 into their domestic laws. On June 19, 2018, the Luxembourg government tabled a draft bill (n°7318) (the 'draft law') before the Luxembourg Parliament (Chambre des Députés) that would implement ATAD 1 as Luxembourg domestic law.

On October 5, 2018, the Chamber of Commerce issued extensive comments to the draft law. The State Council also published, on November 13, its comments on the text and expressed a view on areas needing changes or more clarification.

Amendments to the draft law now have been released to meet the modifications required by the State Council. These amendments are minimal, and most of the prior questions and comments remain. This Insight briefly covers significant clarifications or changes versus clerical amendments.

The draft law needs to go through the Luxembourg legislative process. Although changes are not expected, the law may be subject to further amendments before the Luxembourg Parliament final vote.

PwC observation:

These amendments indicate the new Luxembourg government's willingness to formally adopt the draft law before year-end in order to comply with EU requirements.

Companies should consider the upcoming changes, as they may need to take action immediately in order to be effective on January 1, 2019.

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Mauritius

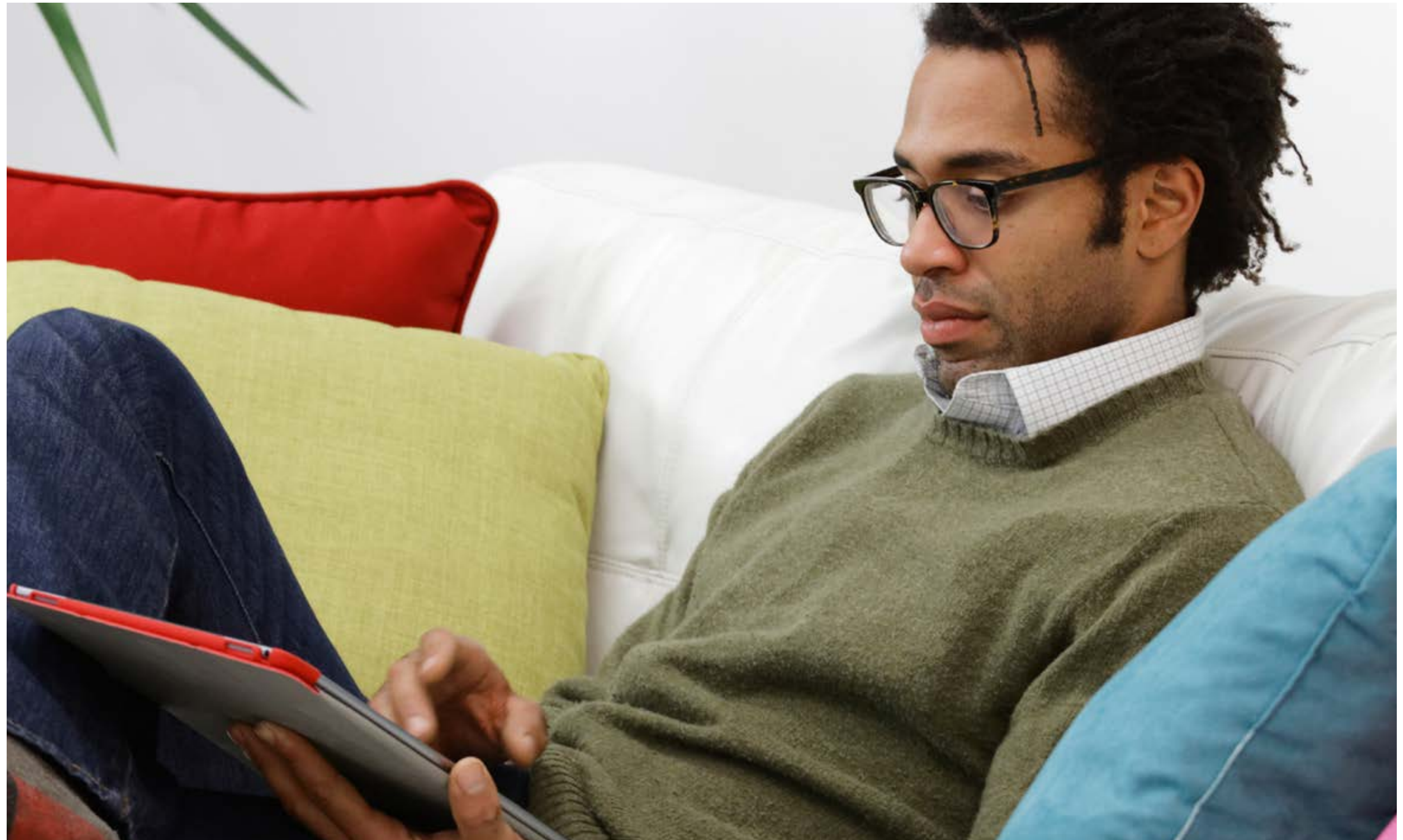
OECD classifies Mauritius tax law regime as non-harmful after changes

Mauritius recently enacted tax reform under Finance Act 2018 in order to comply with the OECD's BEPS initiatives. As a result of these reforms, the OECD concluded on November 13 that Mauritius does not have a 'harmful tax regime.' Also under Finance Act 2018, Mauritius amended its tax law by adopting the place of effective management (POEM) standard. The Mauritius Revenue Authority (MRA) issued a statement of practice (SoP) concerning POEM on November 28.

Please see our **PwC Insight** for more information.

PwC observation:

The OECD's approval of Mauritius as a non-harmful tax regime confirms the country's position as a compliant jurisdiction and aligns with the latest international practices and standards. The MRA's recent guidance on POEM also provides further certainty to foreign investors.



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Mexico

Mexico's proposed elimination of 'universal compensation' would significantly impact businesses

The Mexican Executive branch presented to Congress on December 15 the 2019 Budget ('the Proposed Budget'), which includes the Federal Spending Law (FSL), the Federal Revenue Law (FRL), and changes to the tax law, all with an expected effective date of January 1, 2019. In one significant change for Mexican businesses, the Proposed Budget would eliminate universal compensation, which allows taxpayers to compensate favorable balances and balances due from all Federal taxes.

By law, the Proposed Budget must be approved by Congress no later than December 31, 2018. As the current Executive´s political party controls both houses of Congress, Congress likely will not significantly change the Proposed Budget.

Please see our **PwC Insight** for more information.

PwC observation:

The elimination of universal compensation, and the inability to compensate VAT, excise, and income tax balances going forward, in practice will significantly impact Mexican businesses. Not only will this change affect operating cash flow, but also there may be an increase in the risk of recovery of VAT or excise tax balances from a practical perspective. Multinational businesses should understand how their Mexican subsidiaries are currently compensating their Mexican taxes and the impact this change may have on their Mexican financial result.

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Spain

Spain's draft bill includes ATAD, tax haven provisions

The Spanish Ministry of Finance published three draft bills for public consultation on October 23. Two of these tax bills introduce a financial transactions tax and a digital services tax. The third tax bill introduces measures to prevent tax fraud by transposing some of the provisions contained in the EU's ATAD, transposing the Directive on Tax Dispute Resolution Mechanisms in the EU, and broadening the tax haven definition to align it with EU and OECD standards.

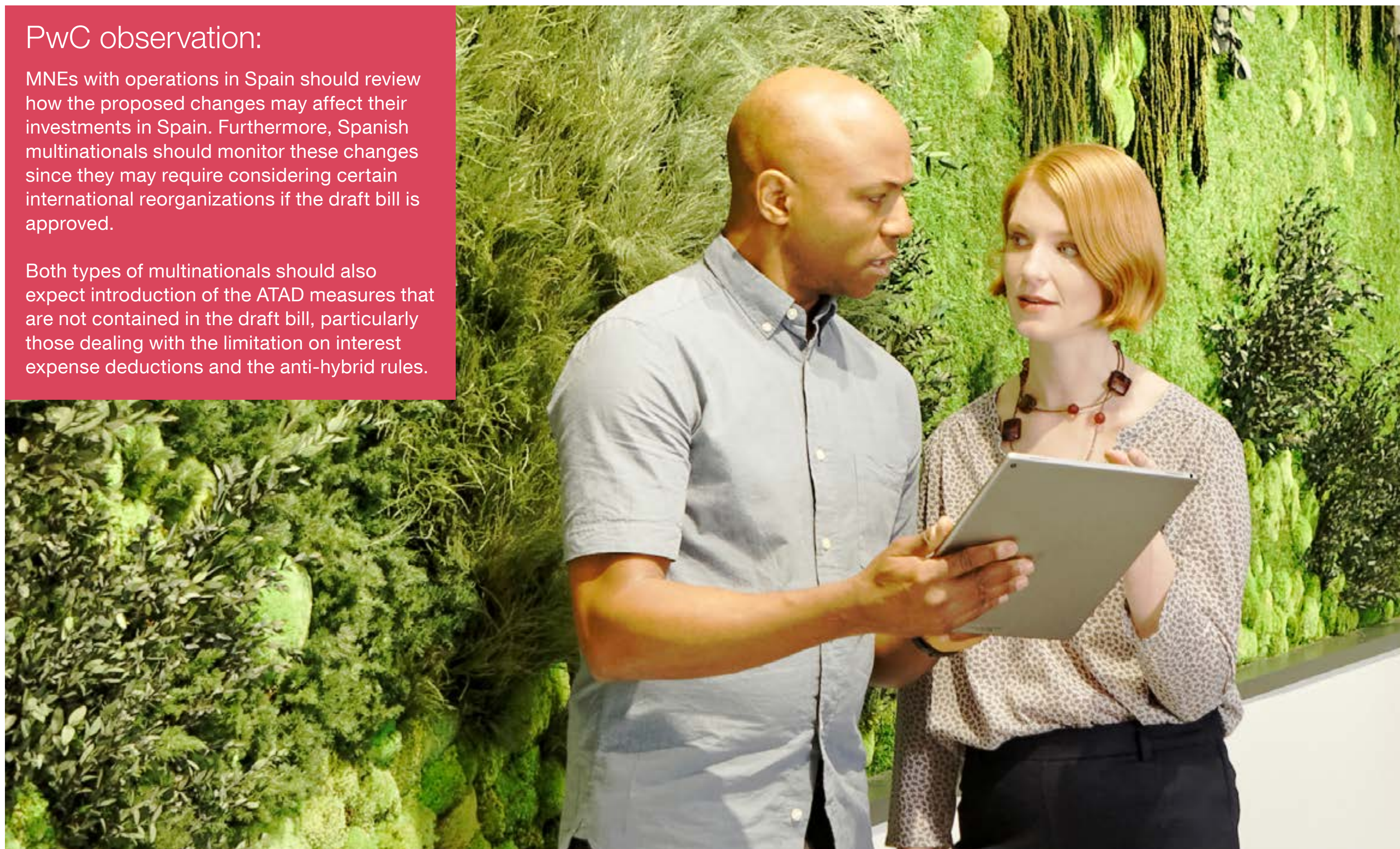
By law, the Proposed Budget must be approved by Congress no later than December 31, 2018. As the current Executive´s political party controls both houses of Congress, Congress likely will not significantly change the Proposed Budget.

Please see our **PwC Insight** for discussion of the most relevant proposed tax amendments contained in the draft bill that aim to prevent tax fraud.

PwC observation:

MNEs with operations in Spain should review how the proposed changes may affect their investments in Spain. Furthermore, Spanish multinationals should monitor these changes since they may require considering certain international reorganizations if the draft bill is approved.

Both types of multinationals should also expect introduction of the ATAD measures that are not contained in the draft bill, particularly those dealing with the limitation on interest expense deductions and the anti-hybrid rules.



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Venezuela

Venezuela increases its large financial transaction tax

The Venezuelan government increased the large financial transaction tax rate from 1% to 2% through Presidential Decree No. 3,654, which was published in the Official Gazette on November 8, 2018. The increase became effective on November 19, 2018.

Please see our **PwC Insight** for more information.

PwC observation:

Venezuelan affiliates of foreign multinational entities that are designated as 'special' by the tax authorities should evaluate how the rate increase could affect their business operations.

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China

China further clarifies the implementation details of WHT deferral treatment on foreign direct re-investment

Recently, China's SAT issued Public Notice [2018] No.53 to clarify some uncertainties around the WHT deferral treatment on foreign direct re-investment.

Under the current China corporate income tax Law, dividends derived by a non-tax resident enterprise (TRE) from China are subject to a 10% WHT in China, unless a more favorable treaty benefit applies. In order to attract foreign investment, in December 2017, China introduced a WHT deferral treatment on direct re-investment by foreign investors using the profits distributed from TREs into China's 'encouraged projects', which was expanded to all 'non-prohibited projects' later in September 2018. The direct re-investment includes capital injection in a new or existing TRE, or acquiring the shares in an existing TRE from third parties.

Subsequent to the enhancement of the above preferential treatment, the SAT issued Public Notice [2018] No.53 (Notice 53) to clarify the implementation details, with the following highlights:

- Increase of paid-in capital or capital reserve by foreign investors could be eligible for the deferral treatment. Notice 53 clarifies that foreign investors who use the profits distributed by the TRE to settle the capital it has committed to pay before can also enjoy the treatment.
- In the past, the dividends had to be transferred from the TRE to the investee / transferor's bank account directly in order to fulfil the conditions for the WHT deferral. Now, Notice 53 clarifies that the condition could also be fulfilled if it is transferred through a special RMB deposit account held by the foreign investor and then to the account of investee / transferor within the same day.
- If the investments are recouped by the foreign investors via equity transfer, equity repurchase liquidation, etc., the deferred WHT shall be repaid. Notice 53 clarifies that the foreign investors enjoy the treaty benefit effective at the time the dividends were distributed.

PwC observation:

Notice 53 also sets out documentation and procedural matters in relation to the application of the preferential treatment. Foreign investors who have cash in China should review their investment plan and consider tax-efficient re-investment options.

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Treasury issues proposed rules under Section 163(j)

Treasury released proposed regulations on November 26 that address the Section 163(j) interest expense limitation rules ('the Proposed Regulations'). The 2017 tax reform act (the Act) revised Section 163(j) ('new Section 163(j)') to generally limit deductions for net business interest expense to 30% of a company's 'adjusted taxable income' (ATI). Prior to release of the Proposed Regulations, the IRS issued Notice 2018-28, which provided initial guidance with respect to certain aspects of Section 163(j), including its application to consolidated groups and the carryforward of a taxpayer's disallowed disqualified interest under 'old' Section 163(j). Notice 2018-28, however, left many questions unresolved for taxpayers applying new Section 163(j).

The Proposed Regulations provide needed guidance related to the mechanics of determining the interest expense limitation. They also clarify the application of Section 163(j) to consolidated groups, RICs, REITs, partnerships, CFCs, and other foreign corporations. The Proposed Regulations do not, however, include rules for coordinating between new Section 163(j) and the base erosion and anti-avoidance tax (BEAT) provisions under Section 59A. Rather, the Proposed Regulations reserve on the interactions of those two Code sections because these issues will be considered in separate guidance under Section 59A. Further, the Proposed Regulations withdrew the 1991 proposed regulations under old Section 163(j) ('the 1991 Proposed Regulations'). Simultaneously with the Proposed Regulations, the IRS on November 26 also released Rev. Proc. 2018-59, which provides a safe harbor allowing taxpayers to treat certain infrastructure projects as real property trades or businesses solely for purposes of qualifying as an electing real property trade or business under Section 163(j)(7)(B).

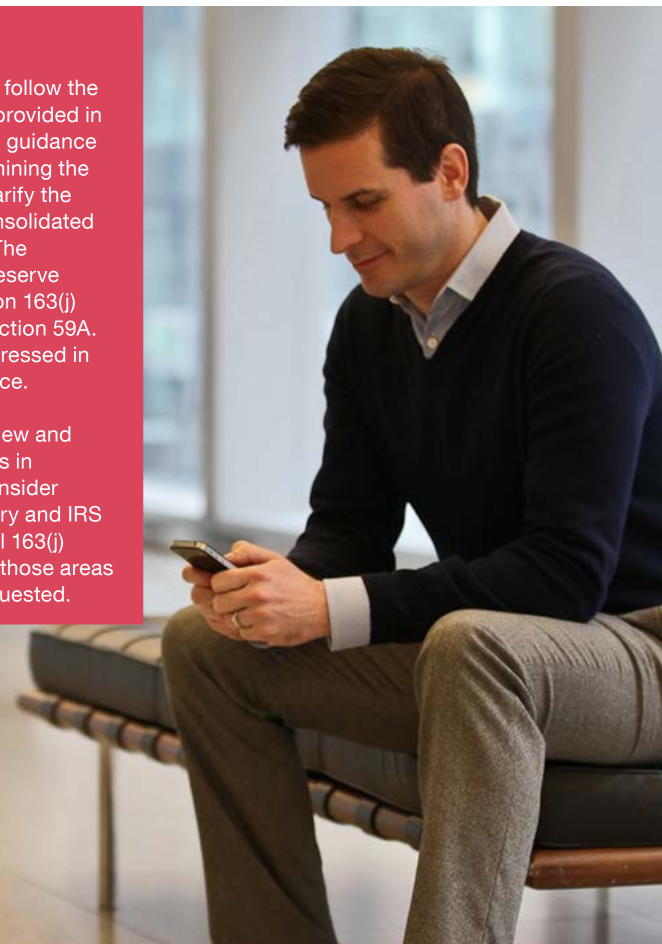
The regulations are proposed to be effective for tax years ending after the date the regulations are published in final form in the Federal Register. However, the regulations state that taxpayers may elect to apply the Proposed Regulations for tax years beginning after December 31, 2017, provided certain conditions are met.

Please see our **PwC Insight** for more information.

PwC observation:

The Proposed Regulations closely follow the previous administrative guidance provided in Notice 2018-28, provide additional guidance related to the mechanics of determining the interest expense limitation, and clarify the application of Section 163(j) to consolidated groups, partnerships, and CFCs. The Proposed Regulations, however, reserve on the interactions between Section 163(j) and the BEAT provisions under Section 59A. That issue is anticipated to be addressed in forthcoming administrative guidance.

Taxpayers should immediately review and assess the impact of the provisions in the Proposed Regulations, and consider commenting on issues that Treasury and IRS should address before issuing final 163(j) guidance, particularly in regard to those areas in which comments have been requested.



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United States

Treasury issues proposed rules related to foreign tax credits

Treasury released proposed regulations (the Proposed Regulations) under Sections 78, 861, 901, 904, 954, 960, and 965 on November 28. The Proposed Regulations are the first form of administrative guidance with respect to the foreign tax credit (FTC) regime following the enactment of the 2017 Act. Of relevance to the Proposed Regulations, the Act limited the FTC for US corporate taxpayers by repealing the indirect credit under Section 902, amending the deemed-paid credit under Section 960, and introducing two new FTC limitation baskets under Section 904.

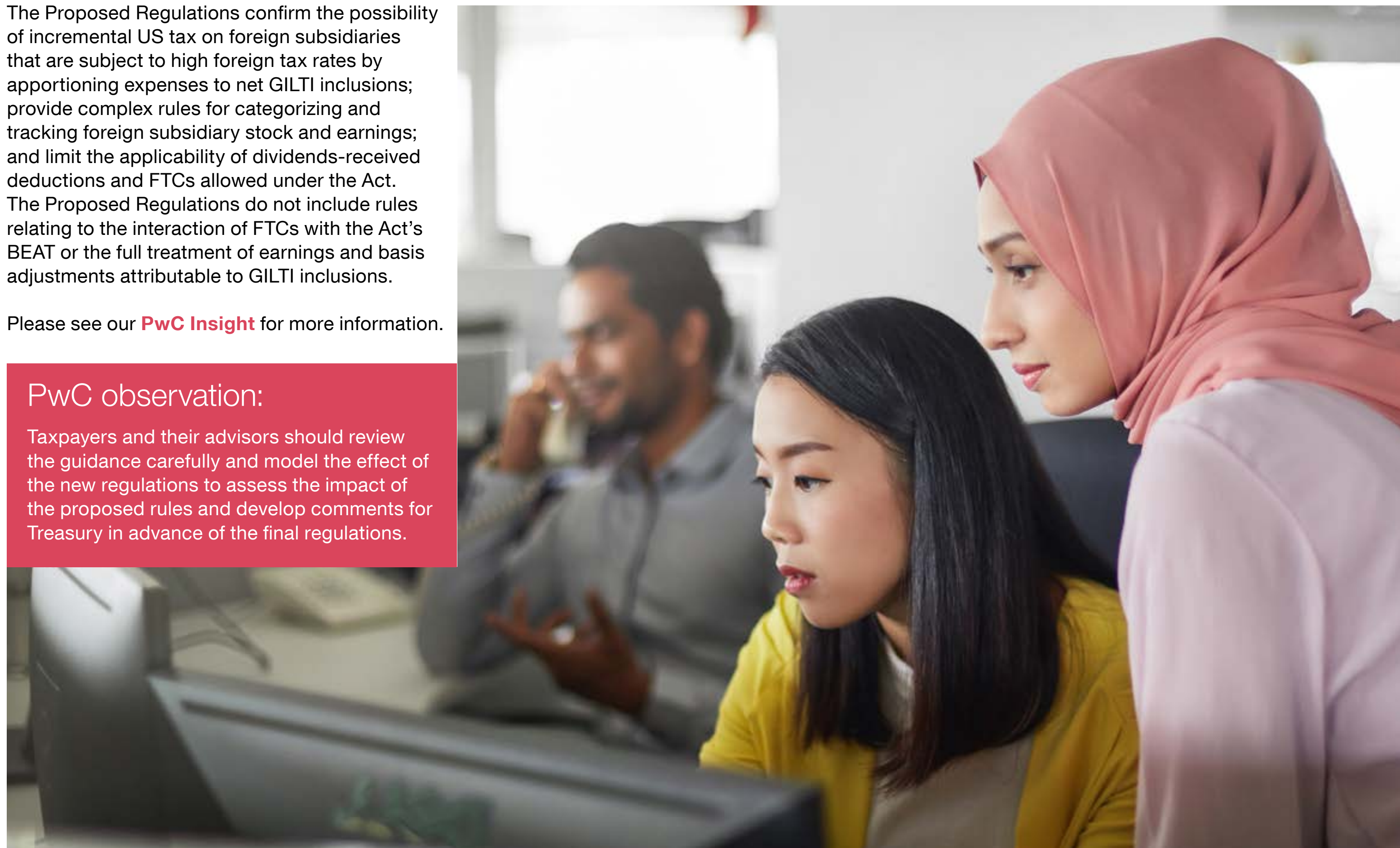
The Proposed Regulations provide needed guidance related to the mechanics of determining the FTC limitation under Section 904 (including the allocation and apportionment of expenses); the scope of the new foreign branch basket; and the extent of deemed-paid FTCs with respect to subpart F and global intangible low-taxed income (GILTI) inclusions.

The Proposed Regulations confirm the possibility of incremental US tax on foreign subsidiaries that are subject to high foreign tax rates by apportioning expenses to net GILTI inclusions; provide complex rules for categorizing and tracking foreign subsidiary stock and earnings; and limit the applicability of dividends-received deductions and FTCs allowed under the Act. The Proposed Regulations do not include rules relating to the interaction of FTCs with the Act's BEAT or the full treatment of earnings and basis adjustments attributable to GILTI inclusions.

Please see our **PwC Insight** for more information.

PwC observation:

Taxpayers and their advisors should review the guidance carefully and model the effect of the new regulations to assess the impact of the proposed rules and develop comments for Treasury in advance of the final regulations.



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Treasury issues proposed BEAT rules

Treasury has released proposed regulations (the Proposed Regulations) for the base erosion and anti-abuse tax (BEAT). The BEAT rules require certain corporations to pay a minimum tax on payments to non-US related parties. The Proposed Regulations, released on December 13, are the first regulatory guidance under new Section 59A, which was enacted by the 2017 Act.

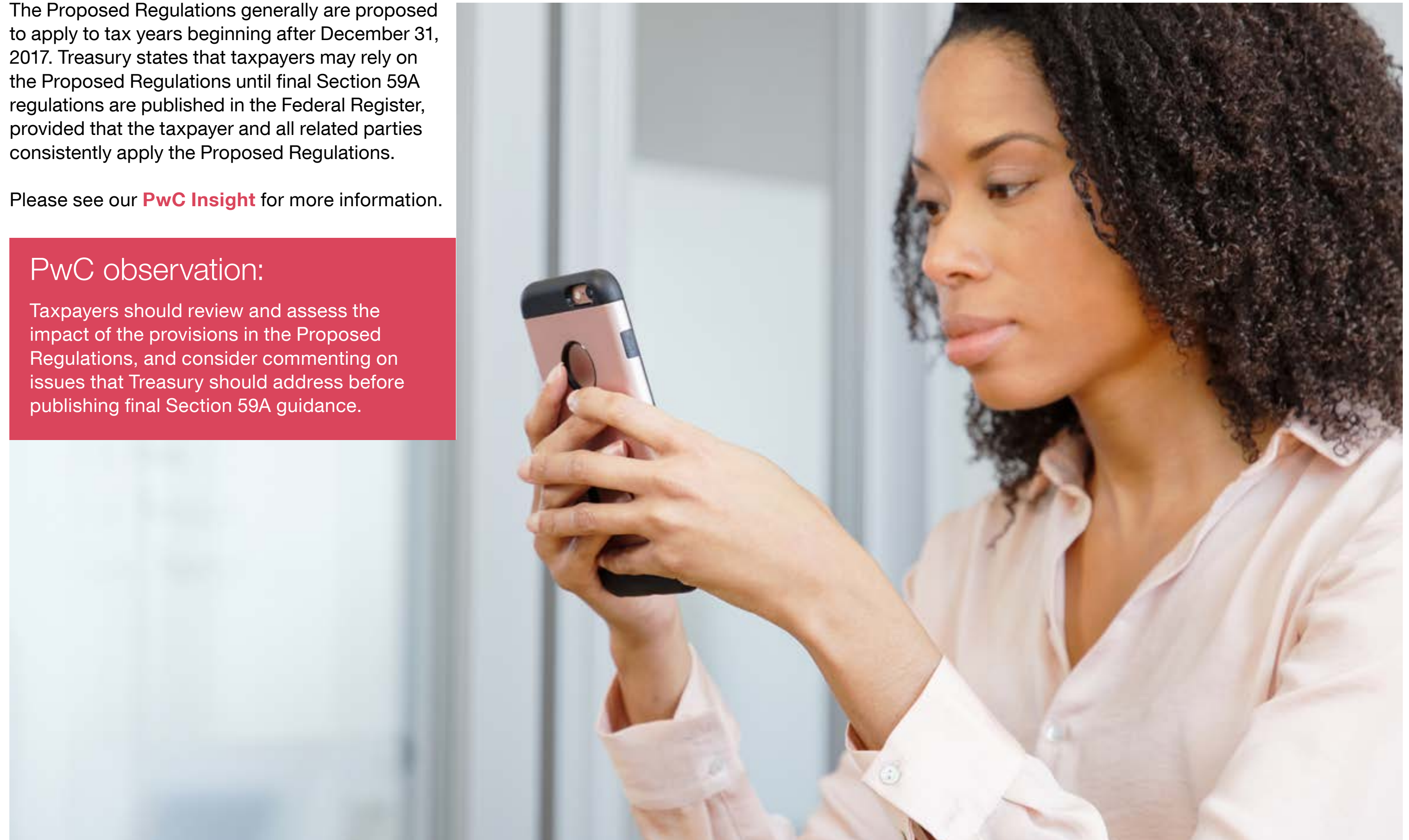
The Proposed Regulations provide needed guidance related to the mechanics of determining, among other things, the applicable taxpayer status, a taxpayer's base erosion percentage, and a taxpayer's modified taxable income (MTI). The Proposed Regulations also address the application of Section 59A to certain partnerships, banks, registered securities dealers, insurance companies, and consolidated groups. The Proposed Regulations reserve on the application of the BEAT to certain expatriated entities. The Proposed Regulations also provide an anti-abuse rule that generally disregards certain transactions undertaken with a principal purpose of avoiding Section 59A.

The Proposed Regulations generally are proposed to apply to tax years beginning after December 31, 2017. Treasury states that taxpayers may rely on the Proposed Regulations until final Section 59A regulations are published in the Federal Register, provided that the taxpayer and all related parties consistently apply the Proposed Regulations.

Please see our **PwC Insight** for more information.

PwC observation:

Taxpayers should review and assess the impact of the provisions in the Proposed Regulations, and consider commenting on issues that Treasury should address before publishing final Section 59A guidance.



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IRS provides key guidance on previously taxed E&P under Section 959, but leaves issues unresolved

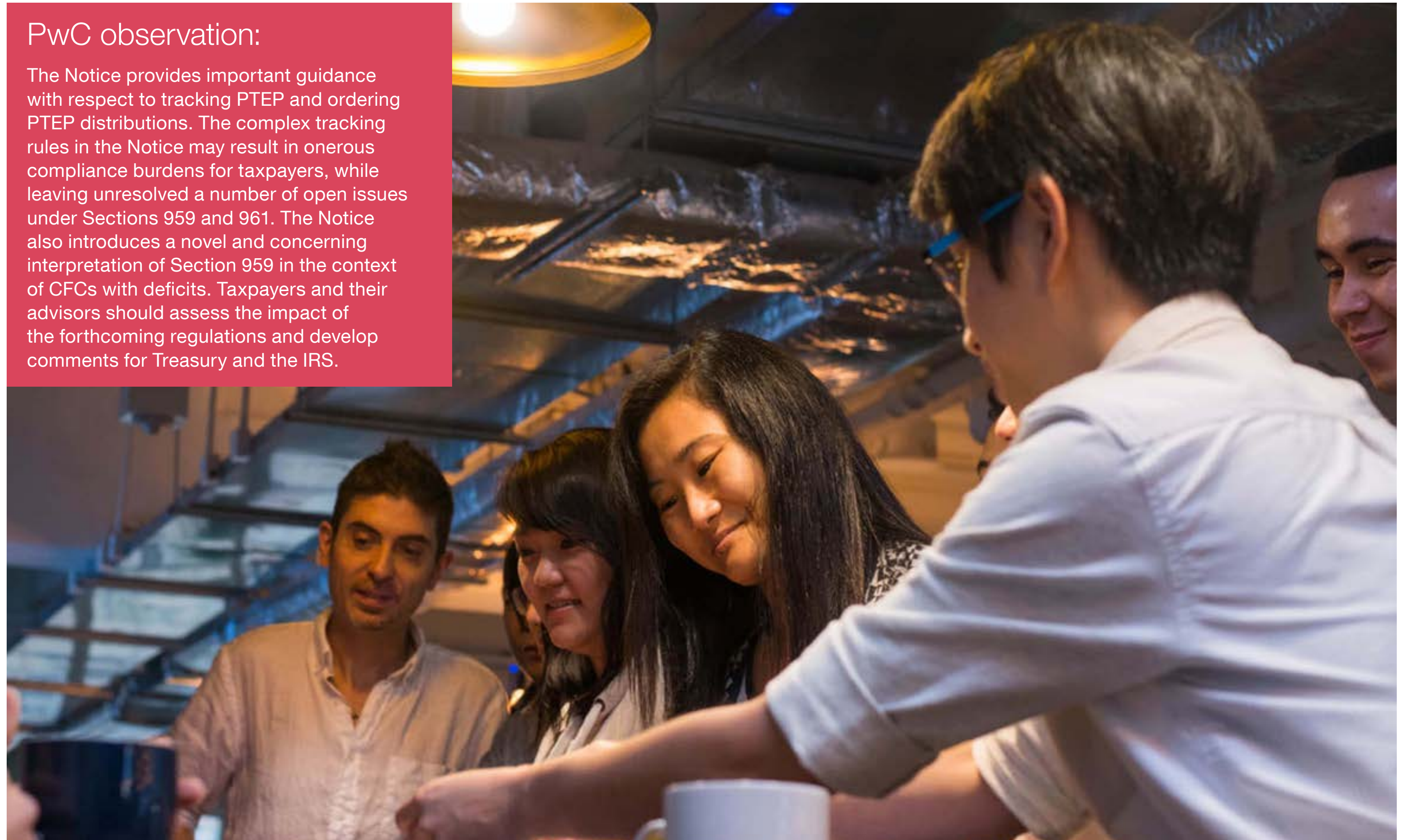
The IRS issued Notice 2019-01 on December 14, providing administrative guidance and indicating plans to issue regulations under Section 959 relating to previously taxed earnings and profits (PTEP, historically referred to as previously taxed income, or PTI). The Notice provides important guidance and examples related to tracking PTEP and ordering PTEP distributions, including 16 PTEP groups to track annually by Section 904 category.

The ordering rules prioritize Section 965 PTEP over other types of PTEP, but otherwise order PTEP distributions on an annual last-in first-out basis, pro rata from the different categories and groups. The Notice also provides transition rules for taxpayers that have not tracked PTEP at the level of detail required under the Notice. While the Notice addresses a number of important issues, it also proposes withdrawing prior proposed regulations that answered questions now left unresolved by the Notice.

Please see our **PwC Insight** for more information.

PwC observation:

The Notice provides important guidance with respect to tracking PTEP and ordering PTEP distributions. The complex tracking rules in the Notice may result in onerous compliance burdens for taxpayers, while leaving unresolved a number of open issues under Sections 959 and 961. The Notice also introduces a novel and concerning interpretation of Section 959 in the context of CFCs with deficits. Taxpayers and their advisors should assess the impact of the forthcoming regulations and develop comments for Treasury and the IRS.



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United States

Treasury releases proposed antihybrid regulations

Treasury released proposed regulations under the new dividends received deduction (DRD) and anti-hybrid rules as enacted under Sections 245A and 267A, respectively. Section 245A generally provides a 100% DRD for the foreign-source portion of dividends received by a US corporation from foreign corporations with respect to which it is a US corporate shareholder. Section 267A disallows deductions for certain related-party payments in connection with hybrid transactions or made by or to hybrid entities.

The Proposed Regulations, released December 20, are the first administrative guidance under both Section 245A and Section 267A, which were enacted by the 2017 Act. The Proposed Regulations provide needed guidance related to the mechanics of the new anti-hybrid provisions under Sections 245A and 267A, but also provide several rules that expand the reach of those sections. In particular, the regulations under Section 245A propose to deny the DRD in cases where certain US shareholders receive a 'hybrid dividend' made by CFCs, clarify the application of Section 245A for hybrid dividends of tiered corporations, and address certain 'hybrid deduction accounts' that are relevant upon the transfer of CFC stock. In addition, the Proposed Regulations clarify the scope of Section 267A as applied to hybrid arrangements involving the payment of interest or royalties by certain branches, reverse hybrid entities, and other hybrid mismatch arrangements. This guidance also proposes to modify the DCL rules under Section 1503(d) and check-the-box rules under Section 7701 in order to prevent the use of the same deduction in both the United States and in a foreign country. Finally, the Proposed Regulations amend a number of tax reporting requirements under Sections 6038, 6038A, and 6038C.

Please see our **PwC Insight** for more information.

PwC observation:

The Proposed Regulations, which are the first regulatory guidance under Sections 245A and 267A, clarify the application of guidance related to the mechanics of those provisions and expand the statutory rules in a number of respects. Taxpayers should immediately assess the impact of the provisions in the Proposed Regulations, and consider commenting on issues that Treasury should address before publishing final Section 245A, Section 267A, and DCL guidance.

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Netherlands

Dutch Supreme Court provides additional guidance on the deductibility of costs in relation to the acquisition or disposal of shareholdings

The Dutch Supreme Court, on December 7, 2018, provided additional guidance on the deductibility of costs incurred in relation to the acquisition or sale of shareholdings covered by the participation exemption. The guidance outlines how to assess whether the costs incurred actually relate to the acquisition or disposal of shareholdings, and also introduces rules for how to account for such costs.

Under the Dutch participation exemption, benefits derived from a shareholding (e.g., dividends or capital gains) are exempt at the shareholder level. Under the participation exemption regime, certain costs incurred in relation to the acquisition or disposal of a shareholding are not deductible.

In the underlying case, a Dutch taxpayer sold a shareholding to which the participation exemption applied. In dispute was the extent to which the taxpayer could deduct (part of) the costs from its taxable profit, as the taxpayer argued part of these costs should not be regarded as costs 'related to the disposal' of its shareholding. In response, the Supreme Court formulated as a main rule that costs are non-deductible (i.e., regarded as acquisition/disposal costs) if such costs would not have been incurred by the taxpayer, had this taxpayer not entered into the process of acquiring or disposing of a shareholding. In this respect, it is irrelevant whether such costs are internal or external. If a taxpayer incurs costs, but at a later stage, the acquisition or disposal of the shareholding fails, such costs are however (fully) deductible.

Finally, the Supreme Court stated that as long as the acquisition or disposal process has not been completed, the costs incurred must be capitalized in the tax balance sheet of the taxpayer as a 'transitional' asset. If the outcome of the acquisition or disposal process becomes clear, such asset should be written off, taking into account the new 'main rule' formulated by the Supreme Court.

PwC observation:

The Supreme Court's decision deviates from what is considered standard practice. For that reason, taxpayers should review past positions (to the extent tax returns are still under consideration by the Dutch tax authorities).

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OECD

OECD introduces minimum 'substance' requirements in low-tax jurisdictions

The OECD Inclusive Framework (IF), in follow-up work related to BEPS Action 5, has released new global standards that apply to 'no or only nominal tax' jurisdictions and that require 'substantial activities' in order for the tax regime not to be considered a 'harmful tax practice.' The objective is to prevent such low-tax jurisdictions from attracting profits from certain mobile activities without corresponding economic activity. The types of mobile activities covered include headquarters, distribution centers, service centers, financing, leasing, fund management, banking, insurance, shipping, holding companies, and the provision of intangibles.

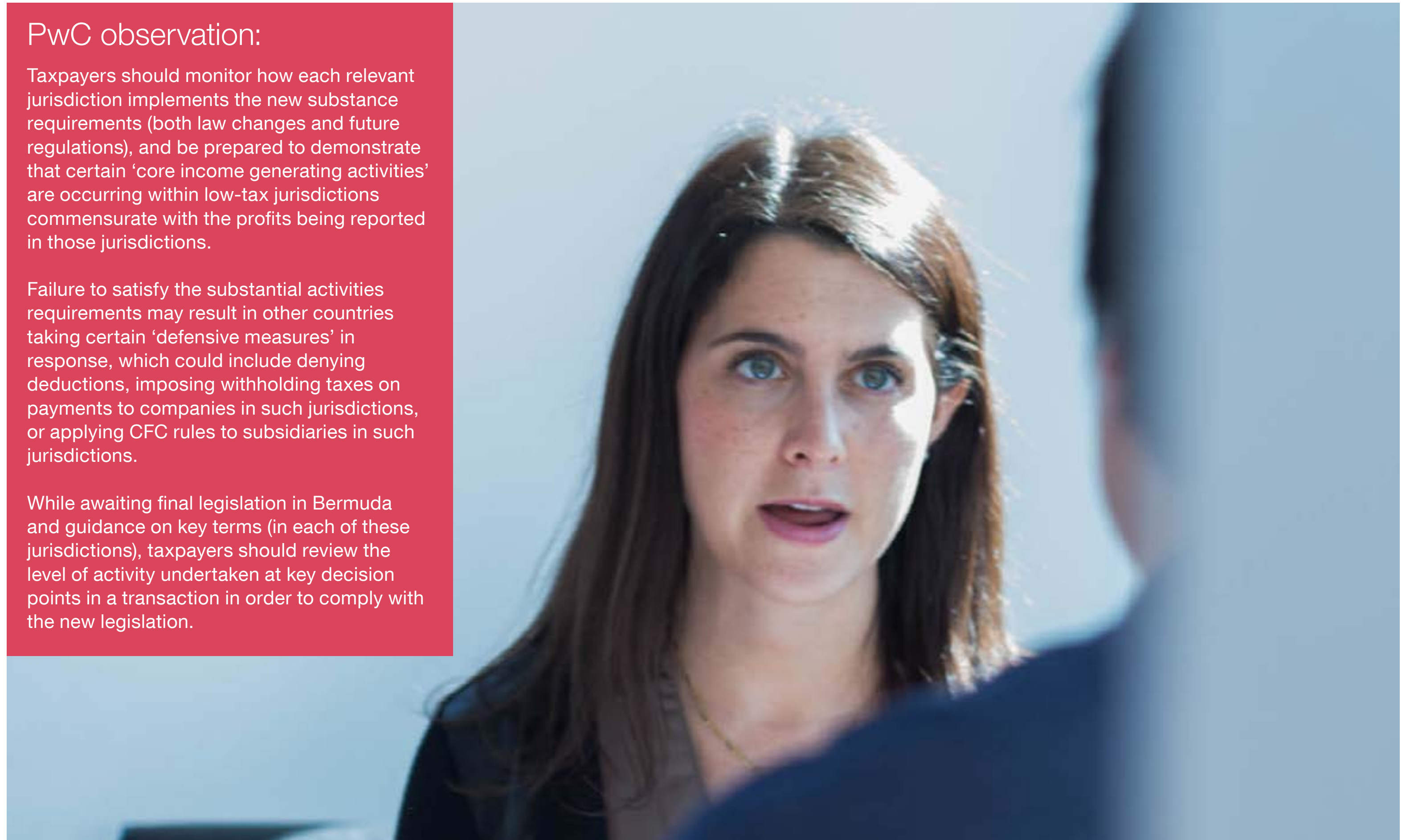
The standards are contained in a document entitled 'Resumption of Application of Substantial Activities Factor to No or only Nominal Tax Jurisdictions'. This document sets out the background, rationale, and detailed information around reinstating the substantial activities factor. As discussed in our **PwC Insight**, Barbados, Bermuda, and Cayman Islands have announced new domestic laws intended to meet the substance requirements.

PwC observation:

Taxpayers should monitor how each relevant jurisdiction implements the new substance requirements (both law changes and future regulations), and be prepared to demonstrate that certain 'core income generating activities' are occurring within low-tax jurisdictions commensurate with the profits being reported in those jurisdictions.

Failure to satisfy the substantial activities requirements may result in other countries taking certain 'defensive measures' in response, which could include denying deductions, imposing withholding taxes on payments to companies in such jurisdictions, or applying CFC rules to subsidiaries in such jurisdictions.

While awaiting final legislation in Bermuda and guidance on key terms (in each of these jurisdictions), taxpayers should review the level of activity undertaken at key decision points in a transaction in order to comply with the new legislation.



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Chile

Taxpayers can seek refunds after Chile applies most-favored nation clauses

Earlier this year, the Chilean government published Circulars Nos. 22/2018 and 50/2018 regarding application of the most-favored nation (MFN) clauses to 10 tax treaties. The MFN application is due to the December 28, 2016 entry-into-force of the Chile - Japan tax treaty and impacts Chilean withholding taxes on interest and royalties. Residents of tax treaty countries affected by the MFN clauses may seek a tax refund from the Chilean authorities with respect to any interest or royalty payments made on or after January 1, 2017.

Please see our **PwC Insight** for more information.

PwC observation:

Residents of the impacted countries that have been subject to withholding taxes in Chile since January 2017 on qualifying interest and royalty payments at rates that did not account for the MFN clause have the right to seek a tax refund from the Chilean tax authorities for the rate differential.

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Glossary

Acronym	Definition
Act	2017 tax reform reconciliation act
AEOI	automatic exchange of information
ATAD	Anti-tax Avoidance Directive
BEAT	base erosion and anti-abuse tax
BEPS	Base Erosion and Profit Shifting
CIT	Corporate Income Tax
CFC	controlled foreign corporation
DTA	double tax agreement
DAC6	EU Mandatory Disclosure Rules
DCL	dual-consolidated loss
DRD	dividend received deduction
EPI	environmental protection installations
EU	European Union
FTC	frequently asked questions
FSL	Federal Spending Law
FRL	Federal Revenue Law
GAAR	General Anti-Avoidance Rule
GILTI	Global Low Income Tax Income

Acronym	Definition
IRS	Internal Revenue Service
IF	Inclusive Framework
MFN	most favored nation
MLI	Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Based Erosion and Profit Shifting
MNEs	multinational enterprises
MRA	Mauritius Revenue Authority
MTI	modified taxable income
LIFO	last in first out
OECD	Organisation for Economic Co-operation and Development
PE	permanent establishment
POEM	place of effective management
PTEP	previously taxed earnings & profits
QDI	qualifying debt instruments
RMB	Renminbi
SAT	State Administration of Taxation
VAT	value added tax
WHT	withholding tax

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