At the intersection of international tax and digital transformation

Just-in-time taxation

EY

Building a better working world

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EY is a regular contributor to CCH's *Global Tax Weekly*. As tax and technology professionals, from member firms around the world, we share our insight and technology perspective on topics of interest to executives faced with taxation issues resulting from disruptive innovation and technology-enabled digital transformation. The content contained in this document was first published in *Global Tax Weekly* – and is being reprinted with full knowledge and permission from Wolters Kluwer, copyright 2016 CCH.

In this edition

These local country and international dynamics present fundamental considerations for tax practitioners and international finance executives, who must:

- Understand the level of uncertainty you face in monitoring and preparing for ongoing change in digital economy taxation, with potentially varying tax treatment from country to country
- Map the tax treatment of IP, transfer pricing, R&D and other issues related to your digital business models from the very outset, as you first develop your strategies, and build in flexibility for the long term
- Engage with tax administrators and policymakers in the markets you serve, to encourage beneficial tax outcomes and consider joining forces with like-minded companies or business advocacy groups for greater political influence

Overview

Time is of the essence, so let's get straight to the point. Global taxation is moving to a just-in-time environment. If you look at what's happening in Mexico today, as we do in this edition of our column, you'll see what could be coming your way. And you might not be ready for it.

Governments around the world are modernizing their tax administrations — from the increasingly common e-filing of traditional returns and source data to the more advanced e-audit and e-assess capabilities now deployed in Mexico. Some tax authorities are digitizing at different speeds or with different priorities or competence. But the common theme is that technology is enabling them to become more efficient and aggressive at assessing and collecting tax.

Within ten years or less, the traditional tax calendar should become a thing of the past, replaced by a same-day — or even same-transaction — taxing system. Within that time, if all goes right, digitizing taxation promises to streamline what is today an inefficient tax system, bring greater clarity and cut down on controversy.

But what about right now? Tax departments can be forgiven if they find themselves buffeted by too much change. Many find themselves catching up to their tax administrators' new digital approaches. At the same time, as you'll also read in this column, digital tax policies are evolving at great (and variable) velocity, as are the digital business models that continue to outstrip policymaking itself.

The good news is that technology can also help companies prepare for digital taxation. That may be cold comfort for those who see digital taxation as invasive or who now have to retool and reskill their tax departments with systems expertise, data analytics capabilities and more. But the only answer is that the sooner the realization sets in and the transition begins, the better positioned companies will be for the future of global taxation.

Speaking of transitions, we would be remiss in not addressing the tax developments ahead as a new administration comes into office in the United States in January. As we describe below, the alignment of the Republican White House and Congress could end the logjam on US tax reform. The question now is what shape that reform will take.

We are also pleased to announce the launch of EY's *Worldwide Digital Tax Guide* on our digital tax website.[1] The new guide, which updates and expands our existing *Worldwide Cloud Computing Tax Guide*, looks at sector-specific digital business models within technology, automotive, banking and capital markets, consumer products, telecommunications, media and entertainment, insurance, and life sciences. It features known and emerging tax and legal issues, insights and opportunities with those business models, specifically analyzing issues of nexus, indirect taxation and the landscape created by Action 1 ("Addressing the Tax Challenges of the Digital Economy") of the Organisation for Economic Co-operation and Development's Base Erosion and Profit Shifting initiative (OECD BEPS). The *Worldwide Digital Tax Guide* will provide these insights for approximately 120 countries. Country-specific regulations around digital tax administration will be available soon.

[1] View our *Worldwide Digital Tax Guide* at ey.com/gl/en/services/tax/ey-digital-tax-guide

Highlights and takeaways

Tax update	Technology impact	Ask yourself
The US election puts Republicans in control of both the White House and Congress.	Long-stymied tax reform could become a reality in the coming year.	Have you begun scenario planning for what could be dramatic tax change?
Mexico initiates electronic audits.	As a leader in digitizing and automating taxation, Mexico is considered a model that other countries could follow.	How will you adapt to the new realities of digital taxation?
Italian tax authorities rule on virtual currency and the sharing economy.	Italy provides an early look at how value-added taxes (VAT) might be handled in emerging digital economy business models.	How will your business model innovation affect your VAT tax obligations?
A Danish data center is determined not to create a PE.	The ruling distinguishes Denmark on the question of local servers used by nonresident companies.	Where do your various jurisdictional authorities draw the line between server ownership and control?
The Spanish Supreme Court confirms a broad interpretation of PE.	In this case, computer sales fall under the tax provisions covering both a fixed place of business and a dependent agent.	Where is the actual substance in your international structure?
Incorporation of 2015 changed OECD transfer pricing guidelines into Australian law could impact profit attribution in global value chains.	The guidance comes on top of several other Australian measures aimed at stemming tax multinational tax leakage through IP value transfers and PE avoidance.	Do these measures add up to creating tax exposures for your operations in Australia?

Tax update	Technology impact	Ask yourself
The UK enacts anti-hybrid mismatch rules and expands its royalty withholding regime.	These new anti-avoidance measures could impact many structures common to US-headquartered multinationals in the technology sector.	Do these latest moves heighten your risk profile, beyond the UK's existing diverted profits tax?
Swiss tax reform aims to foster innovation.	Patent boxes, R&D deductions and lowered corporate rates are being proposed in Swiss cantons.	Are you staying on top of all the new tax incentives arising in jurisdictions of interest?
Israel proposes a new innovation box regime.	The regime would enhance tax incentives available to IP-based technology companies.	Have you considered tax incentives for IP related to your Israeli R&D activities?
Taiwan Cabinet proposes to tax cross-border e-commerce.	Business tax and VAT would be applied to consumer sales, including low-value sales.	How are e-commerce cross-border rules affecting your operating costs and pricing strategies?
The European Commission finds that Ireland granted illegal State aid and orders a recovery.	The Commission's latest conclusion has introduced significant uncertainty within the technology sector.	Have you considered the impact this case may have on your existing global value supply chain?
The US finalizes the active royalty exception rule on subpart F income.	Officers or employees of the controlled foreign corporation (CFC) must develop or create the licensed IP to qualify for the exception.	Are royalties received by your CFC sourced from IP that is developed or created by the CFC's own employees?

Preview of 2016 US election and the tax landscape

Donald Trump's victory over Hillary Clinton in the US presidential election has teed up comprehensive tax reform as a clear priority for the new Republican President and the Republican Congress.

A unified Republican government makes the process of achieving a significant tax reform more manageable next year, in particular because House Speaker Paul Ryan pledged during the campaign to advance such a plan in the form of so-called "budget reconciliation legislation," which would mean that only a simple majority of senators would be necessary to pass it, rather than the usual 60-vote majority.

A lot of the groundwork has been laid through proposals and negotiations over the last few years on various key aspects of business tax reform, but Congressional Republican leaders and the new President will have to decide whether to push forward with legislation that embodies the existing House Republican Tax Reform Blueprint or the outlines of a tax reform plan that President-elect Trump championed during the campaign.

Considerations
How these changes will affect tech companies is uncertain, but given a unified Republican government, the groundwork is laid for significant changes to the US tax code. We will provide a deeper analysis on these proposals in future columns.

Contributor:
Allan Thompson (allan.thompson@ey.com), Ernst & Young LLP (US)

Mexico initiates electronic audits

The Servicio de Administración Tributaria (SAT), Mexico's tax authority, is considered to be at the forefront of administrations worldwide that are digitizing and automating taxation.

As the latest step in its transformation of the Mexican compliance system, the SAT recently initiated electronic audits that will be performed based on information filed electronically by taxpayers.

Taxpayers in Mexico are already required to file tax returns, issue invoices and file accounting records — all electronically. As such, there is a significant amount of information available to the SAT for review, without even contacting the taxpayer directly. Taxpayers should expect the availability of information to grow as the exchange of data increases among tax administrations around the world, with the implementation of country-by-country reporting.

In digitizing audits, the SAT indicated that the areas to be reviewed include:

- Differences between the tax liabilities reported in a tax return and the amount of taxes actually paid
- Income tax or VAT withholding omissions
- Incorrect credit of estimated tax payments against the annual income tax liability
- Deduction of donations in excess of the amounts allowed
- Incorrect calculations of accruable or deductible inflationary adjustments
- Incorrect deductions for interest expense

How it works

All correspondence will be conducted electronically through taxpayers' registered email accounts, and documents will be made available to taxpayers in an electronic drop-box. Once an audit has begun and electronic information is reviewed, the process should occur as follows:

- The SAT will notify the taxpayer of the review with the pre-assessment. The taxpayer will have three days to access the notification or will be deemed to have received it on the fourth day. If there is no challenge or response by the taxpayer of the pre-assessment, the pre-assessment is considered accepted, and the SAT may issue the final assessment against the taxpayer.
- Taxpayers will have 15 days to challenge the pre-assessment.
- The SAT would then have 10 days to review any information and documentation provided by the taxpayer. As part of this review, additional information may be requested from the taxpayer.
- The SAT would then have 40 days to issue and notify the taxpayer of a final assessment.

How to prepare

With this new tax landscape in Mexico, it will be crucial for taxpayers to be prepared for e-audits, ensuring they are able to support electronic requests and mount rapid audit defenses to issues raised in the SAT's pre-assessments. This includes understanding the data available to the tax authority to detect exposures or inconsistencies before they are identified by the SAT. Furthermore, taxpayers must be responsive to electronic correspondence, because a nonresponse can result in missed deadlines and an unexpected assessment.

Compliance with direct and indirect tax reporting and filing obligations should be aligned, taking into account that e-tax returns, e-invoicing and e-accounting are the main sources for performing the e-audits. Consequently, delays or errors in recording transactions could trigger inconsistencies that may raise a red flag.

Considerations

Companies everywhere should be watching Mexican tax developments as they unfold. Some observers consider Mexico a model — ahead of the curve as governments worldwide modernize their tax departments, set up cross-border information exchanges, and share leading practices and tools for automating their work. In many cases, corporate tax departments are in catch-up mode and need to adapt quickly to the realities of digital taxation. In Mexico, the reality is there today.

Contributors:
Ana Mingramm (ana.mingramm@ey.com) and Terri Grosselin (terri.grosselin@ey.com), Latin America Business Center, New York, Ernst & Young LLP (US)

Italian tax authorities rule on virtual currency and the sharing economy

Italy's tax authorities recently issued clarifications on how they will handle VAT associated with two emerging digital economy business models: virtual currency and the sharing economy.

In September 2016, authorities clarified that currency exchanges using bitcoin and other virtual currencies should be considered VAT-exempt services with no right of deduction as "transactions related to foreign currency with an official exchange rate and credits in foreign currency," under existing Italian VAT law. This interpretation is in line with the Court of Justice of the European Union's 2015 ruling in the *Skatteverket v. David Hedqvist* case.[1]

Italian authorities also ruled recently on the VAT treatment of online accommodation services, including room sharing in private homes. Under the ruling, European Union (EU) brokers are required to register for VAT purposes in Italy and to issue invoices charging domestic VAT for business-to-consumer (B2C) supplies. In addition, for business-to-business (B2B) supplies, VAT should be accounted for by the Italian business customer, through the application of a reverse-charging mechanism. The service provider must, therefore, qualify the status of the customer in order to apply the correct VAT principle and method of accounting.

Furthermore, authorities ruled that local VAT applies both in cases where the broker acts on behalf of the final client and in cases where it acts on behalf of the supplier of intermediated services. This is because both could qualify as "customers" for VAT purposes. Finally, authorities clarified that online intermediary services related to short-term accommodation do not qualify as "electronically supplied services" and therefore cannot benefit from the EU mini one-stop-shop (MOSS) VAT registration and filing regime.

Considerations

The virtual currency ruling should prompt businesses to carefully consider implications in terms of VAT cash flow, input tax recovery and reporting obligations. The ruling on accommodation may require foreign businesses that supply online brokering and booking services related to room sharing and other short-term accommodation in private residences to register for VAT, depending on the status of their clients. In the case of B2C supplies – since the MOSS scheme is not applicable – foreign businesses should also consider any potential liability in terms of omitted VAT payment and local VAT compliance fulfillments (periodic filings, invoicing, bookkeeping, etc.).

Contributors:
Stefano Pavesi (stefano.pavesi@it.ey.com) and Emanuele Muolo (emanuele.muolo@it.ey.com),
Studio Legale Tributario, in association with Ernst & Young Milan

[1] Case C-264/14 *Skatteverket v. David Hedqvist*, accessed via eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62014CC0264

Ruling in Denmark: data center doesn't always create a PE

SKAT, the Danish tax authority, has issued a ruling that distinguishes Denmark from other countries on the question of whether local servers used by nonresident companies constitute a PE.

Specifically, SKAT recently ruled that a data center in Denmark, operated under a hosting agreement by the Danish subsidiary of a nonresident taxpayer, does not constitute a PE of the nonresident taxpayer. The ruling contains a very thorough analysis of how a server can create a PE, subject to taxation, taking into account both OECD guidance and practice from other jurisdictions.

According to ordinary OECD principles, a data center should only create a PE if a nonresident taxpayer exercises control over the servers as if it in fact owned or operated the servers. The nonresident taxpayer was not considered to exercise such control, because it did not instruct the employees of the subsidiary or otherwise exercise any control over the work carried out by the subsidiary's employees. Furthermore, the foreign company normally had no physical access to the servers, though small groups of employees of the foreign company might from time to time be granted access. In this way, the hosting agreement typically does not put the server and its location at the disposal of the enterprise that conducts business through the website hosted.

Nevertheless, the foreign parent company has had remote access to the servers, allowing it to survey the efficiency of the data center's hardware and software, to install and uninstall applications, to maintain applications, and to handle software and data in the data center. If a server fails to function in a satisfactory manner, remote control could be used to shut down the server and redirect the internet traffic to other servers.

Considerations

This conclusion is in line with a previous decision from SKAT, reinforcing the fact that Denmark allows a nonresident taxpayer to control websites stored at servers in Denmark that are operated by another entity and, to a limited extent, also allows the taxpayer to control the servers, without creating a PE in Denmark. Foreign companies might assess the comparative merits of Danish data center regulation. If already operating through a Danish data center, they should consider their options regarding control over their servers through remote access.

Contributors:
Nina Brodersen (nina.brodersen1@ey.com), Scandinavian Tax Desk, New York, Ernst & Young LLP (US) and Jens Wittendorff (jens.wittendorff@dk.ey.com), Ernst & Young P/S, Denmark

Spanish Supreme Court confirms broad interpretation of PE

The Spanish Supreme Court recently ruled that a Spanish entity (SpainCo) belonging to a multinational group constituted a PE of an Irish entity (IrishCo) of the group, under both the "fixed place of business" and the "dependent agent" clauses of the Spain–Ireland tax treaty.

Originally, IrishCo was responsible for manufacturing and selling computer products through local subsidiaries in several European countries (including SpainCo, which was operated as a full-fledged distributor). Later, a reorganization was implemented, resulting in IrishCo taking over the sales and distribution functions, with SpainCo being recharacterized as a commissionaire. However, SpainCo continued to be involved in the logistics, marketing, and after-sales services and administration of the group's online store in Spain.

In June 2016, the Supreme Court confirmed that IrishCo had a PE in Spain under both of the following:

- The "fixed place of business" clause of the Spain–Ireland tax treaty, because IrishCo had a place at its disposal in Spain that was linked to the conduct of its business activity, regardless of whether such activity was effectively carried out by its own employees or by SpainCo at the latter's premises and with its personnel.
- The "dependent agent" clause of the tax treaty, because SpainCo had the faculty to bind IrishCo with clients even if there was no written agreement. Furthermore, SpainCo did not qualify as an independent agent because it operated exclusively for IrishCo under its comprehensive control and instructions.

Considerations

The resolution is of special interest because:

- It follows the trend set by the Spanish Supreme Court in earlier judgments, which upheld the Spanish tax authorities' functional approach with regard to post-restructuring schemes and commissionaire arrangements involving complex business structures in Spain
- It aligns with OECD BEPS Action 7, which states the need to update the treaty definition of PE in order to prevent abuses through the use of commissionaire arrangements

Attention should always be paid to international structures in terms of substance, especially under OECD BEPS guidelines. Consideration should be given on a case-by-case basis to all similar structures already in place, as well as to future conversions. Filing for an advanced pricing agreement or tax ruling with the Spanish tax authorities may also be considered as an alternative to mitigate the risk of challenge in the event of a tax audit.

Contributors:
Laura Ezquerra Martin (laura.ezquerramartin@es.ey.com), Ernst & Young Abogados, S.L.P., Madrid, and José Antonio Bustos (joseantonio.bustos@ey.com) and Manuel Paz (manuel.pazfigueiras@ey.com), Spanish Tax Desk, New York, Ernst & Young LLP (US)

Australian transfer pricing guidance to impact profit attribution in global value chains

The Australian Government has implemented OECD BEPS Actions 8–10, formally adopting the changed OECD transfer pricing guidelines into Australian law from 1 July 2016.

These align transfer pricing outcomes with the global value chain, while providing guidance on what are considered to be high risk-related party dealings. This complements the existing Australian transfer pricing rules which were substantially enhanced in 2012 to provide powers for the recharacterization of intercompany transactions rather than merely adjusting the price of transactions.

Taxpayers with the following intragroup arrangements may be significantly impacted by the changed transfer pricing guidelines:

- Assumption of risks and attribution of associated profits by a group member on a contractual basis, including the use of "limited risk entities" in the global value chain without the activity of managing those risks
- Commodity transactions not currently priced by applying the Comparable Uncontrolled Price (CUP) method or where there are significant discounts to the CUP in connection with marketing hubs
- Transfers of IP where, within a lookback period of up to five years, the transfer value of the IP is inconsistent with actual profits attributed to it
- Attribution of profits associated with the use of intangibles that is inconsistent with development, enhancement, maintenance, protection and exploitation (DEMPE) activities

Considerations

The new guidelines, together with the following major changes now falling into place, could transform the landscape for many multinational enterprises in Australia:

- Country-by-country reporting information collected from 1 January 2016
- The Multinational Anti-Avoidance Law (MAAL) effective from 1 January 2016
- A voluntary tax transparency code, encouraged for adoption from fiscal year 2016
- A diverted profits tax, for income tax years beginning on or after 1 July 2017
- Anti-hybrid rules effective from the later of 1 January 2018 or six months following royal assent
- GST (10%) on digital supplies, low value supplies and business to consumer supplies from 1 July 2017
- A multilateral instrument for changes to double tax treaties from late 2016
- Increased funding of the Australian Taxation Office, combined with a target to raise an additional AUD3.7b (US$2.8b) in taxes over a four-year period
- Increased penalties

Together these represent a major catalyst for multinationals to review their global value chain and operating structures.

Contributors:
Paul Balkus (paul.balkus@au.ey.com), Ernst & Young Australia and Andrew Nelson (andrew.nelson@ey.com), Australian Tax Desk, New York, Ernst & Young LLP (US)

UK enacts anti-hybrid mismatch rules and expands royalty withholding regime

The UK Government has enacted new anti-avoidance measures designed to combat erosion of the UK tax base, which could impact many structures common to US-headquartered multinationals in the technology sector.

One measure introduces a wide-reaching regime designed to counteract hybrid mismatches, while another expands the scope of deductions of income tax at source on royalty and other IP-related payments.

Anti-hybrid mismatch rules

For payments or "quasi-payments" made on or after 1 January 2017, it is necessary to test whether a hybrid mismatch arises. These rules apply to all payments, including payments related to royalties/cost of goods sold, as well as financing transactions.

Broadly, a mismatch could arise if:

- There is a payment or "quasi-payment" (including certain accounting and tax deductions) made by a UK-resident company, PE or avoided PE
- The payment involves a hybrid instrument or entity, broadly defined to include (for example) a multinational company (i.e., a company with a branch) or an entity with a US check-the-box election
- There is a mismatch between the amount of the UK deduction and the amount of income brought into tax in the recipient, and that mismatch arises because of the hybrid nature of the entity or instrument

Mismatches may be direct or indirect (an "imported mismatch"), meaning that it is often necessary to test the entire supply chain, and a UK disallowance may arise even where the UK payment is not made directly to a hybrid.

Deductions for royalties and IP-related payments

The UK Government has also enacted changes to the royalty withholding regime, including enhanced anti-avoidance measures, an extension to the scope of the types of IP falling within the UK domestic withholding regime, and a change to the rule on when a royalty has a UK source, to include royalty payments made by a PE or an avoided PE of the UK. In practice, this means that there may be a significant UK withholding requirement on payments between two non-UK entities (e.g., a European distributor company and a low-tax IP owner).

The rules are broadly written and include a number of targeted anti-avoidance measures, intended to prevent arrangements designed to circumvent the changes. The rules apply to payments made on or after 28 June 2016 (or 17 March 2016, in some cases).

Considerations

The interaction of the new rules with the UK's diverted profits tax, another anti-avoidance measure related to cross-border transfer pricing and the existence of PEs, are particularly complex. And with the heightened UK public scrutiny of the tax affairs of technology companies, the risk profile and amount of tax at stake for the sector may be significant.

Contributors:
James A. Taylor (james.taylor1@ey.com), Ernst & Young LLP (US)
and Jennifer Cooper (jcooper6@uk.ey.com), Ernst & Young LLP (UK)

Swiss tax reform aims to maintain its competitiveness in a rapidly changing environment, with patent boxes, R&D deductions and lowered corporate rates

Following the recent adoption of the federal tax reform package by the Swiss Parliament, the Swiss cantons are now outlining their corporate tax strategies for local implementation to attract foreign investments and foster innovation.

In June 2016, the Swiss Parliament approved the final bill on the third series of corporate tax reform, foreseeing the replacement of certain preferential tax regimes with a new set of internationally accepted measures. The legislative changes will go along with a broad reduction of corporate income tax rates to 11.5%–14% (including federal taxes) in most relevant cantons. The reform aims to ensure that Switzerland remains attractive for multinational corporations while being fully aligned with international taxation standards in a post-BEPS world.

Replacement measures outlined in the federal bill will, to a large extent, serve as a toolkit for the cantons to adapt into their cantonal tax legislation as they see fit to remain competitive and tailor to their specific portfolio of corporate taxpayers.

The measures available to the cantons include:

- Patent box (in line with the OECD's modified nexus approach)
- R&D super-deduction
- Notional interest deduction on surplus equity (also to be introduced at the federal level)
- Transitional rules to ensure a smooth transition from a preferential regime to ordinary taxation (mandatory measure)
- Step-up upon migration to Switzerland (mandatory; also to be introduced at the federal level)
- Reduction of statutory corporate income tax rate
- Targeted capital tax reductions

Most relevant cantons have already announced their tax strategies – pharmaceutical hubs Basel-Stadt and Basel-Landschaft, for instance, will focus on significantly lowering their tax rates and introducing a patent box regime, with Basel-Landschaft additionally allowing R&D super-deductions of 150%. Geneva plans to lower its headline tax rate from 24.2% to 13.5%, and seeks to develop a broad long-term strategy to foster innovation. Zug (12%), Lucerne (11.5%–12.5%) and Schaffhausen (12%–12.5%) are expected to provide, aside from attractive replacement measures, the lowest headline tax rates in Switzerland after the reform.

The federal bill is subject to a popular referendum, which is scheduled to take place on 12 February 2017. Provided that Swiss voters formally approve the reform package in the upcoming vote, the Swiss corporate tax reform will enter into force on 1 January 2019.

Considerations

In a post-BEPS world, multinationals seeking to realign the substance within their global value chains are gaining new options, including tax incentives. Tax strategists should weigh all available incentives as well as all aspects of location when adjusting their international structures.

Contributors:
Thomas Semadeni (thomas.semadeni@ey.com) and Anna Eldring (anna.eldring1@ey.com), Swiss Tax Desk, Ernst & Young LLP (US)

Israel proposes innovation box regime to attract IP investments

The Israeli Government recently proposed a new innovation box regime that would enhance tax incentives available to IP-based technology companies. The regime, with an expected effective date of 1 January 2017, is tailored to a post-BEPS world.

Over the years, as Israel has evolved into a leading technology innovation center, many multinational companies have accessed local talent and technology through acquisitions of Israeli tech companies and by establishing R&D centers. Currently more than 270 of the largest technology multinationals operate development- and technology-related manufacturing centers in Israel.

Against the backdrop of the OECD's BEPS project and new international transfer pricing standards, global technology companies are seeking to ensure alignment among the allocation of their profits, the ownership of their IP and their value-creating functions. In this new reality, Israel has identified an opportunity to provide tax benefits to multinationals that will choose to hold IP in Israel. The R&D activity already existing in Israel benefit from the preferential IP tax regime, in line with the BEPS limitation of tax benefits to the proportional level of R&D activity undertaken by the taxpayer.

The proposed regime would include a corporate income tax rate of 6% on all IP-based income and on capital gains from future sale of the IP. The 6% rate would apply to qualifying technology companies with consolidated revenues of more than ILS10b (US$2.5b). Other qualifying companies with consolidated revenues less than ILS10b would be subject to a 12% corporate income tax rate. Additionally, withholding tax on dividends would be subject to a reduced rate of 4% for all qualifying companies. Entering into the innovation box regime would not be conditioned on making additional investments in Israel. Exiting from the regime would not trigger a claw-back of the tax benefits.

Considerations

Multinationals that have acquired Israeli technology companies, or are planning to do so, should assess the applicability and impact of the new tax regime to the post-acquisition integration of the Israeli IP within their global structure. Moreover, companies that currently operate R&D centers in Israel on a cost-plus basis can simply enjoy the tax benefits as of January 2017 by switching the ownership of the IP developed in Israel to the Israeli entity without the need to relocate employees. Lastly, the tax benefits can also apply to IP that was previously developed in Israel on cost-plus basis and will now be on-shored into Israel.

Contributors:
Sharon Shulman (sharon.shulman@il.ey.com), Kost Forer Gabbay & Kasierer, Tel Aviv, Ernst & Young Israel,
and Rani Gilady (rani.gilady1@ey.com), Israel Tax Desk, Ernst & Young LLP (US)

Taiwan Cabinet proposes to tax cross-border e-commerce

In September 2016, Taiwan's Executive Yuan released draft amendments to the Value-added and Non-Value-added Business Tax Act, requiring foreign e-commerce operators without a fixed place of business in Taiwan to register and pay tax when selling to Taiwanese individuals. The amendments would also make low-value cross-border sales subject to business tax.

Under the current system, when foreign e-commerce operators sell to Taiwanese purchasers, the Taiwanese purchasers are responsible for paying the business tax through reverse charges. However, in a situation where the purchasers are individuals, the existing tax system does not have procedures to enforce individual purchasers to make a voluntary tax payment, causing difficulties for the tax authority to collect the tax. To solve the issue, the draft amendments require the foreign e-commerce operators to register with Taiwan's tax authority and file a return.

The new requirements would apply if total e-commerce sales exceed a certain threshold (yet to be specified). A registrant would be assigned a taxpayer ID number to be used when filing bimonthly business tax returns. Failure to comply with the filing requirements may result in penalties of up to five times the amount of tax due and loss of a license to operate. An application for a tax registration must be submitted prior to commencement of operations. Failure to comply with this requirement may result in a penalty ranging from NTD3,000 to NTD30,000 (US$100 to US$1,000).

Additionally, under the current law, when a transaction amount is below a certain threshold, the sale is exempt from business tax. To level the playing field between foreign e-commerce operators and their Taiwanese counterparts, this threshold would be removed.

Considerations

The details of the amendments are still under review. However, once the amendments become effective, foreign e-commerce operators would become subject to registration and return filing requirements in Taiwan, as they have in many other jurisdictions in recent years. Because their operating costs will likely increase, it is recommended that they prepare early for the changes.

Contributors:
Sophie Chou (sophie.chou@tw.ey.com), Chien-Hua Yang (chienhua.yang@tw.ey.com) and Anna Tsai (anna.tsai@tw.ey.com), Ernst & Young Taiwan

European Commission finds Ireland granted illegal State aid and orders a recovery

On 30 August 2016, the European Commission (the Commission) released its decision in its investigation into the (alleged) State aid issues associated with a multinational company's tax arrangements agreed with the Irish Government.[1]

The Commission has concluded that two tax rulings issued by Ireland have substantially and artificially lowered the tax paid by the multinational in Ireland since 1991. The Commission has ordered that Ireland must now recover the unpaid taxes in Ireland from the multinational for the years 2003 to 2014 of up to EUR13b, plus interest. The Irish Government has formally appealed the decision as it disagrees profoundly with the Commission's decision. A press release issued by the Irish Department of Finance confirms that "Ireland's position remains that the full amount of tax was paid in this case and no State aid was provided." The multinational has also said that it will appeal the decision.

For further analysis, please see "European Commission finds Ireland granted illegal State aid and orders recovery – a further review."[2]

Contributors:
Joe Bollard (joe.bollard@ie.ey.com), Ernst & Young Ireland and James Burrows (james.burrows1@ey.com), Irish Tax Desk, New York, Ernst & Young LLP (US)

1 EU Commission, SA.38373. The non-confidential version of the decision is not yet available. Press release, IP/16/2923.
2 "European Commission finds Ireland granted illegal State aid and orders recovery – a further review," *EY Global Tax Alert*, 7 September 2016, © 2016 EYGM Limited

US finalizes its active royalty exception on subpart F income

The US Internal Revenue Service (IRS) and US Department of the Treasury have finalized subpart F income exceptions granted for active royalties on IP licensed by controlled foreign corporations (CFCs).

The final regulations adopt with no changes the temporary regulations published in September 2015 and apply to royalties received or accrued during taxable years of CFCs ending on or after 1 September 2015, and to taxable years of United States shareholders in which or with which such taxable years end. They include:

- A CFC is not a developer or creator for purposes of the active royalties exception to the foreign personal holding company income rules unless its own employees and officers perform the required functions
- Employees may also be located in more than one country in order to meet the active royalty exception
- A CFC cannot meet the active royalty exception through cost-sharing arrangements, and cost-sharing payments will not be treated as active licensing expenses for purposes of determining whether an organization is "substantial"

Considerations

For the active royalty exception to apply, tech companies must ensure that the licensed IP is developed or created by the CFC's own officers and employees. It is important to note that cost-sharing payments made by the CFC to another controlled participant do not qualify as activities undertaken by a CFC's own officers and employees.

Contributors:
Arlene Fitzpatrick (arlene.fitzpatrick@ey.com), Peg O'Connor (margaret.oconnor@ey.com) and Allan Thompson (allan.thompson@ey.com), Ernst & Young LLP (US)

About the authors

Channing Flynn (channing.flynn@ey.com), Stephen Bates (stephen.bates@ey.com) and Allan Thompson (allan.thompson@ey.com) are collaborating on this column with members of the global EY organization's network of tax professionals in member firm technology practices.

Channing Flynn
is an International Tax Partner of Ernst & Young LLP (US) based in both San Francisco and San Jose, and EY's Global Technology Industry Tax Leader.

Stephen Bates
is an Ernst & Young LLP (US) International Tax Principal based in San Francisco.

Allan Thompson
is a Senior Manager in our International Tax Services practice of Ernst & Young LLP (US), based in New York.

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Preview of 2016 US election and the tax landscape

Ana Mingramm and Terri Grosselin
Mexico initiates electronic audits

Stefano Pavesi and Emanuele Muolo
Italian tax authorities rule on virtual currency and the sharing economy

Nina Brodersen and Jens Wittendorff
Ruling in Denmark: data center doesn't always create a PE

Laura Ezquerra Martin, José Antonio Bustos and Manuel Paz
Spanish Supreme Court confirms broad interpretation of PE

Paul Balkus and Andrew Nelson
Australian transfer pricing guidance to impact profit attribution in global value chains

James A. Taylor and Jennifer Cooper
UK enacts anti-hybrid mismatch rules and expands royalty withholding regime

Thomas Semadeni and Anna Eldring
Swiss tax reform aims to maintain its competitiveness in a rapidly changing environment, with patent boxes, R&D deductions and lowered corporate rates

Sharon Shulman and Rani Gilady
Israel proposes innovation box regime to attract IP investments

Sophie Chou, Chien-Hua Yang and Anna Tsai
Taiwan Cabinet proposes to tax cross-border e-commerce

Joe Bollard and James Burrows
European Commission finds Ireland granted illegal State aid and orders a recovery

Arlene Fitzpatrick, Peg O'Connor and Allan Thompson
US finalizes its active royalty exception on subpart F income

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Technology sector leader

Greg Cudahy
EY Global Leader — TMT
Technology, Media & Entertainment and Telecommunications
+1 404 817 4450
greg.cudahy@ey.com

Technology service line leaders

Channing Flynn
EY Global Technology Sector Leader
Tax Services
+1 408 947 5435
channing.flynn@ey.com

Jeff Liu
EY Global Technology Sector Leader
Transaction Advisory Services
+1 415 894 8817
jeffrey.liu@ey.com

Dave Padmos
EY Global Technology Sector Leader
Advisory Services
+1 206 654 6314
dave.padmos@ey.com

Guy Wanger
EY Global Technology Sector Leader
Assurance Services
+1 650 802 4687
guy.wanger@ey.com

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