“I think what we see in general, and what we maybe see in some of the most advanced tax administrations, is that we are really becoming truly digital.

We clearly started this journey with personal taxpayers.

I think the next wave will be the business side.”

—Interview with Hans Christian Holte, Norwegian Tax Commissioner and new chair of the OECD’s Forum on Tax Administration
New digital tax policies: what, when, where, how and by whom?

Eight for 2018 and beyond: key transfer pricing risks to consider

International Monetary Fund and World Bank launch a new program, offering their potential alternative to the arm’s-length principle

Global connectivity means it’s easier today for companies to be faced with tax controversy. How can you manage the risk?

How tax authorities are increasingly scrutinizing procurement function activities

Taxpayers in India face key compliance challenges around the sale and transfer of intellectual property

Spain proposes a digital services tax

United States: US Supreme Court overturns Quill, eliminates physical presence nexus standard for sales and use tax collection

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It's always interesting how the true objectives and impacts of an event come into focus more easily with a little time and distance. It's a little like sitting at 35,000 feet in an airplane—the higher view of the world simply allows for a greater sense of objectivity, and a clearer picture.

The BEPS project, for example, has deliberately made the arm’s-length standard less precise and even more subjective than it already was. This was an objective of the project, designed to increase the risk profile of structures that sought to allocate profits to tax havens or create stateless income.

This makes the role of tax administration and its link to tax policy even more important. “The focus of the OECD’s Forum on Tax Administration, like that of most national tax administrations, is on implementation rather than policy, although it will provide important feedback and input to the policymaking process, too,” says FTA Chair Hans Christian Holte, Director General of the Norwegian Tax Administration, in our feature interview.

“We are now entering the implementation period for BEPS...” he says. “So the spotlight is falling onto tax administrations, questioning how they can simultaneously enhance compliance, tackle tax crime, reduce the administrative burden on taxpayers and support economic growth through effective implementation, internal change and engagement with taxpayers.”

With those words, Holte effectively explains how the tax world has moved into a different phase—one of implementation and policing—and that the work of the subsidiary body of the OECD that he chairs must now follow through and deliver the three C’s (certainty, consistency and currency) that taxpayers want (and hopefully avoid the complexity and confusion that they don’t!).

With the speed, volume and complexity of tax policy, legislative and regulatory change continuing to accelerate, accessing the leading global insights has never been more important.

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Digital tax: If you are asking what the product is, it’s probably you ...

2018 may come to pass as the first year of concrete action and new laws around the taxation of digital activity. While it was included in the BEPS project in 2015, the digital debate of today takes a very different form. Instead of focusing on anti-avoidance and stateless income, as our article on page 14 explains, the debate is now focused on what digital activities drive currently untaxed value, and how the division of taxing rights among countries should work in the future.

How (and indeed, if) the European Commission’s pair of digital proposals play out is still uncertain, and recent events seem to indicate that the focus—for a long-term solution, at least—is returning to the OECD. As Klaus von Brocke and Steve Bill write in their page 20 article discussing the EU’s unique policy formation process, the European proposals are now being picked apart and reassembled by Working Party on Tax Questions within the Commission.

Simultaneously, as professionals from our State and Local Tax group outline on page 42, the Supreme Court in the South Dakota v. Wayfair case has overturned Quill, eliminating the physical presence nexus standard for sales and use tax collection. The most pressing issue for multistate taxpayers, they explain, is whether the states will attempt to assert liability for uncollected taxes on a retroactive basis. But no less importantly, all taxpayers must immediately consider the impact of this decision on their operations.

The voice of business
Top three risk areas: EY 2017-18 Tax risk and controversy survey

1. Transfer pricing of goods and service
2. Indirect taxes — including VAT, GST and customs
3. Permanent establishment risk

No. 1 tax risk

EY’s 2017-18 Tax Risk and Controversy Survey identifies transfer pricing as the issue representing the highest tax risk for companies. Page 25 sees the publication of the first article in a new EY series titled “Eight for 2018 and beyond.” This series identifies and discusses key transfer pricing risks, providing readers with actionable insights and practical takeaways. This first article in the series focuses on the transfer pricing aspects of the sale or transfer of intellectual property assets.

Finding your path forward

Today, company tax leaders are being tasked with doing more to inform strategic tax and business decisions and to drive a new wave of increased productivity. Globalization’s volatile environment means a higher degree of risk and more challenging mobility issues, but it also brings opportunities. Being able to effectively respond to global trends will help keep you ahead of the curve, grow your market share and revenue, and can improve efficiencies. We hope this publication helps you find your path forward.
Something I continue to take great pleasure from in my role as Global Tax Policy Leader for EY is the opportunity it gives me to meet and talk to the people who shape the world of tax. This group—tax policymakers, standard setters, regulators and tax commissioners—work on the very leading edge of an industry that is undergoing dramatic change and reform. Whilst I did not enter the world of tax because I thought it was going to set the world on fire, it has become one of the most interesting sectors to work in, delivering an added bonus.

Hans Christian Holte stands squarely in the middle of this group of leaders; indeed, his near-200cm (6 foot 6) frame almost guarantees that he is a highly noticeable presence. Holte is both the Norwegian Tax Commissioner and the new Chair of the Organisation for Economic Co-operation and Development’s (OECD) 50-jurisdiction Forum on Tax Administration (FTA). The FTA group includes OECD and non-OECD countries and is the OECD subsidiary body that encourages tax authority leaders to come together, cooperate and collaborate around ideas that they hope will improve the administration of tax for both government and taxpayers alike.

Game-changer

The stunning historic architecture of Oslo’s old town belies just how innovative and forward-thinking is this nation of more than 5 million people. It is this desire to move forward that has, in part, cemented a high level of trust between taxpayers and the Norwegian Tax Administration (Skatteetaten).
“In general, I feel that the relationship between the tax administration and Norway’s business community is in good shape,” says Holte. “That has to do with what is vital for all tax administrations—the general level of trust and legitimacy that we enjoy as a tax authority. This is driven by several aspects; the first is to do with the high level of trust that exists in Norwegian society when it comes to public authorities generally. The second comes back to the journey that we have been on for several decades to simplify tax administration through things such as providing a pre-filled tax return to the common citizen. That was a game-changer in my mind. So we have a good basis in society in general.”

I asked, “Does that change the way in which tax disputes play out?” “Well, it doesn’t mean that everything is idyllic when it comes to the relationship between the tax authority and business. We still have our heated discussions and disputes. But we do that off a strong foundation of trust.” That is a useful point for all tax administrations to consider.

Come together

While Holte’s views on administering the Norwegian tax regime are fascinating in their own right (he has been Norway’s Tax Commissioner since 2013, joining that agency after five years as Director of Norway’s Agency for Public Management and eGovernment), it was his views on how tax administrations work together under the FTA that were of equal interest to me during our conversation.

Almost a decade ago, EY colleagues and I wrote in an whitepaper Tax administration without borders that “tax administrations are increasingly recognizing that the ability to look at international transactions and global businesses through a ‘multilateral lens’ is far more effective than only understanding and seeing their national view. Increased cooperation has been made possible by the many international groups and forums dedicated to helping tax authorities share more information and knowledge —about processes as well as taxpayers—to improve compliance and curb abuses.”

In that same publication, then-Australian Taxation Office (ATO) Commissioner Michael D’Ascenzo noted that “the level of cooperation among the more mature tax administrations is very high at the moment. And, it is very high at a personal level as well as at an organization level, and that really makes it a little easier to get things done.”

The FTA, which also comprises a number of specialist networks, including the Joint International Taskforce on Shared Intelligence and Collaboration (JITSIC), dates back in its various iterations, in fact, to 2002. And while it has been almost a decade since D’Ascenzo’s words, it is clear to see that many factors—the “fair share” debate, the new era of tax and financial transparency and the advent of the BEPS initiative—have all led to an increase in not only the number of countries engaged in FTA work, but how widely and deeply the group cooperates.

In fact, even the last few (i.e., post-BEPS) years have led to an acceleration in the closeness of FTA members and their willingness to share their leading practices and experiences. I say this from personal experience; I have been fortunate to have a first-hand view of what it is to participate in the FTA, as EY has been involved in helping the FTA’s Digital Transformation subgroup, a relatively new group within the FTA. While attending these sessions, I have seen a dramatic shift in the way tax leaders connect with one another after just three years—from tentative nods and hellos in the early days, to passionate, heads-down-over-a-piece-of-paper or whiteboard sharing of their learnings on artificial intelligence, advanced analytics and blockchain at the most recent meeting I attended.

“Today, the FTA has a membership of 50 advanced and emerging tax administrations,” Holte says. “We collaborate together on various ongoing projects and through communities of interest, which currently include studying the shadow economy, looking at behavioral insights, digital transformation, data analytics and risk management. We also cooperate via a number of what we call ‘enduring programs,’ which include J ITSIC, the Large Business and International Programme, The Tax Debt Management network and the Capacity Building network. All of these are grouped under three broad pillars – supporting the international agenda, improving compliance and future tax administration.”

As I noted earlier, my early (very early) morning journey to Oslo was taken up with, once email was done, reviewing our agreed interview questions and reading through some of the interviews EY has conducted recently with Holte’s peers. One that particularly caught my eye was a November 2017 EY interview with the ATO’s Deputy Commissioner, Jeremy Hirschhorn. “At the parliamentary level, governments are much more interested, when it comes to tax, in the big headline elements, the broad brush,” said Hirschhorn. “They’re interested in rate and mix, they’re interested in the BEPS program, international moves, to doing things that are solving a problem.” I wondered how that focus on the big ticket items would affect the tax administrators that work together under the FTA. Does it mean that the role of tax administration is actually becoming equal, if not more important than the setting of policy in the first place?

The FTA focus, like that of most national tax administrations,” says Holte, “is on implementation rather than policy, although it will provide important feedback and input to the policymaking process, too. We are now entering the implementation period for BEPS, at a time that digital transformation is occurring at an accelerating pace on all sides. So the spotlight is falling onto tax administrations, questioning how they can simultaneously enhance compliance, tackle tax crime, reduce the administrative burden on taxpayers and support economic growth through effective implementation, internal change and engagement with taxpayers.”

That engagement with taxpayers, says Holte, is a particularly important strand in any tax administrator’s tactics. “We need an open dialogue, mutual understanding and two-way flows of information. Jointly, FTA members collect around 8.5 trillion euros each year. So even small changes in compliance and reductions in administrative burden can have significant economic and societal impacts.”

We’re in a paradigm shift, right now

That mention of digital transformation highlighted an area of our interview that I was particularly looking forward to.

As a national tax administration, Norway has long been at the forefront of technology developments and was one of the pioneering Nordic countries to first introduce the concept of pre-populated tax returns. Preparing for our session at Skatteetaten’s colorfully decorated management offices on the outskirts of Oslo, I had been reading my preparation materials, which included a set of poll results from a recent EY webcast that detailed how more than 2,000 of our clients are experiencing revenue authorities’ digitalization.

Seventy-three percent of survey respondents have seen an increase in digital data submission requirements over the course of the last three years. That is not surprising; but what did surprise me, however, is that 83% said they have “partial” or “no” awareness of the tests that countries are running over their submitted data.

I was therefore keen to hear Holte’s (himself a regular user of Twitter: @HCHolte) views on whether corporate taxpayers should expect a slow-but-steady progression of changes around the world, or more of a disruptive, seismic paradigm shift to full digitalization and corporate systems “talking” directly to those of the tax authority.

“We think we’re actually right in that paradigm shift right now,” he immediately confirmed. “I think it’s happening already, and it has significant implications at both national and international levels. There are different speeds at which different tax administrations are moving through this shift, but I think what we see in general, and what we maybe see in some of the most advanced tax administrations, is that we are really becoming truly digital. We clearly started this journey with personal taxpayers. I think the next wave will be the business side. That’s also a very interesting journey, because we have all the systems taking care of accounting, for example, inside the business, and we have the traditional way of reporting to paper-based schemes to the tax authorities. But we’re moving away from that model. It’s moving away today, and within the next 10 years I think it will be replaced by what could be quite digital channels of information, going from the accounting systems directly to the tax authorities.”

“If we do this properly, I think we could balance both efficiency and simplicity, and also take care of data protection and privacy issues,” he agreed. “I think we have to have all those kinds of issues in our heads when we design these solutions, but I think there is great potential for actually making this happen in a way that both increases compliance and also makes the administrative burden on the business side less, and also, it actually makes tax certainty a more real thing.”

“I am very proud to have become Chair of the FTA at this pivotal time,” Holte told me at the end of our discussion. “And while I can talk about the FTA work program, which is ambitious and challenging, I should make it clear that the opinions I express are, of course, my own, and not those of the OECD itself.”
"I think we're actually right in that [digital] paradigm shift right now. I think it's happening already, and it has significant implications at both national and international levels."

That administrative burden on business was one area that I try and include into every interview with every tax official. I have always personally viewed the move to fully digital tax administration with hope, but also concern about how taxpayers will fare on the journey. Just the previous day, we had agreed internally at EY to invest a significant additional amount of time and resources on doing more to track digital tax developments – across both the policy and administrative dimensions – in far more detail, and across a range of more than 60 countries.

On the administrative side, we are seeing a number of countries adopting Standard Audit File for Tax (SAF-T) requirements including, recently, Poland and Norway, with the Netherlands also known to be looking at new obligations in this area. As much as tax authority leaders hope that digitalization will eventually reduce the overall compliance burden, clients continue to tell us that the exact requirements they must meet in each country are wildly different, not to mention rapidly changing. "Is there a role here for the FTA to play, in terms of driving for more consistency between nations' requirements?" I asked.

"The introduction of SAF-T was designed to standardize the production and reporting of accounting information, making the taxpayer's data available for further analysis and reconciliation," says Holte. "Internationally, though, there are relatively large differences between countries' tax systems and how they are administered.

Now, the new FTA Community of Interest on Digital Transformation will set its own agenda and will, I am sure, focus on all taxpayer segments, including large businesses. I think that the work being undertaken in the FTA on the International Compliance Assurance Programme (ICAP), risk assessments and joint audits in particular has an important role to play here in terms identifying different approaches and the reasons behind them. Over time, we may be able to identify a single set of information which can be provided by multinational companies globally. Whether that means we will look again at SAF-T or whether tax administrations may better align with the evolving systems used by business is also something to consider further."

Addressing uncertainty

Reduction in administrative burden suffered by taxpayers is welcome. But against a backdrop of global change and reform, increased transparency and more aggressive scrutiny of taxpayers, another similar theme has risen to the top of the agenda of the OECD and other bodies supporting the tax community: tax uncertainty.

In that regard, my discussion with Holte — about midway between the release of the IMF/OECD report to G20 leaders on tax certainty, and the starting gun sounding for the automatic exchange of country-by-country (CbC) reports to begin between tax authorities — came at an opportune time. On CbC, the OECD says that more than 1,400 exchange relationships have been activated; as a result, virtually every client I talk to brings up the question of whether the exchange of CbC reports will drive more incoming inquiries and, ultimately, tax disputes. "How do you expect tax administrations will approach the use of CbC reports?" I asked. "Do you foresee a distinct uptick in controversy, or do you instead expect this to build up slowly, over time?"

"CbC reports represent an unprecedented opportunity for tax authorities to use information on the global activities of a multinational group in conducting their risk assessment," says Holte. Given this opportunity, and the significant investment by countries and by business to introduce and comply with
CbC reporting, it is vitally important that tax authorities do use CbC reports effectively for the assessment of transfer pricing and other BEPS-related risks.”

“Exactly how do you anticipate them using these reports?” I asked. “A good pointer in my mind is the Country-by-Country Reporting: Handbook on Effective Tax Risk Assessment that we, the FTA, released in 2017,” he responded. “It provides guidance to tax authorities, identifies the types of risk indicators that they may be able to detect and also talks about some of the challenges that will be faced by revenue authorities, such as dealing with false positives,” says Holte.

That handbook, which contains information on 19 tests that any given tax authority may well run on the data, is clearly something that businesses should look at incorporating into their own pre-submission reports. But there will still be questions. I asked if he expected a slow and measured approach to scrutiny, or real “fireworks”?

“Questions will arise that will need to be answered,” he confirmed. “Exactly how many questions and on which issues will depend in part on how a company has completed its report. Table 3 (of the CbC report) provides an opportunity for groups to provide additional information and clarity, and we would encourage groups to use this to the fullest extent possible, particularly where elements of their report may be unclear. The extent to which these questions will lead to more inquiries and examinations is something we will have to wait and see,” says Holte.

“Yes, there will be cases where a CbC report reveals a possible risk. But I should note that there are strict protections to ensure that the information contained in CbC reports is used for the risk assessment of multinationals and not the tax assessment of this group. The OECD has issued guidance on the approaches that tax authorities must follow to ensure they use CbC reports appropriately.”

CbCR reporting is not the only potential source of uncertainty facing taxpayers in 2018, of course; far from it. With the OECD’s multilateral instrument (MLI) entering into force the day after the 30 June 2018 start of CbC report exchange (a coincidence), taxpayers will have another source of uncertainty to address—the advent of a new, untested and arguably highly subjective Principal Purpose Test (PPT). This new test will allow tax authorities to disallow any structure or transaction “if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit.”

As background, the vast majority of tax treaties follow the Model Tax Convention (MTC) developed by the OECD more than 50 years ago. The MTC—and, as a result, most tax treaties—did not contain a General Anti-Avoidance Rule (GAAR) that tax authorities could apply to effectively disallow an entitlement.

This situation fundamentally changes following the BEPS project, where more than 110 jurisdictions have committed to implement a minimum standard on tax treaty abuse. They are doing so through the inclusion of anti-abuse provisions, including the PPT, that are specifically defined in the final BEPS Action 6 Report, Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, into their bilateral tax treaties.

Given the wording of the test, the PPT looks very subjective in nature. Consequently, there will likely be significant uncertainty and differences in interpretation and application of the PPT among different tax authorities. Furthermore the PPT may potentially be limited by local country case law or legislation, such as for instance, the EU Cadbury Schweppes case law.

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Countries are already including the PPT in their tax treaties. In fact, more than 1,200 tax treaties are already scheduled to incorporate the PPT as a result of countries signing the MLI, and with the number of signatories expected to increase from 80 to around 100 jurisdictions soon, more than 2,000 out of a total global stock of around 3,000 treaties currently in force globally will include the test.

So, I asked Holte, “Are our clients right to be concerned that the majority of countries adopting and using a PPT will not have the experience of managing such a test?”

“I think we should start with the rationale for a PPT, which is an important tool to help improve fairness in the international tax system,” says Holte. “It has been clear over the last decade or so that we have seen many instances of complex structures and transactions by multinational groups primarily designed for the purpose of minimizing tax, often to zero, rather than for what the public—the ultimate guardians of the tax system—would consider to be legitimate business reasons. The introduction of the PPT is a direct response, and we hope it will improve the ability of tax administrations to achieve fair outcomes and, hopefully, change the aggressive behaviors of some companies and their advisors."

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“A PPT inevitably introduces a degree of uncertainty, since it is intended to do what more detailed anti-avoidance rules cannot achieve by taking a broader purposive approach.”

“But does it indeed create uncertainty?” I asked. “In order to work effectively, a PPT inevitably introduces a degree of uncertainty, since it is intended to do what more detailed anti-avoidance rules cannot achieve by taking a broader purposive approach. Care has been taken, however, to minimize the uncertainty while achieving that purpose,” says Holte. “A common, international standard on the PPT in the OECD Model Tax Convention, with common guidance in the commentaries, along with an updated preamble should, in my view, lead to a more consistent international approach to dealing with tax treaty abuse. But, as with many aspects of BEPS, it is up to taxpayers and their advisors to reflect on exactly where the appropriate boundaries of tax planning lie against the backdrop of what BEPS is trying to achieve—namely that tax is paid where substantive economic activity takes place.”

Is multilateral assurance the way of the future?
Creating uncertainty is one thing. Reducing it is quite another.

Almost coinciding with Holte’s picking up of the FTA reins comes the piloting of the new ICAP program that he mentioned earlier in our discussion.

ICAP has been designed and is supported on an ongoing basis by the OECD. The ICAP pilot started in January 2018 and will last around 18 months. It involves eight jurisdictions—Australia, Canada, Italy, Japan, the Netherlands, Spain, the UK and the US, with two others, France and Germany, participating in observer roles.

Under ICAP, a group of countries—not always the full eight—will work with the taxpayer to review a package of relevant documentation, including the taxpayer’s CbC reports, and, if all is well, the company will receive assurance that they will not receive further compliance interventions from the covered tax administrations for a period of two years—at least, not driven by their CbC reports, assuming such reports do not change materially.

Any issues that cannot be agreed via ICAP (and therefore require further attention) will be handled outside of ICAP, via processes such as advance pricing agreements (APAs) or, when deemed necessary, a tax audit.

Expanding ICAP’s scope and coverage may present future challenges for the OECD. “What, then, do you think ICAP might look like in three years’ time?” I asked.
“These are early days,” he grinned, being careful to not raise expectations or promise to deliver any miracles. “We’ve observed a good energy from both tax administrators and the pilot companies involved. It’s premature to speculate where we might be in three years’ time. There are clear challenges around how tax administrations and taxpayers manage the right level of resource if ICAP is rolled out more widely - always on a voluntary basis, I might add. But as we progress, it is likely that we will identify ways we can standardize the provision of information and streamline processes - including making more of virtual interactions.”

Transitioning to a post-BEPS world

ICAP represents a novel and innovative approach to trying to develop more tax certainty. Although joint or simultaneous audits (and multilateral APAs, despite their limited number) are arguably multilateral in nature, ICAP is the first formal, highly visible, multi-country tax certainty program to be launched.

One of its stated objectives is to deliver taxpayers with higher levels of certainty and assurance. Another is to encourage taxpayers to change their behavior over time, transitioning more smoothly to a “post-BEPS” world.

In a similar vein, I have had a number of conversations with clients in recent months during which they have queried whether the FTA could develop a similar (but different) multilateral program that might help a taxpayer move from pre- to post-BEPS structures more effectively. This could be via pre-clearing particular structures or transactional approaches, for example. “Is that something that the FTA might look at as a future best practice?” I asked.

“This is something that we are gradually moving toward,” says Holte. “We should not underestimate, however, the amount of devil there is in the detail, and the limits of pre-clearance on something like business models overall, versus something much more empirical like an APA. That said, it should be possible over time to be clearer on what the characteristics are that allow tax administrators, either individual or collectively, to categorize multinationals as lower risk. This would not only help multinationals in setting their own risk parameters, but also help focus the work of tax administrations on areas of higher risk and reducing tax uncertainty.”

Final thoughts

Hans Christian Holte is a generous and fastidiously polite man. At the end of our 90-minute conversation, I asked whether he had any other messages he would like to communicate to EY’s clients.

“I would encourage taxpayers to keep the lines of communication open, and to keep the dialog going. These are new days for all of us.”

“These are indeed exciting times in the tax world,” he confirmed. “Giant steps forward have been made in tax transparency after the global financial crisis a decade ago. Well-designed tax rules, international agreements and new communication technologies are all essential means. But all means and tools must be applied by skilled and competent administrators if the system is to work as intended. New agreements that oblige automatic sharing of vast amounts of taxpayer information will provide new opportunities to arrive at correct results. At the same time, tax authorities have to live up to their responsibilities to protect taxpayer information. So it’s a two-way street, in almost all cases. It always has been, but the world is definitely getting more complex. So I would encourage taxpayers to keep the lines of communication open, and to keep the dialog going. These are new days for all of us.”
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Join EY tax policy and controversy leaders for a review of EY’s eighth annual tax policy outlook report, as they discuss:

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► The impact of BEPS-related changes in 2018, including BEPS implementation via the OECD’s multilateral instrument
► The continuing support for changes and improvements to R&D and other business incentives as governments search for internationally acceptable ways to stay competitive
► The outlook for digital tax policy
► The outlook for G-20, OECD and European Commission activity in 2018
► How other governments may consider responding to US international tax reform from a policy perspective
► Key enforcement trends and audit triggers around the world

Tax administration goes digital

Join our panelists as they review the key findings of new EY report, focusing on:

► The drivers behind the accelerating digitization of tax administration
► Global and regional trends
► Country cases studies from Brazil and Norway
► Current digital audit triggers and controversy focus issues
► A framework approach that companies may wish to consider implementing in response to new requirements
► What the future may hold

Cross-border controversy implications of US tax reform

This webcast covers the reactions by some foreign tax authorities, particularly within the European Union, with respect to certain provisions of the TCJA. Reactions include issues raised in connection with:

► The potential double taxation and/or treaty discrimination caused by the base erosion and anti-abuse tax (BEAT)
► Whether foreign-derived intangible income (FDII) creates a potential regime that may be inconsistent with Action 5 of the OECD’s BEPS project

ey.com/webcasts
As global business becomes ever-more digital, a growing number of policymakers and commentators argue that tax protocols developed almost 100 years ago are now struggling to keep pace. In response, some countries and supranational groups are exploring different digital taxation models for the future. The details of such models are a moving target at present, and the current lack of agreement on how to proceed threatens to leave behind it a confusing tax landscape made up of a patchwork of different tax policies.

The outcomes to this situation could be confusion about which types of business activity are subject to tax, distortion of business decisions, double taxation, tax disputes, and potentially unanticipated increased costs to the existing and future digital strategies of businesses.

In this article, we will look at the European Commission’s (the Commission) digital tax proposals at summary level, before looking more closely at what is driving the debate, what potential outcomes we may see, by whom, when and under which processes.
French President Emanuel Macron proposed a new tax on internet companies in the following activities:

The taxpayer-reported 3% tax would apply to revenue from activities in which users are deemed to play a major role.

The first proposal is described as an “interim” 3% digital services tax (DST) on gross revenues (i.e., turnover) derived from users’ participation in the digital activities that some (but definitely not all) countries that there is a mismatch between where profits are currently taxed and where and how certain digital activities create value. To be clear, notwithstanding the fact that taxing digitalized activity was first addressed within the OECD’s BEPS project, the current debate is not about tax avoidance or the existence of stateless income. It is, rather, about the division of tax rights among countries who consider that their citizens contribute to the profits made by some digitally focused companies, even if they do so via unconventional means.

The Commission believes the value creation mismatch is the result of a combination of several factors. First, they say that businesses can today supply digital services where they are not physically established, which the Commission describes as “scale without mass.” Second, they posit that digital business models tend to have a heavy reliance on intellectual property assets, and are therefore more mobile. And third (and perhaps the biggest challenge in the debate) the Commission believes that a higher level of value than currently assessed comes from user participation in the digital activities that some platforms enable—commonly described as “user value creation”.

To combat this perceived mismatch, the Commission in late March released two digital tax proposals that, if enacted in their current state, could significantly increase tax costs and compliance burdens for many businesses around the world.

The first proposal is described as an “interim” 3% digital services tax (DST) on gross revenues (i.e., turnover) derived from activities in which users are deemed to play a major role in value creation.

The taxpayer-reported 3% tax would apply to revenue from the following activities:

A. The placing on a digital interface of advertising targeted at users of that interface;

B. The making available to users of a multi-sided digital interface which allows users to find other users and to interact with them, and which may also facilitate the provision of underlying supplies of goods or services directly between users;

C. The transmission of data collected about users and generated from users’ activities on digital interfaces.

Companies with total annual worldwide revenues of €750 million or more and that have annual EU taxable revenues of €50 million or more would be subject to the tax.

Certain types of companies—such as digital advertisers and platforms designed to allow users to connect with one another and trade in goods and services—would be within the scope of the tax as currently proposed, while others, such as online marketplaces without user-to-user selling, would be outside the scope. But the tax status of many other types of companies is far less clear. For example, many companies may sell information about their consumers to other companies (such as market researchers), but only a portion of the data may be from “digital” sources as defined by the Commission. It’s also unclear whether background data analytics and data transmission to and from the cloud by businesses offering Software-as-a-service (SaaS) are included in scope.

The Commission’s second, longer-term proposal is far broader, with more than 50 different digital activities potentially subject to tax. A “significant digital presence” (SDP) concept would result in a new digital permanent establishment (PE) definition, intended to establish taxable nexus, along with revised profit allocation rules to determine how the taxes on digitally-derived profits are distributed among countries.

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1 French President Emanuel Macron proposed a new tax on internet companies in April, although without providing any detail. Other examples include Italy, which established a 3% web tax on digital transactions, effective January 1, 2019; Slovakia, which amended its income tax in January 2018 to add a tax on providers of services on digital platforms; Hungary, which proposed an internet tax in October 2017; and India, which introduced an equalization levy on online advertising revenue in 2016 and a revised permanent establishment concept in 2018.

The United States has stated on record that it is opposed to tax policies and proposals that single out digital companies.

Under this proposal, a company would be considered to have a significant digital presence (and therefore a PE) if the entity meets any one of three criteria:

- It exceeds €7 million in annual revenues from digital services in an EU Member State
- It has more than 100,000 users who access its digital services in a Member State in a tax year
- It enters into more than 3,000 business contracts for digital services in a Member State in a tax year

If subject to tax, the company would pay the headline corporate income tax rate in an EU Member State.

As drafted, both proposals are scheduled to go into effect January 1, 2020, although in reality, the timing of both remains far less clear. And while the longer-term proposal mirrors ongoing discussions occurring at OECD level, it would dramatically change the way cross-border tax norms operate today. If enacted at the EU level, it would require tax treaties to be renegotiated between countries and a change to the OECD’s Model Tax Convention. That scenario could result in two different tax systems—one for the EU, and another for the rest of the world.

The challenging concept of unanimity

To be implemented, both of the Commission’s digital tax proposals would need to gain unanimous support among EU Member States. Individual countries’ political and economic concerns may make this challenging, especially for the “interim” DST proposal, which some Member States fear may negatively affect some key industries and trade relationships.

There is a possibility that the “enhanced cooperation” measure of the EU —seldom used— could be exercised if nine or more Member States wish to take the proposal forward. If either scenario fails to play out, an alternative (and, we suggest, unwelcome) outcome is that a number of EU Member States could simply move forward, unilaterally, with their own digital tax measures.

OECD: we agree to disagree

The OECD originally initiated, and has thus far led, the digital tax debate in connection with its ongoing BEPS project. Just a few days before the Commission issued its proposals, the Paris-based OECD issued an interim report on the tax challenges of digitalization, concluding that there is no consensus on the merits of an interim tax such as the one proposed by the Commission.

Indeed, the OECD report eschewed specific recommendations and stated that the 116-nation strong BEPS Inclusive Framework (the group of jurisdictions that have agreed to implement the BEPS minimum standards) instead chose to further analyze the issues and complexities involved in developing policies in this area.

The report affirmed the OECD’s goal of producing a final report in 2020, and an update to G20 leaders in 2019. Some EU Member States, meanwhile, have also expressed their preference to wait for the OECD’s long-term recommendations, further complicating the situation.

US stance

The United States has stated on record that it is opposed to tax policies and proposals that single out digital companies, and Chip Harter, US Deputy Assistant Secretary (International Tax Affairs) to the Treasury has been reported as saying, for example, that “permanent establishment issues are no longer a factor in the digital tax debate because the largest MNEs have shifted or are in the process of shifting to structures that use local low-risk distributors to report income on locally filed tax returns, relying on transfer pricing principles to determine how much profit to report.”

In fact, some of the resistance by EU Member States to the Commission’s interim proposals may be based on concern about US retaliation at a time when trade tensions are particularly high.

Where do we go from here?

Timing issues and impacts

The Commission hopes that both tax proposals will be submitted to the Council (the decision-making body of the EU, made up of all heads of state of all EU Member States) for adoption with final national adoption occurring by 31 December 2019 for 1 January 2020 transposition into EU Member States’ national laws.

But these dates are very tentative, and indeed, the SDP proposal in particular will require consensus agreement of a magnitude that is arguably similar or even greater than that of key ATAD measures themselves, given the potential redifision of taxing rights it represents.

Moreover, should consensus indeed be reached, the SDP will take significant time to execute as it will require changes to hundreds of double tax conventions.

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1 This measure would not bind the remaining Member States.

A host of converging factors (many of which are deeply political) mean that it is quite possible that many nations—both in and out of the EU—will move forward and adopt independent turnover taxes of some form in the short to medium term.

That scenario in turn drives one of the most commonly-voiced criticisms of the DST—that the likely extended timeline for implementation of the SDP means that the "interim" DST may well have far longer duration than anticipated.

For either proposal to reach national enactment, much needs to occur during the coming four to six months. It is also worth bearing in mind that the EU legislative process is known for generating outcomes that can sometimes look somewhat different from what was originally envisaged.

The situation is not this clear cut; a host of converging factors (many of which are deeply political) mean that it is quite possible that many nations—both in and outside the EU—will move forward and adopt independent turnover taxes of some form in the short to medium term.

Recent media reports, meanwhile, have stated that some countries (including Germany) may have cooled on the Commission’s 3% DST proposal in particular, fearing that it may indeed be an inhibitor to domestic activities or that it may prompt retaliatory measures.

So, while the wheels have by no means “come off” the Commission’s proposals, the go-forward picture may present an increased risk of unilateral actions on digital—which, of course, will mean more double taxation and more disputes.

A closer look at the drivers of the debate

Answering the question of “what happens next?” also requires a far closer look at some of the key issues behind the debate, as well as a study of how those issues link to political motivations.

As noted, this debate is not about tax avoidance. Equally, nor is it about taxing the end consumer of digital goods or services; that has largely been addressed via the application of VAT or GST in many jurisdictions. Rather, it is about taxing net profits and the division of taxing rights among countries.

Many countries agree on what is driving the perceived need for change—i.e., the potential mismatch resulting from the interplay of the concepts of scale without mass, increased reliance on intellectual property and the contributions made by digital users and the value of the data they create. What is less clear is how, when and by whom these issues will ultimately be tackled in terms of new tax policies.

This is a very political exercise at its heart, both domestically and internationally, and the digital tax issue is but one related strand in a multifaceted web of issues.

The EU’s legislative process

The EU’s legislative process will also contribute to the complexity of developments. The European Commission is but one player in a novel and unique legislative approach that each proposal issued by the Commission must transit.

The European Commission has the sole right to introduce new tax proposals; once a proposal has been introduced, it is effectively sent to the appropriate tax working group(s), which is where the detailed work is performed, with participants from all Member States meeting regularly to discuss the details of the proposal and to try and reach a consensus position. In these discussions, the working groups are free to make whatever amendments they want to what the Commission has proposed.

So, effectively, a proposal can be disassembled and then reassembled by the working group(s). The Commission can, but very rarely does, take a position that the working groups have distorted their original proposal so much that it is unrecognizable from its original form, and withdraw the proposal. Normally, however, what occurs is that the discussion carries on, as there is no time limit to the discussion—as has been the case with 2011’s CCCTB proposal.

Once the working groups have developed a proposal into a form acceptable to all Member States, the Council adopts it, according to a timeline set by the Commission—typically (but not always) allowing for a year or more of lead time for domestic legislation to be prepared. The European Parliament (made up of 750 elected members) must be asked for an opinion on the final proposal, but such opinion is not binding upon the Commission.

See the article on page 20 for a more in-depth analysis of the EU’s tax legislative processes.
There is, however, an “escape clause” from unanimity, though it is very rarely used and has only been tried once on the tax side and twice on a wider scope.\(^6\)

Known as “enhanced cooperation,” the procedure may only be invoked if the Council (made up of representatives from the 28 Member States, the legislative decision-makers in all cases) fail to agree on a final proposal and proceedings come to a halt, but more than nine Member States still want to move forward. The Commission can withdraw the current proposal and come forward with a new proposal, under enhanced cooperation, under which the final laws will apply only to those Member States that participated in enhanced cooperation and therefore agree to be bound by them.

**The current DST proposal: potential outcomes**

Given the contours of the political landscape, coupled with the novelty of the EU’s legislative process, it is possible that one of the following scenarios will play out:

- EU Member States choose not to use their veto for an issue with relatively small revenue impacts, and we see a new DST via unanimity
- A group of EU Member States move forward under the enhanced cooperation mechanism
- A group of EU Member States moves forward with a similar set of measures, but outside of the Commission’s mechanisms
- EU Member States wanting a DST move forward with their own unilateral measures, creating a patchwork approach of inconsistently designed measures

Overall, it is also worth noting that the sense of confusion and lack of consensus in regard to the Commission’s proposals is arguably driving a return of the world’s focus to how the OECD will address the issue.

Do recent unilateral actions indicate any particular sense of direction?

In short, yes. Not unexpectedly, we already see a number of related developments playing out, and not limited solely to the EU bloc. For example:

- On 30 April 2018, Spain proposed the introduction of a Digital Services Tax, which is now expected to effective in 2019. Even though no draft of the proposed new tax has yet been disclosed, it will presumably be aligned with the EU’s DST proposal. If the EU measure is developed as anticipated, the scope of Spain’s new law is expected to be the same as that of the EU’s 3% DST. The Spanish tax is likely to be introduced unilaterally.
- Likewise, Austria is expected to publish forecasted revenues from the proposed 3% DST on gross revenues on digital transactions, analyzed by category, according to the three areas of business activity identified by the Commission. Austria is also believed to be drafting domestic legislation around both the DST and the SDP, allowing adoption domestically should the EU proposals not move forward. An open question remains as to what rate Austria may apply; it may follow the 3% rate put forward by the Commission, but equally could look toward a 4% or even 5% rate, on the basis that a precedent-setting tax is already in place in Austria.
- Australia’s 2018 budget was held on 8 May 2018. The treasurer stated in his speech that the “next big challenge is to ensure big multinational digital and tech companies pay their fair share of tax.” He further stated that he has been working with the G20 to bring the digital economy into the global tax net and that in a few weeks he will release a discussion paper that will explore options for taxing digital business in Australia. This all comes not long after the Australian Financial Review reported the treasurer as stating that he would not wait for other countries to go it alone, and that “The absence and delay in arriving at a multilateral solution will only continue to invite unilateral action by individual jurisdictions. As a consequence future multilateral action will likely be more focused on harmonizing approaches already commenced, than establishment.”\(^7\)
- Two months earlier, on 13 March 2018, the UK Government noted that the participation and engagement of users is an important aspect of value creation for certain digital business models, and is likely to be reflected through several channels, such as the provision of content or as a contribution to certain intangibles such as brand. The preferred and most sustainable solution to this challenge, says the UK’s policy paper, is reform of the international corporate tax framework to reflect the value of user participation. In the absence of international reform, the paper notes there is a need to consider interim measures, such as revenue-based taxes. The Government thinks there are benefits to implementing an interim measure on a multilateral basis and intends to work closely with the EU and international partners on this issue. However it notes that the UK is willing to act unilaterally. As recently as 10 August 2018, the UK Chancellor told Sky News that the Government wants to ensure that taxation is fair between businesses doing business the traditional way and those doing business online and that “requires us to renegotiate international tax treaties because many of the big online businesses are international companies”. He went on to say that the Government “may have to look at temporary tax measures to rebalance the playing field until we can get international agreements.” The Chancellor noted that “The EU has been talking about a tax on online platform businesses based on value generated” and said “That’s certainly something we’d be prepared to consider.”

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\(^6\) In the areas of patents and divorce law.

The likelihood is that new taxes on digital activity of some form will soon need to be factored into businesses’ strategic plans.

- Finally, the OECD is expected to publish statistics on digital penetration in OECD countries and to make available simulations of various instruments that may tax either profits or turnover — i.e., virtual PEs, withholding taxes, and excises/levies.

What to watch for next

The Bulgarian Presidency issued a digital taxation roadmap document on 23 May 2018. In the roadmap, the Presidency outlined its desire for the Commission’s Working Party on Tax Questions (WPTQ) to complete a first round of detailed technical analysis on the DST by June 2018, allowing the Presidency to then table a first DST compromise proposal.

The WPTQ is a group made of members from each of the 28 Member States which now has the challenging task of disassembling and then trying to reassemble the DST proposal into something around which consensus can be secured, given the need for unanimity in tax matters at EU level. Here, it has been widely reported in various tax journals recently that a series of changes have been suggested to the DST.

These changes come in the form of a leaked version of the original proposal which in turn contains a whole series of questions posed by the Presidency. It is not – at this stage – a revised proposal, but more a series of open questions for consideration by the Member States. While the compromise proposal contains 15-20 changes overall, two of the open questions in particular stand out.

First, the (Bulgarian) Presidency asks “Would delegations consider narrowing down the scope of the Directive by excluding the services in Art. 31(c)?” (i.e. “The transmission of data collected about users and generated from users’ activities on digital interfaces”). The proposed DST threshold of 750 million Euro of worldwide revenues, one of two DST thresholds, is marked for potential deletion, with the Presidency asking “Would Member States consider reviewing the thresholds regarding worldwide revenues?” To do so would potentially leave the DST with a single monetary threshold, that of 50 million Euro of taxable revenues obtained by the entity within the Union during the relevant financial year.

On the SDP, the roadmap notes that the same technical analysis is expected to be completed by June 2018, and the WPTQ meetings of 4 and 5 June 2018 will be dedicated to SDP discussions. The roadmap makes no mention of a similar compromise proposal on the SDP, however, instead noting that “…work on this legislative proposal will have to be calibrated with a view to monitoring and reflecting, as appropriate, progress made in the G20/OECD debate, which is expected to be concluded by 2020.”

Concluding thoughts

Many factors, including politics and economic interest, are shaping the current digital tax debate. Not least, the new Austrian Presidency has signalled that the interim measure will be given high priority during its term, which runs from July to December 2018.

While many details are still evolving, the likelihood is that new taxes on digital activity of some form will soon need to be factored into businesses’ strategic plans.

Given the complexity of the issues outlined in this article, companies should begin studying existing and planned digital activity with a new lens, and to bring tax into the wider business strategy conversation. Putting in place or increasing efforts to assess, quantify, plan for and comply with changes at both multilateral and national levels will be a pre-requisite, moving forward.

Scaling the digital tax divide

What boards and executive leadership need to know about the proposed digital tax policies

Given the complexity of the issues outlined in this article, company boards should begin viewing their existing digital activity and pipeline projects with a new lens, and to bring tax into the conversation.

Digital tax issues may also need to be incorporated into investor communications. Investors need to know about tax issues related to digital activities that may reduce profits if these taxes go into effect. They also should be informed about the possibility and potential impact of restructuring parts of a digital strategy or even the need to exit lines of business or markets completely depending on how tax proposals advance.

Scaling the digital tax divide is a short, new EY article designed with the C-suite, board and audit committee audience in mind. It is designed to help educate these audiences on why this digital debate is occurring, setting out the high level contours of the debate and the related proposals, and offering executive leadership a number of questions to ask themselves. Scaling the digital tax divide can be downloaded at www.ey.com/insbriefing.

ECOFIN is an Economic and Financial Affairs Council configuration — made up of the economics and finance ministers from all member states. Relevant European Commissioners also participate in meetings.
As noted in the previous article, late March 2018 saw the European Commission (EC) issue two new proposals that could potentially change the way digitalized business activity is taxed. Their technical composition aside, the proposals—which could deliver two new EU Directives—immediately raised questions from businesses who wanted to know the likelihood of the proposals passing into law, the timeline on which that may occur and whether or not the technical contours of the proposals are likely to change between now and becoming law.

The legislative processes of the European Union (EU) are unknown to the vast majority of people, and they pose many questions: Does every EU Member State need to agree with the proposals for them to pass into law? Which groups or bodies can influence the final composition of a Directive? Can Member States opt to enact parts but not all of a proposal? In this discussion, EU tax and law professionals Dr. Klaus von Brocke and Steve Bill walk readers through some of the key steps that these proposals will now be passing through. While not an exhaustive guide to EU governance and processes, it provides a short, effective briefing for tax professionals.
Basis of EU law

Steve Bill: Starting at square one, EU taxes are, and will remain for the foreseeable future, very much under the control of sovereign states. National and local governments levy all taxes within the EU and retain all receipts. Other than the sole exception of customs duties, the European budget is financed by direct levies on Member States.

Since the EU itself doesn’t levy taxes, why does it get involved in taxation matters at all? The answer to that is quite simple: the EU has an “internal market” that requires some harmonization of Member States’ tax laws to function properly. In particular, and since 1993 when the internal market was set up, there has been a very high level of harmonization of indirect taxes, particularly VAT and excise duties. This is the complete opposite to the US, where indirect local sales taxes are not at all harmonized.

Harmonization has occurred because the EU constitution (the Treaty) has an article that enables the Commission to make proposals specifically for indirect taxes. The Commission must justify that these proposals improve the functioning of the internal market or help competition within the internal market. This typically falls into two categories. First, there are instruments that are designed to make tax law less onerous for businesses carrying on intracommunity trade. Second, there are instruments for exchanging information and mutual assistance that make it easier for tax administrations to cooperate and to assist each other.

Rob Thomas: Klaus, can you help us understand those articles in the Treaty for the Functioning of the European Union (the EU Treaty) on which the proposals for the taxation of digital activities are based?

Klaus von Brocke: First, Article 113 gives the European Union competence to harmonize indirect taxation. For its part, Article 115 is normally used as the basis for direct tax measures designed to reinforce the functioning of the EU internal market, which is intended to be an area without any barriers to the free flow of goods, capital, services, and persons (for both individuals as well as companies).

From the point of the European Commission, the problem with Article 115 is that it has very strict conditions that must be fulfilled. It is important to note the principle of subsidiarity, which means that the Commission can only make proposals on a specific matter if it can justify that the matter cannot be dealt with in a better and more efficient way at the level of the individual Member States. In other words, the Commission has to demonstrate that a specific problem can only be alleviated if all 28 Member States harmonize their law in a specific area.
The incumbent presidency has the power to set the agenda for the Council’s work and to drive discussion on the specific proposals that it particularly wishes to see adopted. The current President of the Council is Austria, while the last President (from January to July 2018) was Bulgaria, under whose guidance the issue of taxation in the digital economy was made a top priority. Romania will hold the next presidency, beginning 1 December 2018.

Rob Thomas: Let’s move on and talk about the cast of players, if I can call it that, in the EU theater. We have a number of different players that play different roles in the legislative process.

Klaus von Brocke: At the top of the whole institution is the European Council, where all the heads of state and governments meet and deal with pressing current issues. It is a political, rather than a legislative body. More important for day-to-day legislative work are the next three institutions: the Commission, the Council of Ministers, and to a lesser degree, the European Parliament. The European Commission has a hybrid role. On the one hand it is the “guardian” of the EU Treaty and has responsibility for surveilling the manner in which the Member States implement EU law. On the other hand, it has the sole right to initiate legislative proposals, which it formulates and then presents to the Council of Ministers and the Parliament.

For its part, the Council of Ministers, where all the 28 Member States are represented, has the sole legislative right in taxation matters. So, the Commission proposes, but the Member States in the forum of the Council of Ministers actually decide. Moreover, in the field of taxation, there is a requirement for unanimity — i.e., all 28 Member States have to agree before a proposal can be adopted as law. Lastly, the European Parliament has a purely advisory role in respect of taxation proposals made under Articles 113 and 115. If the Parliament disagrees or proposes amendments, neither the Commission nor the Council is required to take on board its comments.

Finally, there is the EU Presidency. The Treaty lays down a system of rotation whereby each Member State assumes, for a period of six months the responsibility of chairing and leading the work of the Council of Ministers.

The detailed discussion of proposals put forward by the Commission is carried out in the relevant Council Working Group, in this case, the working party on tax questions (WPTQ), which is comprised of officials from all Member States. When proposals are ripe for conclusion, or when particular issues arise that require political guidance, they are referred to as ECOFIN, which normally meets once a month to discuss an agenda drawn up by the Presidency. COREPER, which is the standing committee of the Permanent Representatives of the Member States, prepares these monthly meetings.

Also of importance in the tax area is the Code of Conduct on Business Taxation group. This is a standing committee of Member State officials that has been set up by the Council outside the normal legislative framework. It appoints its own chairman and thus does not have the rotating Presidency of normal Council groups. It was initially established as a peer review group designed to eliminate “harmful” tax practices.

Rob Thomas: Klaus, regarding the Code of Conduct group, we almost see that as working in parallel with the OECD’s group that looks at harmful tax practices under BEPS Action 5. Is that EU Code of Conduct group also looking at some of the US tax reform proposals that some Member States do not necessarily like?
Klaus von Brocke: The agenda for the Code of Conduct group, until 2020, is focused on three areas. The first is a further round of examination of peer reviews of potentially harmful tax practices. The second issue is the role of monitoring the EU’s “black” and “grey” lists of non-cooperative jurisdictions. The third issue involves monitoring the newly-enacted mechanism to avoid double taxation.

Rob Thomas: Steve, what does the actual legislative process tend to look like—and I use the word tend, because it does not always play out as expected? Who are the really important players in terms of taking an idea through to actual national implementation in the EU?

Steve Bill: The process normally starts within the Commission’s Directorate General for Taxation and the Customs Union (known as “DG Taxud”). The Commission identifies areas where it considers that legislation is necessary in order to improve the functioning of the internal market and/or to reduce the distortion on competition.

In order to establish the necessity for a proposal, the Commission normally carries out an impact assessment, which includes a public consultation. If there is justification, the Commission comes forward with a proposal which is then sent to the Council of Ministers and the Parliament.

At this stage, the Member States’ ministers make an initial review of the proposal at one of their monthly ECOFIN meetings, then send it down to the WPTQ, which is where the real work gets done. Here the representatives meet regularly and discuss the details of the proposal. In those discussions, guided by the Presidency, the Council is free to make whatever amendments it wants to what the Commission has proposed. The Commission participates in the discussion, but cannot prevent the Council from amending its proposal. The only sanction that the Commission has, and this very rarely happens, is to withdraw its proposal.

There is no time limit to the discussions and the Council is not obliged to adopt a Commission proposal. Given that there has to be unanimity in tax matters, it is not unusual therefore for discussions to carry on inconclusively for several months or years and for the Council to finally stop its discussions. At that point, the Commission may withdraw its proposal and go back to the drawing board.

There are basically two types of proposals; one type is designed to harmonize the tax rules in the EU Member States, (in order to make trading easier within the EU), and the other is designed to improve cooperation between Member States. The first proposals are the difficult ones, because Member States may not be very keen to agree to something that means that they have to change their tax laws. On the other hand, when the Commission comes forward with proposals to improve cooperation between Member States, not unsurprisingly, the Member States perk up their ears and seem to be much more keen and ready to agree.

Where does the Parliament fit into all of this? The Parliament merely gives an opinion. The Council cannot adopt a proposal if it does not have an opinion from the Parliament, but it does not have to take any account of that opinion—and often does not.

There is an escape clause from unanimity, but it is very rarely used, and has only been tried once in the tax area and in fact, has only been used a couple of times in all. This is the so-called “enhanced cooperation” mechanism. This is a procedure that can be enacted if the Council fails to secure the necessary level of agreement but a group of nine or more Member States indicate that they still want to do something in the relevant area. The Commission may withdraw its initial proposal and come forward with a new proposal that would only be applicable within those Member States who want to be bound by the new rules. It will only really be used when the discussions have halted, but there has been significant agreement between a significant number of Member States on the type of rules that they would like to see introduced.

Basically, enhanced cooperation should only really come right at the end of the process where Member States have gone through all the pain of rewriting and agreeing the text and then finding that a few Member States will not sign up to.

Rob Thomas: Let’s talk about all this in relation to the digital proposals. We have two proposals, one short term and one long term. The first is a 3% gross revenues tax and the second is a significant digital presence – or in other words, a change to both nexus and profit attribution rules.
Legislative process – digital

Rob Thomas: First I’d like to ask about the timing issues. Is this a phased approach, or is it possible that the Council could actually move forward with the gross revenues tax at a faster pace than the Commission may have initially indicated?

Klaus von Brocke: There was a bit of confusion out there when these proposals were published. The digital services tax should only last as long as there is no agreement on the permanent solution, as the term “interim solution” indicates. What we understood was the timings in the draft were put into brackets because of the upcoming elections of the European Parliament next year. In any case, the timings proposed by the Commission are always an aspiration and do not in any way bind the Council. What is interesting, though, is the speed at which the various subgroups have started work. ECOFIN ministers quickly took note of these two proposals, and the relevant working parties immediately started to examine them. This illustrates how seriously the EU Member States take this issue.

Rob Thomas: Thanks for that Klaus. Steve, is it fair to say that the Commission really wants to use the gross revenues tax proposal merely to create momentum behind the longer term solution?

Steve Bill: Member States were looking at what was going on in the OECD and they weren’t happy that the OECD was saying, in effect, that special digital rules are not necessary since the current general rules are sufficient. What these Member States fear is that they are not getting their fair slice of the tax cake and therefore want some form of indirect tax, at least in the short term. So, at the end of 2017, they asked the Commission to come forward with an appropriate proposal. But the Commission already had its own ideas on what was necessary, which is set out in the second proposal, and which could easily be embodied in the already-proposed Common Consolidated Corporate Tax Base.

Rob Thomas: Klaus, do you have a picture of who is for and against at this point in time and what impact might that actually have as the Council meetings move forward?

Klaus von Brocke: You have, of course, the obvious ones, mainly the smaller countries who are against this kind of proposal, such as Ireland, Netherlands, Luxembourg, but you also have a very prominent Nordic country, Finland, which hosts quite a lot of multinationals, that is also against this proposal. That doesn’t necessarily mean they will end up voting against the proposal, however; this is a very political situation.

On the other side, you have five big Member States, in France, Germany, Italy, Spain and the UK who, alongside Estonia, originally initiated this action. We understand that Germany in particular was initially strongly in favor of the digital services tax and not just as an interim solution. But politics changes rapidly, and we’ve seen Germany in particular soften its stance quite considerably lately.

RobThomas: Steve, the existing VAT Directive that says Member States may not move forward independently with other turnover taxes. On this basis, are Member States precluded from moving forward with a gross revenues tax independently if they feel that the timeline of the Commission, because of all this internal debate, is too long?

Steve Bill: It’s not clear whether the type of digital services tax that some Member States are introducing would be an “illegal” turnover tax. Similar type gross turnover taxes implemented unilaterally in the past by Member States, have been found by the European Court of Justice to be illegal. The adoption of a Directive would overcome that impediment, and, while the proposal is on the table, I think it would probably be open to Member States to pre-empt the adoption of that proposal and to move forward unilaterally. I am sure the Commission itself certainly would not open infringement proceedings against a Member State that was going in the direction that the Commission had proposed that they should go. Thus, for the short term at least, I don’t see any impediment to Member States acting unilaterally.
Eight for 2018 and beyond is a series of transfer pricing-related articles designed to provide a review of key focus points for the coming year and beyond. In this excerpt of the first article in the series, we provide a special focus on the transfer pricing aspects of the sale or transfer of intellectual property (IP).

2017 was an eventful year for global tax reform and 2018 is shaping up to deliver much the same outcome, if not more. And with many changes already scheduled for 2019, this three-year period looks set to deliver transformation in all areas.

We will see many countries continue to implement the Base Erosion and Profit Shifting (BEPS) action items of the Organisation for Economic Co-operation and Development (OECD) at a high pace in 2018, including signing the multilateral instrument (MLI) and various tax-related exchange of information agreements. The European Union (EU) is working on several initiatives that go beyond what has been agreed upon by OECD member countries. And US tax reform has been enacted, with many countries now in the process of reacting to it.

It will also be marked as the year in which companies around the world really start to understand how all of these changes combine to impact their businesses and how they may need to adjust. At the same time, reform initiatives, far from abating, will continue, especially in the area of digital taxation, an area where intangibles play a strong role.
From an IP valuation/transfer pricing perspective, the TCJA effectively codifies valuation principles long espoused by the US Treasury and the IRS.

Against this backdrop of relentless and fundamental change, long-term trends continue to play out. In fact, whatever year it is, the leading cause of risk in successive EY Tax Risk and Controversy Surveys is perennially agreed to be transfer pricing (TP). In this article, we identify and elaborate on eight key TP risks (among others) that companies should proactively address in 2018 and beyond.

We will then pick up and explore our first identified TP risk in more detail — that of the challenges of addressing the sale or transfer of intellectual property (IP) — before returning in subsequent articles to discuss the remaining topics.

Eight key transfer pricing risks for 2018 and beyond

- Intellectual Property (IP) related developments
- Intercompany financing transactions
- High-value services transactions
- Headquarters and management services transactions
- The procurement function and permanent establishment risk
- Limited-risk entity structures
- Two-sided nature of pricing a transaction
- Limitation of deductibility of costs based on domestic rules instead of based on TP adjustments

Access ey.com/tpcbriefing for future articles in this series

A review of ongoing IP-related developments

As the world transitions from the industrial to the digital age, IP is increasingly becoming a primary driver of business profits. Therefore, the importance of IP-related TP is also growing.

At the same time, the crucial features of IP that distinguish it from other assets is that it is highly mobile, and at times difficult to define and price when compared to other assets or services. The key issues related to IP and TP therefore tend to be:

- Identification of the asset: what is the IP subject to analysis?
- Delineation of the transaction: who owns, uses and contributes to the development of the IP?
- Valuation: what is the value of the IP?

There are multiple converging trends affecting some or all of these key issues, including US tax reform, the OECD-level debate on intangibles and the global debate on digital taxation. Furthermore, it should be noted that many differences of opinion exist between mature and emerging jurisdictions.

US tax reform related to IP

One of the most important developments regarding IP expected to impact companies’ related strategies in 2018 and beyond is US tax reform, i.e., the Tax Cuts and Jobs Act (TCJA), which contains several changes related to how IP is defined and taxed from a US perspective.

Most importantly, the TCJA codifies an expansive definition of what constitutes IP, which now explicitly includes workforce in place, goodwill and going concern as IP within the meaning of Section 936(h)(3)(B).

A further important change is the introduction of the global intangible low-taxed income (GILTI), foreign-derived intangible income (FDII) and base erosion anti-abuse tax (BEAT) measures. A collective impact of these changes is that, on one hand, it makes the US a more competitive location in which to develop and own IP. On the other hand, however, it may limit the options that companies have to restructure their supply chains through outbound IP transactions.

From an IP valuation/transfer pricing perspective, the TCJA effectively codifies valuation principles long espoused by the US Treasury and the IRS. Therefore, terms such as “workforce” or “goodwill” should not be used to inappropriately justify transfers of value without compensation. However, it should not be the case that all aspects of the accounting value of goodwill, workforce, etc. are necessarily compensable. Instead, the determination of appropriate compensation will not simply turn on the classification of the contribution. Depending on the nature of the IP covered in the intercompany transaction, comparable uncontrolled transactions (CUTs) may be considered less reliable going forward. The aforementioned notwithstanding, the income method, properly implemented, is still a (potentially) appropriate method, depending on individual facts and circumstances.

Due to the expanded definition of IP, as well as the move to a semi-territorial tax regime, corporate taxpayers should expect an increased focus on TP by US tax authorities as well as from non-US tax authorities/governments as they respond to US changes.
Companies should therefore closely examine the impact that US tax reform has on their IP structures, including:

- Alignment of IP with value creation
- Ability to shift manufacturing footprint
- IP or principal company structure in US
- The location of research and development (R&D) centers

To the extent that such structures are covered by an existing advance pricing agreement (APA), companies should evaluate the implications of US tax reform.

In summary, companies need to evaluate the costs and benefits of their current IP strategy in relation to US tax reform. The most important factors to consider in this regard are the location of current IP (US, foreign onshore, foreign offshore), foreign and US tax rates, connectedness to business/supply chain/customers, substance, the interplay of the new GILTI, FDII, BEAT taxes and costs of IP migration/unwind.

Rest-of-world responses to US tax reform

Nations around the world will be impacted by US tax reform, but the US’ trading partners are being careful to react to US tax reform in a thoughtful and measured manner, taking time to assess the implications of US reform on their foreign direct investment (FDI) inflows and on taxpayer and investor behaviors.

For the past two annual editions, the EY Tax policy outlooks have noted that a number of countries are either creating or enhancing their R&D and other business incentives, looking for “acceptable” ways to stay tax competitive within the constraints of BEPS. Whether this activity accelerates further in light of US tax reform is open to debate, but it would not be surprising. Likewise, the IP-related measures in the US tax reform package may take some time to impact taxpayer and investor behaviors. All things considered, this is an area to watch with interest in the coming months and years.

The European Union is believed to be assessing whether to take action against certain TCJA provisions, suggesting that certain of the international tax provisions are discriminatory or in violation of World Trade Organization (WTO) rules. The tax press is reporting that the EU has requested that the OECD Forum on Harmful Tax Practices conduct a “fast track” review of certain of the TCJA’s provisions. The request reportedly came after a meeting of EU finance ministers in which the Europeans discussed how to react to the tax reform law and whether to take action in the WTO.

According to the report, a recent EU document states that the new BEAT may contravene the OECD Model Tax Convention’s Article 24 on non-discrimination. The document reportedly also addresses the TCJA’s FDII provision.

All this comes after the European Commission (EC) indicated it will survey European MNCs on how the TCJA’s international tax provisions may affect them. A questionnaire has been issued to companies, asking them to describe the type of transactions and business operations that will be affected by certain TCJA provisions, and whether they plan to change their business strategies as a result.

Transparency

A further development at EU-level impacting IP planning in general is that the Council of the EU has reached agreement on a draft directive aimed at boosting transparency to tackle what it sees as aggressive cross-border tax planning.²

The draft directive (known as the Mandatory Disclosure Regime), which took effect on 25 June 2018, will require “intermediaries” such as tax advisors, accountants and lawyers that design and/or promote tax planning arrangements to report transactions and arrangements that are considered by the EU to be potentially aggressive. If there is no intermediary utilized, the obligation falls to the taxpayer.

Given the breadth of the transactions and arrangements covered, relevant reporting obligations in respect of IP sale or transfer will likely result for both companies headquartered in Europe and for non-European companies active in Europe. Determining if there is a reportable cross-border arrangement raises complex technical and procedural issues for MNEs and their advisors.

The OECD-level debate on IP

Arguably the most important development in terms of taxation of IP that will continue to impact MNCs with IP structures is the OECD’s BEPS project, specifically Actions 8-10. The recommendations of Actions 8-10 have been included in the revised Chapters I and VI of the OECD Transfer Pricing Guidelines published in 2017, and discussions around modified Chapters I and VI indicate a general international consensus with respect to the definition and valuation of IP, with some notable exceptions.

There does, however, seem to be a fundamental disagreement between OECD member states as to the interpretation of the guidance provided in Chapter I regarding risk, i.e., whether contractual arrangements between related parties in general, including when these involve IP, should be respected, or if they can be recast based on the six-step risk framework laid out in Chapter 1 of the revised OECD Guidelines. Some OECD members argue that contractual allocations of risk should be respected only when they are supported by actual decision-making.

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The Council of the European Union has reached agreement on a draft directive aimed at boosting transparency to tackle what it sees as aggressive cross-border tax planning.

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A new roundtable discussion reviews the new provisions and how they may impact your business, including:

► Background and timeline
► Details of the mandatory disclosure requirements, including the purpose of the reporting, what arrangements are reportable, when reporting must be made and what happens with reported information
► Implications of reporting/failure to report
► The need for tracking and reporting systems and procedures

Download the report at ey.com/tpcbriefing.
On 22 April 2018, the International Monetary Fund (IMF) and World Bank Group (WB) held a joint international tax conference as part of the WB’s Annual Spring Meetings entitled “Splitting the Riches: The Present and Future of Taxation by Formula.” The half-day session effectively marked the public launch of a new international tax research and work program that challenges the “conventional wisdom” of the arm’s-length principle (ALP) as the basis for deciding the division of taxing rights in relation to related-party transactions.

The main aim of the program is to offer an alternative to ALP-based tax systems, designed to simplify assignment of taxing rights (especially for developing countries) and to create what these groups feel is a more equitable split of the tax base.

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The International Monetary Fund and World Bank launch a new program, offering their potential alternative to the arm’s-length principle
For developing countries in particular, accessing comparables—if they even exist—involves potentially high administrative costs and access to data that may be limited. Finally, with tax authorities with low capacity or limited experience, the margin for error may be high, leading to a growing number of disputes.

The IMF and WB argue that the current basis for most international corporate taxation, the application of the ALP to determine how and where multinationals’ profits are booked and taxed, fails to deliver an adequate division of taxing rights between countries that capture where profits are being generated. They posit further that the rollout of the G-20 and OECD BEPS initiative aimed at addressing key weaknesses in the current international tax framework, does not tackle the fundamental cause of the significant spillovers inherent in a system based on ALP. Further, the attempt to tax digital transactions from nonresident providers and the growing importance of intangible assets create further challenges to the current international system, they say.

A range of questions regarding the effectiveness of the ALP have sparked discussions on whether it is sustainable. Many of the perceived weaknesses in the ALP became evident in the course of developing guidance for finding comparable transactions upon which to determine the value of a transaction at arm’s length, says a report published by the IMF, OECD, WB and United Nations in January, 2017. But while much has been written about the problems with the ALP in practice, much less is known about the advantages and disadvantages of alternative systems used in a handful of countries and by subnational governments, typically based on a formulary approach to profit attribution. The event brought together a variety of experts to discuss these issues.

ALP’s challenges

The premise of the conference and work program is that the ALP is not sufficient to both prevent base erosion especially through transfer mispricing and related instruments/vehicles and that it is too complicated for even middle-income countries to use. In particular, participants argued that the ALP is based on finding comparable prices to calculate an arm’s-length price, but in many cases such comparables either do not exist or are calculated inaccurately.

For example, the comparables have difficulty taking into account economies of scale and scope, intangible assets and digital transactions. In addition, more generally, many transactions do not have domestic, regional or even global comparable prices, given the facts and circumstances surrounding the transaction. For developing countries in particular, accessing comparables—if they even exist—involves potentially high administrative costs and access to data that may be limited. Finally, with tax authorities with low capacity or limited experience, the margin for error may be high, leading to a growing number of disputes.

A possible alternative to the ALP: formulary apportionment

Against this backdrop, the panelists presenting on this particular topic at the event argued that formulary apportionment (FA) may represent a suitable alternative approach. FA works as follows:

► The income of an entire group is calculated, which eliminates the need to separate between controlled (intragroup) pricing and uncontrolled pricing.
► Income is apportioned (attributed) by “factors” that reflect economic activity (which could be sales/turnover, capital, labor, etc.), weighted according to importance (which varies among countries).
► Income/profit is taxed according to the individual countries’ tax law.

The panelists argued that the key advantages of FA would be to enhance transparency, reduce complexity and eliminate channels for tax avoidance. Specifically, they argued that FA:

► Eliminates transaction-based documentation (and having to calculate the transfer price)
► Eliminates the need for other instruments such as controlled foreign company rules or foreign tax credits
► Eliminates other main vehicles for tax avoidance such as potentially excessive deductions of interest

Practically speaking, it is unlikely that there will be a policy shift that is operationalized in the short and medium terms.

However, FA has its own set of challenges, including:

► A potentially decreased tax base (when group income is consolidated to include loss-making companies)
► Requires more intercountry coordination to determine legitimate deductions and special tax rules
► Intercountry coordination could reduce an individual country’s tax sovereignty
► Could induce group restructuring to take advantage of lower tax jurisdictions, misallocation of resources for tax savings and thus sparking harmful forms of tax competition

Examples of formulary apportionment in practice

The event chose to include active examples of FA at the subnational level, using the intrastate profit-split in the United States; similarly, between provinces in Canada, these systems have been in place for a long time and are generally viewed as working effectively, though with their own particular challenges. At the same time, these examples are simpler than a multinational situation, since they are all within the same currency zone and only apportion the subnational portion of a tax liability. The example of the Common Consolidated Corporate Tax Base (CCCTB) proposed by the EU gets a step closer to what formulary apportionment could look like for a multinational, said the panelists.

Will formulary apportionment be operationalized by lesser developed countries?

The IMF and WB presented a compelling case for both rethinking the use of ALP especially in developing or capacity/experience constrained countries, arguing that a viable alternative could be to use FA. But, practically speaking, it is unlikely that there will be a policy shift that is operationalized in the short and medium terms. In the short term, the IMF will conduct additional empirical research and investigation on the experiences of the limited number of countries using formulary apportionment, looking at size of the tax base, revenue generation and possibly adjustment disputes that are based on FA-related adjustments. One medium- or perhaps long-term scenario could be that both the IMF and the WB add in FA or more likely, partial FA (as detailed above) in the menu of options for countries wishing to implement or strengthen transfer pricing regimes in particular.

While operationalization is not expected on a widespread basis, this is a debate, post-BEPS, that is just beginning. Indeed, the digital debate in Europe that rages today is not so much about stateless income and tax avoidance as it is about the division of taxing rights. BEPS 2.0? Perhaps!

Rich Stern was previously Global Program Lead for the Business Taxation Program for the World Bank Group, before joining EY Austria in 2017.
Global connectivity means it’s easier today for businesses to be faced with tax controversy. How can you manage the risk?

Governments worldwide are collecting and sharing taxpayer information at a rapid pace. At the same time, tax policy and legislative changes in one jurisdiction - like, for example, the United States’ enactment of tax reform - can trigger changes across the globe as countries seek to remain competitive and protect their tax base.

Tax has become increasingly connected, and companies must act so that their people, policies and systems are keeping pace.
Enhanced tools are allowing tax authorities to develop a more comprehensive global picture of a businesses’ operations, employees, sales, intangibles and tax transactions. They are also marking the “slow death” of the annual cycle that once framed the tax function.

Tax controversy: a typical picture

How are companies experiencing this interconnectivity?

Take, for example this increasingly common scenario. A multinational firm is confronting many tax controversy challenges around the globe including:

- A transfer-pricing dispute with the German Federal Central Tax Office
- Argentine authorities that are considering revoking an operating license
- A Southeast Asian nation preparing to “name and shame” the company in the newspapers
- Several ongoing contentious disputes in multiple jurisdictions where the company has operations

In addition, the company is about to undertake a corporate restructuring in Russia, adding another layer of tax exposure. By the end of the year, this organization is facing controversies with dozens of different tax authorities – and its leadership is looking to the vice president of tax for a strategy to manage and resolve existing controversies and to mitigate future controversies.

The company is experiencing first-hand how the tax information collection and sharing process has accelerated, triggering an increase in tax controversy. Governments worldwide are collecting more from corporations, and they are using a combination of multilateral transparency reforms, digitization, vast data collection, and enhanced data analysis to identify and act on tax issues.

Connectivity – amplified

This increased information sharing and interconnectivity means that tax controversy in one country can now quickly spread and intensify as tax authorities collaborate across borders. Collaboration is being aided by digitization and the volume of information gleaned from country-by-country reports and the master file that large companies must submit to all relevant tax authorities.

Enhanced tools are allowing tax authorities to develop a more comprehensive global picture of a businesses’ operations, employees, sales, intangibles and tax transactions. They are also marking the “slow death” of the annual cycle that once framed the tax function. While companies still file an annual tax return that is still viewed and evaluated only by a tax authority, making that tax data available to the public is under consideration in several jurisdictions, and the traditional tax return may eventually give way to real-time reporting.

The result is that tax controversy is rapidly evolving from two-sided disputes in specific countries into a multi-dimensional, multi-country dynamic. As noted by EY Global International Tax Services Leader Alex Postma: “In a world of increased information sharing among tax authorities, aggressive tax enforcement and associated reputational risks, maintaining a global perspective on all the jurisdictions in which your business operates is critical.”
Tax risk has become a primary concern for the C-suite and for boards. There is more interest than ever in preventing disputes, containing the ones that do arise and resolving issues quickly.

Managing the risk: steps to take now

1. Adopt a top-down, end-to-end global approach to tax controversy with policies and procedures that facilitate oversight and early identification of global tax controversies
2. Determine whether you have the right people, with the right skills, in the right jurisdictions to prevent, manage and resolve tax controversy issues – these individuals must understand how addressing an issue in one jurisdiction can trigger controversy in another
3. Evaluate whether existing systems can provide a complete picture of tax controversies in all jurisdictions in which you operate
4. Integrate tax with business planning to facilitate proactive management of tax controversy that takes into account a company’s entire tax footprint
5. Stay connected with global legislative, regulatory and tax administration changes

As we continue to shift from a world of separate relationships to a connected one in which data is shared and authorities exchange information in real time, successful companies will be those that remain nimble and open to new ways of thinking about tax, tax data, and tax controversy management. Because companies cannot opt out of this increasingly interconnected tax environment, the time to act is now.
How tax authorities are increasingly scrutinizing procurement function activities

Businesses have been confronted with many new tax developments demanding headline attention recently, such as the tariff proposals in the US, mandatory disclosure rules and the digital tax phenomenon in the EU. But there are also a number of tax changes underway that don’t draw the same media focus but can nevertheless significantly affect the global business operations of multinational enterprises (MNEs). The impact that the recently enacted multilateral instrument (MLI) convention will have on procurement is one consequence of those changes.

In the last three decades, procurement has evolved from a business support function focusing mainly on cost management, to a key value driver for many MNEs.

Procurement teams are now engaged in managing group demand, maintaining supplier relationships and strategically sourcing inputs or overseeing quality control, and are also increasingly influencing product design and supplier integration in the supply chain to more strategically drive long-term cost leadership.
Once a taxable presence—in tax parlance, “permanent establishment”—exists, tax consequences can start piling up: from corporation tax returns, transfer pricing reports, CbCR and master file obligations, to new tax liabilities, individual income tax compliance and social security obligations of business travelers to the jurisdiction.

Country-by-country reporting

The increased importance of the procurement function has not escaped the attention of tax authorities. For example, the country-by-country report (CbCR) that multinationals were obligated to file in many countries for the first time by 31 December 2017 specifically required multinationals to indicate which entities are involved in procurement functions.

Also, the CbCR handbook on effective tax risk assessment from the Organisation for Economic Co-operation and Development (OECD) mentions “procurement entities in jurisdictions other than its manufacturing locations” as a risk indicator to which countries’ tax authorities should pay special attention.

Additionally, the master file demands a special section be completed in which the multinational must describe its supply chain and provide an analysis of the various functions performed along the supply chain.

The CbCR and the master file are not the only instruments available to the tax authorities. The 2017 change of the OECD model treaty and commentary strips procurement of its “automatic” preparatory and auxiliary status and consequently from the automatic application of the exemption from the creation of a taxable presence.

Furthermore, even when the activities of a single entity are preparatory and auxiliary, countries may now elect to ignore this exemption if the procurement activities are part of a cohesive business operation with other group entities in the jurisdiction of the procurement activity (the so-called anti-fragmentation rules).

Separately, a change in the OECD model treaty concept of agency permanent establishment (PE) will affect procurement operations, as agency was previously limited to “concluding contracts” but now more broadly includes activities “leading to the conclusion of contracts.”

‘The time is now’

These changes to limit the application of the preparatory and auxiliary exemption and expand the agency definition have been adopted by the majority of the almost 80 jurisdictions that have signed or are expected to sign the MLI convention, which should accelerate the adoption of these changes by the 2,300 or so existing tax treaties between the participating countries.

And with Slovenia’s ratification in March, this MLI convention has now entered into force and will be effective for any particular combination of countries six months after both jurisdictions have ratified the instrument.

In other words, the “time is now,” and a leading practice for multinationals is to thoroughly review their procurement activity ahead of the pending changes. Some areas to which companies with cross-border procurement activities need to pay particular attention are:

► Overall procurement footprint: This should be assessed and mapped against countries adopting changes to the PE rules in their treaties and or domestic law.

► Foreign rep offices or any other fixed presence in another country: These may become taxable presences as a result of the loss of the application of the preparatory and auxiliary test as well as the application of the anti-fragmentation rules.

► Business travellers: Business travelers who negotiate procurement contracts may be considered to play the principal role leading to the conclusion of contracts and may thereby create a tax presence for their principal.

► Agents either related or unrelated to the multinational enterprise: These agents may create a taxable presence if they exclusively or almost exclusively work for the same MNE.

Consequences

Once a taxable presence exists, tax consequences can start piling up: from corporation tax returns, transfer pricing reports, CbCR and master file obligations, to new tax liabilities, individual income tax compliance and social security obligations of business travelers to the jurisdiction.

Ignoring the new normal may come at a cost: many countries have recently increased penalties and sanctions, with a number of countries now wielding potential criminal sanctions in addition to financial penalties for failure to report a PE. Given the consequences that may lie ahead, now is the time for multinationals to begin stress testing their procurement functions.
In our report “Eight for 2018 and beyond: key transfer pricing risks to consider” on page 25, we discussed the challenges of addressing transfer pricing issues related to the sale or transfer of intellectual property (IP). Many countries, we outlined, are both changing their laws in this area, as well as enforcing existing laws more strictly. India arguably illustrates such challenges more fully than most. In this short article, Vijay Iyer, Transfer Pricing Leader for EY India, provides some further insights on the specific challenges presented by India’s tax regime.

**Taxpayers in India face key compliance challenges around the sale and transfer of intellectual property**

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Intangibles are defined under section 2 (11) of the Indian Income Tax Act (the Act), 1961 as “being know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature.” Given the broad scope of the this definition, and to remove ambiguity regarding the types of intangibles covered, section 92B of the Act gives an inclusive definition of intangible property, providing a detailed list of assets that can be covered under intangible properties.
Another reason for differences in the valuation of IP between taxpayer and Indian Revenue Authorities (IRA) is the fact that valuations are undertaken by the taxpayers ex ante, whereas the IRA tend to derive the value of the transferred IP ex post at the time of tax audits.

Since the enactment of transfer pricing regulations in India, taxpayers have faced certain key compliance issues surrounding complex transactions that may be carried out by a multinational enterprise (MNE). One such issue pertains to the transfer of IP by taxpayers to their related entities.

One of the primary challenges faced by taxpayers while transferring IP is the fact that the IP transferred may be bundled IP - i.e., it may comprise more than one specific IP asset. In such a scenario, it is difficult to assign values to each individual IP asset forming part of the larger bundled group. Furthermore, where IP is owned by an MNE group, it may be difficult to split the proceeds arising on the transfer of IP among group entities, given the fact that development, enhancement, maintenance, protection and exploitation (DEMPE) functions may be performed separately by various group entities spread across different tax jurisdictions.

A second key factor also historically attracting scrutiny has been the underlying intent of IP transfers in terms of business substance; with the introduction of a General Anti Avoidance Rule (GAAR) into India’s tax law from April 2017 onwards, transfers will have to be substantiated with commercial reasons, including the ability of the transferee to control the financial and related risk of the IP. In this regard, transfers of IP in the post-GAAR era now have to pass the twin test of (a) the overall arrangement between the taxpayer and the transferee is not an arrangement to avoid taxes in India; and (b) it does not fall in the category of being an “impermissible avoidance agreement.”

In a scenario where IP is sold by the taxpayer to its related entity, the IRA have, in certain cases, alleged that the transaction has been undertaken at a value that is not considered to be at arm’s length, which in turn is a result of the inherent subjective nature of valuation methodology.

Thus, the issues in connection with transfer of IP usually revolve around the difference in the valuation methodology and/or approach, and resulting assumptions of the taxpayer and the IRA. This issue generally occurs when revenue authorities challenge the assumptions adopted by the taxpayer in the valuation of IP. Further, in a scenario when IP is sold/transferred to an entity outside India, the IRA also allege that valuation should be performed from the end user, market perspective, and not restricted to the seller’s market, as the parameters could differ.

One of the methods of valuation for IPs in India is the discounted cash flow (DCF) method. Parameters considered in the DCF method such as future cash flow, discounting factor, growth rate, useful life terminal growth rate and risk premium represent the critical basis of valuation typically adopted by taxpayers. The IRA have been critical of the above parameters, and have austerity scrutinized the assumptions of such parameters on the issue of sale of IP(s) to related entities.

Revenue authorities, even at the Advance Pricing Agreement level, often examine the assumptions and risk parameters considered while arriving at the discount rate adopted by a taxpayer in discounting projected cash flows in order to determine the value of IP. This is also due to the fact that there are multiple sources/databases of information for determining the country risk premium and growth rates, for example, that are used in projecting cash flows. As a specific example, both the Consumer Price Index and the Wholesale Price Index could potentially be relied upon to represent the inflation index of a country. Similarly, country risk premium or beta factor may be not be computed on same assumptions on all reliable public sources/databases. Owing to the these differences in assumptions, the valuation undertaken by different valuers tend to give varied results. Hence, the subjective nature of the valuation exercise often results in the IRA rejecting the valuation report maintained and submitted by the taxpayer.

Another reason for differences in the valuation of IP between taxpayer and IRA is the fact that valuations are undertaken by the taxpayers ex ante, whereas the IRA tend to derive the value of the transferred IP ex post at the time of tax audits. Hence, there is a significant time lag between the time that the valuation is carried out by the taxpayer (while undertaking the transfer) while the same is
A second key factor also historically attracting scrutiny has been the underlying intent of IP transfers in terms of business substance; with the introduction of a General Anti Avoidance Rule (GAAR) into India’s tax law from April 2017 onwards, transfers will have to be substantiated with commercial reasons, including the ability of the transferee to control the financial and related risk of the IP.

Scrubinized and assessed during tax audits by the IRA. By the time the IRA reviews and scrutinizes the valuation during a tax audit—typically two to three years later—the cash flows adopted by the taxpayer (that were once projected cash flows) are then replaced by the IRA (particularly at field office level) by actual cash flows. At higher levels of the IRA, the projections determined on a scientific basis with fair assumptions have tended to be accepted.

Additionally, we are aware that taxpayers typically obtain valuation reports and carry out transactions based on the value arrived at in such valuation reports without maintaining robust documentation to support the assumptions adopted in the valuation reports while undertaking the valuation exercise for transfer of IP. That has proved to be a risk in the Indian context.

The aforementioned factors result in the arm’s length value as computed by the taxpayers for transfer of IP being challenged and disputed by the IRA.

While the term “intangible property” has been clearly defined in the Indian tax law, there still remains ambiguity on the method/approach to be adopted in the valuation of IP. It would be helpful if the IRA were to consider providing additional guidance on the method and approach to be adopted while valuing IP, as well as the specific documentation that taxpayers should provide in support. This would significantly help taxpayers in establishing the arm’s-length nature of their IP transfers during scrutiny proceedings and consequently reduce litigation in India on this front.

Although the above mentioned problems persist before the lower authorities, the Appellate authorities have provided some guidance in the approach to be followed while valuing IP. While there are not many judicial precedents to provide guidance in this regard, the following judgments laying down the principles of valuation, may be referred to:

- Tally Solutions Pvt Ltd vs Dy Commissioner of Income Tax, Circle 12 (4) (ITA no 101/ Bang/ 2013)
- DQ (International) Ltd, Hyderabad vs Asst Commissioner of Income Tax, Circle – 17(1) (ITA no. 151/ Hyd/2015)
Spain proposes a Digital Services Tax

On 30 April 2018, Spain released its 2018 Stability Programme and Budgetary Plan Update (the 2018 program update), which proposes the introduction of a Digital Services Tax (DST) to be effective in 2018. Even though no draft of this proposed new tax has been released yet, it will presumably be aligned with the proposal made by the European Union (EU) to tackle challenges of taxing digitalized business.

In recent years, the main players in the international tax field – in particular, the Organisation for Economic Co-operation and Development (OECD) and the EU – have addressed the challenges of the digital economy, with the goal of ensuring that multinational digital companies contribute to the tax revenues of the territories where they are, de facto, carrying out their business.

The response given at the EU level to the challenges of taxing digitalized business was released on 21 March 2018, when the EU Commission issued the Digital Tax Package, in the form of two proposals for new Directives, focused on a two-phased approach, including: (i) an interim solution, referred to as the Digital
Services Tax (DST); and (ii) a longer term Council Directive laying down rules relating to the corporate taxation of a significant digital presence (SDP or the Significant Digital Presence proposal).

As noted on page 14, the current DST proposal foresees a temporary (in the sense that it will apply only until the SDP solution has been implemented) 3% tax on gross revenues derived from the following digital activities:

- Selling online advertising space
- Digital intermediary activities which allow users to interact with other users and which can facilitate the sale of goods and services among them
- The sale of data generated from user-provided information

The DST, as proposed by the EU, would only apply to companies with total annual worldwide revenue of at least €750 million and EU revenue of €50 million or more.

There is no certainty as when the EU DST proposal will be ultimately approved, especially considering that certain EU Member States have expressly voiced that they prefer a harmonized OECD approach rather than introducing a unilateral measure by the EU.

While the EU Commission acknowledges that the ideal approach would be to find multilateral, international solutions to taxing the digital economy, given the global nature of this challenge, the OECD in their 16 March Interim report on tax challenges arising from digitalization note that “There is no [global] consensus on the need for, or merits of, interim measures, with a number of countries opposed to such measures on the basis that they will give rise to risks and adverse consequences.” The OECD further noted that an update on this [OECD] work will be provided in 2019 and that the BEPS Inclusive Framework (BEPS IF) members are working toward a consensus-based solution by 2020.

Spain

In this context, on 5 April 2018, the Spanish 2018 draft Budget Law was published in the Spanish Parliamentary Official Gazette. The Government committed to increased social spending (in particular, mainly state pensions) and to cut public deficit to nil by 2021. In order to be able to meet these commitments, the Government requires additional sources of income.

In this regard, in the 2018 program update sent to the EU Commission on 30 April 2018, Spain announced its intention to introduce a Spanish DST by the end of 2018 (potentially applicable in 2018), with the objective of taxing digitalized companies in the jurisdiction where their added value is generated. Even though no draft of this proposed new tax has been released yet, the announcement states that Spanish DST will follow the features of the EU proposal. Finally, it is important to note that Spain has not made any announcement yet on the implementation of a new definition of what will constitute a permanent establishment due to a significant digital presence, along with revised profit allocation rules, as per the EU SDP proposal. We understand that Spain will wait until further approval of this Directive by the EU.

Implications

Considering the lack of consensus between EU Member States on the introduction of the DST, the next steps in the approval process will be significant in determining whether this tax will be implemented at an EU level.

Similarly, the outcome of the OECD work with respect to the digital economy should be carefully monitored.

With respect to Spain, it is still uncertain when the proposed wording of the DST will be published. Once available, this would have to be analyzed in detail to confirm whether the main features of the new tax deviate from the EU DST proposal. In particular, it will be key to identify which digital services would fall under the scope of the new tax and which thresholds would apply.

In fact, on 7 August 2018 it was published in the Spanish press that the new law, if approved, would be applicable as from 2019 and not 2018 as it was initially announced. It was also published that, as expected, the proposal to introduce the DST will follow the approval procedure of proposed draft bill after summer. This approval procedure is subject to discussion under the Parliament and Senate and since the ruling party does not have a majority of either chamber, it is dependent on the support of the opposition.

In the meantime, multinational digital companies with a business presence in Spain should start considering the potential impact that this new tax could have on their business model.
On June 21, 2018, the US Supreme Court (Court) issued its much anticipated ruling in South Dakota v. Wayfair. In a 5-4 ruling, a majority of the Court voted to overturn both Quill and National Bellas Hess, finding that the physical presence nexus standard articulated in the two earlier opinions "is unsound and incorrect." As a result of the Court's decision, states may now begin requiring all remote sellers to register, collect and remit sales and use taxes on transactions with in-state customers regardless of the seller's physical presence, provided that they do so in a manner that does not otherwise violate the Commerce Clause by discriminating against or imposing undue burdens on interstate commerce.

The majority opinion: Quill was an unsound and incorrect interpretation of the Commerce Clause

Justice Anthony Kennedy, writing for a majority including Justices Thomas, Ginsburg, Alito and Gorsuch, explained that the Court's precedent interprets the Commerce Clause as prohibiting states from regulating interstate commerce in a manner that is discriminatory or imposes an undue burden. As applied to state taxes, the Court cited the four-factor Complete Auto Transit test, which held that a state tax will be sustained under the Commerce Clause if the tax: 1) applies to an activity with substantial nexus with the taxing state, 2) is fairly apportioned, 3) does not discriminate against interstate commerce, and 4) is fairly related to the services provided by the state.
While joining Justice Kennedy’s opinion, Justice Thomas noted in a concurring opinion that, although he joined with Justice Kennedy in Justice Scalia’s concurring opinion in Quill on stare decisis grounds, looking back over the past quarter century had convinced him that “Bellas Hess and Quill ‘can no longer be rationally justified,’ nor could the Court’s entire negative (dormant) Commerce Clause jurisprudence.

Through its prior rulings in National Bellas Hess and Quill, the Court had held that, at least with respect to sales tax, a seller that lacked any direct or attributed physical presence in a state could not be considered to have a substantial nexus with that state under the Commerce Clause. In a recent decision, however, Justice Kennedy, who authored the opinion in Wayfair but also voted with the majority in Quill, noted that the physical presence standard constituted a “serious, continuing injustice faced by the states. In Wayfair, with the physical presence nexus standard squarely at issue, Justice Kennedy explained that the doctrine had become “further removed from economic reality,” resulting in significant state revenue losses, and “as first formulated and as applied today, is an incorrect interpretation of the Commerce Clause.”

The majority also noted that, while not identical, the nexus standards under the Due Process and Commerce Clauses have significant parallels. This observation is noteworthy, given that the Quill majority drew a sharp distinction between the respective standards, with the Commerce Clause imposing a higher burden on the states. Given the ruling in Wayfair, that distinction becomes less clear, if not, completely non-existent, raising the possibility that, for sales and use tax collection purposes, the standard may now merely be “purposeful availment” or “minimum contacts,” as asserted in previous Commerce Clause cases, including in the original 1992 Quill opinion itself.

Continuing its analysis, the majority explained that: 1) the physical presence standard “is not a necessary interpretation of the requirement that a state tax must be ‘applied to an activity with a substantial nexus with the taxing State;’” 2) Quill does not resolve market distortion but creates it; and 3) Quill “imposes the sort of arbitrary, formalistic distinction that the Court’s modern Commerce Clause precedents disavow.” The Court illustrated these largely economic-based concerns by noting that the administrative costs of compliance were largely unrelated to a taxpayer’s physical presence. The Court also expressed that Quill had effectively become a “judicially created tax shelter for businesses that decide to limit their physical presence and still sell their goods and services to a State’s consumers —something that has become easier and more prevalent as technology has advanced.” Instead, the Court advocated for a more “sensitive, case-by-case analysis of purposes and effects” over the physical presence standard, which is “artificial in its entirety.”

The Court then noted the various state legislative attempts to expand physical presence and compliance burdens—such as “cookie” nexus, expanded affiliated and click-through provisions, and notice and reporting requirements—that had eliminated physical presence as a clear or easily applicable standard, thereby undercutting any arguments based on principles of stare decisis. As such, the majority noted, it was incumbent on the Court to address the “false constitutional premise” of its own creation, and that it would not be appropriate to ask Congress to change what had become “the constitutional default rule.”

Ultimately, the Court chose to focus primarily on the practical economic effect and the continued viability of the physical presence standard given the Internet’s “prevalence and power,” which has “changed the dynamics of the national economy.” The Court also dismissed concerns that compliance costs would harm the market, noting that, eventually, software would be available at a reasonable cost to lessen the burden on small sellers. To this end, the Court noted that the protections in South Dakota’s law—including sales threshold limitations, limits on retroactivity, and Streamlined Sales Tax (SST) membership—were sufficient to limit the burdens on interstate commerce. Nevertheless, the Court did not opine directly on the constitutionality of the law, choosing instead to vacate and remand the case back to South Dakota, where any other Commerce Clause questions might be raised.

Justices Thomas and Gorsuch agree

While joining Justice Kennedy’s opinion, Justice Thomas noted in a concurring opinion that, although he joined with Justice Kennedy in Justice Scalia’s concurring opinion in Quill on stare decisis grounds, looking back over the past quarter century had convinced him that “Bellas Hess and Quill ‘can no longer be rationally justified,’ nor could the Court’s entire negative (dormant) Commerce Clause jurisprudence.

Justice Gorsuch, who also joined the majority but still wrote a separate concurrence, noted that Bellas Hess and Quill amounted to discrimination between in-state and out-of-state businesses, but questioned whether an Article III court could invalidate a state law that offended no Congressional statute. Justice Gorsuch also articulated a view very similar to Justice Thomas’ view (and that of Justice Scalia before him) that the Court’s entire negative Commerce Clause jurisprudence was suspect.
The most pressing issue for multistate taxpayers is whether the states will attempt to assert liability for uncollected taxes on a retroactive basis.

The minority favors Congressional action

In a dissent joined by Justices Breyer, Sotomayor, and Kagan, Chief Justice Roberts explained that, while he agreed that Bellas Hess was wrongly decided, it was incumbent on Congress to exercise its Commerce Clause authority to change the standard, and that stare decisis, which was so important in deciding Quill, "should be an even greater impediment to overruling precedent," especially in light of the Quill Court's specific call for Congress to act.

Implications

The most pressing issue for multistate taxpayers is whether the states will attempt to assert liability for uncollected taxes on a retroactive basis. While most states have indicated that they will not do so, and a few states have enacted legislation specifically prohibiting retroactive assessments, most states do have laws on the books — some dating back to the 1970s — that apply an economic/minimum contacts nexus standard and could conceivably be enforced at will. Many of these laws, often called "anti-Bellas Hess" statutes, though never repealed, were effectively pre-empted by the Court's decision in Quill. Taxpayers should be wary that states will resurrect those statutes and begin enforcing sales tax collection responsibility conceivably as far back as the very first sale a remote seller may have made into the jurisdiction (considering the Court's very clear ruling that Quill and Bellas Hess before it were both "unsound and incorrect" even when decided.)

Regardless, remote sellers that have made sales into a state and not collected sales tax should assess their particular situations immediately and consider approaching the states under their voluntary disclosure or amnesty programs. We anticipate many states will make announcements in the next few days on what they intend to do in light of this significant state sales tax ruling that likely has far-reaching implications. Regarding compliance, multistate businesses that already were collecting in multiple states can expect to see their compliance costs increase, whereas businesses that have not been collecting and do not have a comprehensive sales and use tax compliance system will be under extreme pressure to rapidly assess and quickly implement a feasible and perhaps costly compliance solution. While no state has offered any guarantee, some state tax officials have already publicly stated that they will be "reasonable" in their approaches and hopefully, will allow sufficient time for such companies to prepare to register, collect and remit the appropriate sales taxes.

Regarding SST and the Certified Service Provider (CSP) program, there may be some early stress on the system as the universe of multistate sellers with a collection obligation significantly expands and this program responds to the increased demand for its services.

Finally, but no less importantly, all taxpayers must immediately consider the impact of this decision on their operations; specifically budgeting for increased compliance costs, leveraging additional internal or external resources, and considering potential ASC 450 implications and other reporting obligations. For companies that self-assess use tax on purchases or claim exemptions, it will be important to closely evaluate how increased collection by vendors will affect tax payments, while marketplace providers and small sellers will need to determine who will be considered the "seller of record" responsible for tax collection and remission under various state interpretations.

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>2017</th>
<th>2018</th>
<th>Notes</th>
<th>% of change in 2018</th>
<th>Indicator</th>
<th>2017</th>
<th>2018</th>
<th>% of change in 2018</th>
<th>Indicator</th>
<th>2017</th>
<th>2018</th>
<th>% of change in 2018</th>
<th>Indicator</th>
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<tbody>
<tr>
<td>Argentina</td>
<td>35%</td>
<td>30%</td>
<td>Corporate income tax rate decreases from 35% to 30% for fiscal years starting 1 January 2018 to 31 December 2019, and to 25% for fiscal years starting 1 January 2020 and onwards.</td>
<td>-14.3% Decrease</td>
<td>35%</td>
<td>35%</td>
<td>0%</td>
<td>No change</td>
<td>21%</td>
<td>21%</td>
<td>0%</td>
<td>No change</td>
<td></td>
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<tr>
<td>Australia</td>
<td>30%</td>
<td>30%</td>
<td>0% No change</td>
<td>47.0%</td>
<td>45%</td>
<td>-4.3% Decrease</td>
<td>10%</td>
<td>10%</td>
<td>0% No change</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Brazil</td>
<td>34%</td>
<td>34%</td>
<td>0% No change</td>
<td>27.5%</td>
<td>27.5%</td>
<td>0% No change</td>
<td>18.0%</td>
<td>18%</td>
<td>0% No change</td>
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<td></td>
<td></td>
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<tr>
<td>Canada</td>
<td>28.07%</td>
<td>27.87%</td>
<td>Simple average combined federal rate (15%) and provincial/territorial rate (varies) on general income. By province/territory, combined rates range from 26.5% to 31%</td>
<td>-0.71% Decrease</td>
<td>54%</td>
<td>54%</td>
<td>0% No change</td>
<td>5.0%</td>
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<td>0% No change</td>
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<td>25.0%</td>
<td>25%</td>
<td>0% No change</td>
<td>45%</td>
<td>45%</td>
<td>0% No change</td>
<td>17%</td>
<td>17%</td>
<td>0% No change</td>
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<tr>
<td>France</td>
<td>33.3%</td>
<td>33.3%</td>
<td>0% No change</td>
<td>45%</td>
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<td>0% No change</td>
<td>20%</td>
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<td>0% No change</td>
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<td>30%</td>
<td>30%</td>
<td>0% No change</td>
<td>45%</td>
<td>45%</td>
<td>0% No change</td>
<td>19%</td>
<td>19%</td>
<td>0% No change</td>
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<tr>
<td>India</td>
<td>43.3%</td>
<td>43.3%</td>
<td>Domestic company income tax rate is 30% and will gradually be reduced to 25% over the next three years. Rate shown to left is for foreign companies, and is inclusive of surcharge and education cess.</td>
<td>0% No change</td>
<td>30%</td>
<td>30%</td>
<td>0% No change</td>
<td>12.5% No change</td>
<td></td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
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<td>25%</td>
<td>25%</td>
<td>0% No change</td>
<td>30%</td>
<td>30%</td>
<td>0% No change</td>
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<td>0% No change</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Italy</td>
<td>24%</td>
<td>24%</td>
<td>0% No change</td>
<td>43%</td>
<td>43%</td>
<td>0% No change</td>
<td>22%</td>
<td>22%</td>
<td>0% No change</td>
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<tr>
<td>Japan</td>
<td>29.97%</td>
<td>29.74%</td>
<td>29.74% is the effective tax rate when federal and local (Tokyo) taxes are taken into account.</td>
<td>0% -0.77% Decrease</td>
<td>45%</td>
<td>45%</td>
<td>0% No change</td>
<td>8%</td>
<td>8%</td>
<td>0% No change</td>
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<td></td>
<td></td>
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<tr>
<td>Mexico</td>
<td>30%</td>
<td>30%</td>
<td>0% No change</td>
<td>35%</td>
<td>35%</td>
<td>0% No change</td>
<td>16%</td>
<td>16%</td>
<td>0% No change</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Russia</td>
<td>20%</td>
<td>20%</td>
<td>0% No change</td>
<td>35%</td>
<td>35%</td>
<td>0% No change</td>
<td>18%</td>
<td>18%</td>
<td>0% No change</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>20%</td>
<td>20%</td>
<td>0% No change</td>
<td>20%</td>
<td>20%</td>
<td>0% No change</td>
<td>N/A</td>
<td>5%</td>
<td>N/A Increase (new tax)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>South Africa</td>
<td>28%</td>
<td>28%</td>
<td>0% No change</td>
<td>41%</td>
<td>41%</td>
<td>0% No change</td>
<td>14%</td>
<td>14%</td>
<td>0% No change</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>South Korea</td>
<td>22%</td>
<td>25%</td>
<td>New tax bracket for income over KRW300 billion</td>
<td>0% Increase</td>
<td>38%</td>
<td>38%</td>
<td>0% No change</td>
<td>10%</td>
<td>10%</td>
<td>0% No change</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Turkey</td>
<td>20%</td>
<td>22%</td>
<td>22% for 2018, 2019 and 2020, effective 5 December 2017.</td>
<td>10% Increase</td>
<td>35%</td>
<td>35%</td>
<td>0% No change</td>
<td>18%</td>
<td>18%</td>
<td>0% No change</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>United Kingdom</td>
<td>19%</td>
<td>19%</td>
<td>0% No change</td>
<td>45%</td>
<td>45%</td>
<td>0% No change</td>
<td>20%</td>
<td>20%</td>
<td>0% No change</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>United States</td>
<td>39%</td>
<td>26%</td>
<td>Assumes average state taxes of 5% Taxable years beginning after 2017 and before 2026</td>
<td>0.0% No change</td>
<td>39.6%</td>
<td>37%</td>
<td>-6.6% Decrease</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## Global leaders

**Chris Sanger**
- EY Global Tax Policy Leader
- csanger@uk.ey.com
- +44 20 7951 0150

**Rob Hanson**
- EY Global Tax Controversy Leader
- rob.hanson@ey.com
- +1 202 327 5696

## Area leaders

<table>
<thead>
<tr>
<th>Region</th>
<th>Tax Policy</th>
<th>Area leader</th>
<th>Email Address</th>
<th>Phone Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>EY Americas</td>
<td></td>
<td>Cathy Koch</td>
<td><a href="mailto:cathy.koch@uk.ey.com">cathy.koch@uk.ey.com</a></td>
<td>+1 202 327 7483</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Rob Hanson</td>
<td><a href="mailto:rob.hanson@ey.com">rob.hanson@ey.com</a></td>
<td>+1 202 327 5696</td>
</tr>
<tr>
<td>EY Asia-Pacific</td>
<td>Tax Policy</td>
<td>Siew Moon Sim</td>
<td><a href="mailto:siew-moon.sim@sg.ey.com">siew-moon.sim@sg.ey.com</a></td>
<td>+65 6309 8807</td>
</tr>
<tr>
<td>EY EMEIA</td>
<td>Tax Policy</td>
<td>Jean-Pierre Lieb</td>
<td><a href="mailto:jean.pierre.lieb@ey-avocats.com">jean.pierre.lieb@ey-avocats.com</a></td>
<td>+33 1 55 61 16 10</td>
</tr>
<tr>
<td>EY Japan</td>
<td>Tax Policy</td>
<td>Koichi Sekiya</td>
<td><a href="mailto:koichi.sekiya@jp.ey.com">koichi.sekiya@jp.ey.com</a></td>
<td>+81 3 3506 2447</td>
</tr>
</tbody>
</table>

## Market leaders

<table>
<thead>
<tr>
<th>Country</th>
<th>Tax Policy</th>
<th>Area leader</th>
<th>Email Address</th>
<th>Phone Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td></td>
<td>Carlos Casanovas</td>
<td><a href="mailto:carlos.casanovas@ar.ey.com">carlos.casanovas@ar.ey.com</a></td>
<td>+54 11 4318 1619</td>
</tr>
<tr>
<td>Australia</td>
<td></td>
<td>Alf Capito</td>
<td><a href="mailto:alf.capito@au.ey.com">alf.capito@au.ey.com</a></td>
<td>+61 2 8295 6473</td>
</tr>
<tr>
<td>Austria</td>
<td>Tax Policy</td>
<td>Markus Schragl</td>
<td><a href="mailto:markus.schragl@at.ey.com">markus.schragl@at.ey.com</a></td>
<td>+43 1 21170 1268</td>
</tr>
<tr>
<td>Belgium</td>
<td>Tax Policy</td>
<td>Herwig J oosten</td>
<td><a href="mailto:herwig.joosten@be.ey.com">herwig.joosten@be.ey.com</a></td>
<td>+32 2 774 9349</td>
</tr>
<tr>
<td>Brazil</td>
<td>Tax Policy</td>
<td>Washington Coelho</td>
<td><a href="mailto:washington.coelho@br.ey.com">washington.coelho@br.ey.com</a></td>
<td>+55 11 2573 3446</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Tax Policy and Controversy</td>
<td>Milen Raikov</td>
<td><a href="mailto:milen.raikov@bg.ey.com">milen.raikov@bg.ey.com</a></td>
<td>+359 2 8177 100</td>
</tr>
<tr>
<td>Canada</td>
<td>Tax Policy</td>
<td>Fred O’Riordan</td>
<td><a href="mailto:fred.o.oriodan@ca.ey.com">fred.o.oriodan@ca.ey.com</a></td>
<td>+1 613 598 4808</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>Tax Policy and Controversy</td>
<td>Rafael Sayagués</td>
<td>rafael.sayagué<a href="mailto:s@cr.ey.com">s@cr.ey.com</a></td>
<td>+506 2208 9880</td>
</tr>
<tr>
<td>Croatia</td>
<td>Tax Policy and Controversy</td>
<td>Masa Saric</td>
<td><a href="mailto:masa.saric@hr.ey.com">masa.saric@hr.ey.com</a></td>
<td>+385 1 580 0935</td>
</tr>
<tr>
<td>Cyprus</td>
<td>Tax Policy and Controversy</td>
<td>Philippos Raptopoulos</td>
<td><a href="mailto:philippos.raptopoulos@cy.ey.com">philippos.raptopoulos@cy.ey.com</a></td>
<td>+357 25 209 999</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>Tax Policy and Controversy</td>
<td>Lucie Rihova</td>
<td><a href="mailto:lucie.rihova@cz.ey.com">lucie.rihova@cz.ey.com</a></td>
<td>+420 225 335 504</td>
</tr>
<tr>
<td>Denmark</td>
<td>Tax Policy</td>
<td>Jens Wittendorf</td>
<td><a href="mailto:jens.wittendorf@dk.ey.com">jens.wittendorf@dk.ey.com</a></td>
<td>+45 51 58 2820</td>
</tr>
<tr>
<td>Ecuador</td>
<td>Tax Policy and Controversy</td>
<td>Fernanda Checa</td>
<td><a href="mailto:fernanda.checa@ec.ey.com">fernanda.checa@ec.ey.com</a></td>
<td>+593 2 255 3109</td>
</tr>
<tr>
<td>El Salvador</td>
<td>Tax Policy and Controversy</td>
<td>Rafael Sayagués</td>
<td>rafael.sayagué<a href="mailto:s@cr.ey.com">s@cr.ey.com</a></td>
<td>+506 2208 9880</td>
</tr>
<tr>
<td>Estonia</td>
<td>Tax Policy and Controversy</td>
<td>Ranno Tingas</td>
<td><a href="mailto:ranno.tingas@ee.ey.com">ranno.tingas@ee.ey.com</a></td>
<td>+372 611 4578</td>
</tr>
<tr>
<td>European Union</td>
<td>Tax Policy</td>
<td>Marnix Van Rij</td>
<td><a href="mailto:marnix.van.rij@nl.ey.com">marnix.van.rij@nl.ey.com</a></td>
<td>+31 70 328 6742</td>
</tr>
<tr>
<td>Finland</td>
<td>Tax Policy and Controversy</td>
<td>Klaus von Brocke</td>
<td><a href="mailto:klaus.von.brocke@de.ey.com">klaus.von.brocke@de.ey.com</a></td>
<td>+49 89 14331 12287</td>
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<tr>
<td>France</td>
<td>Tax Policy and Controversy</td>
<td>Jukka Liijynen</td>
<td><a href="mailto:jukka.liijynen@fi.ey.com">jukka.liijynen@fi.ey.com</a></td>
<td>+358 207 280 190</td>
</tr>
<tr>
<td>Germany</td>
<td>Tax Policy</td>
<td>Hermann Ottmar Gauß</td>
<td><a href="mailto:hermann.gauss@de.ey.com">hermann.gauss@de.ey.com</a></td>
<td>+49 30 25471 16242</td>
</tr>
<tr>
<td>Greece</td>
<td>Tax Policy</td>
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