



# BAKER TILLY INTERNATIONAL

*Great Firms, Outstanding Network*

INTERNATIONAL

## International **TAX INSIGHT**

July 2010

### EDITORIAL

Welcome to the July issue of International **TAX INSIGHT**.

In this quarter's issue we feature news of tax developments in Australia, Moldova, New Zealand, Portugal, Russia, Singapore, Spain, Tunisia, the United Kingdom (UK) and the United States of America (USA).

The tax information given is intended as a brief overview and may not cover all circumstances. Readers should seek professional advice before taking any action. Baker Tilly International firms worldwide will be pleased to advise further. To locate your nearest firm, please see the Worldwide Directory at [www.bakertillyinternational.com](http://www.bakertillyinternational.com).

**Bill Hogan**

*Director of taxation, Baker Tilly International*

### AUSTRALIA

#### **Government Responds to Tax Reform Review**

The government has now made public the tax reform recommendations which were included in the report of the Henry Review, the government commissioned study into the changes necessary to bring about the modernisation of the Australian fiscal system, and at the same time it has issued its initial response to those recommendations.

The report was delivered to the government in December 2009. It runs to about 1,300 pages and makes 138 recommendations in what amounts to a proposed programme for a comprehensive "root and branch" reform of the tax system. The government's response has been a limited one however. It has adopted just a handful of the recommendations, has rejected around 20 of them, and has remained largely silent on the remainder. The government states that the changes it will make now in response to the Review "are the first steps in a ten-year agenda", so it can be expected that some of the recommendations will come up for detailed consideration at a later stage.

Principal amongst the changes affecting businesses is a deferred reduction in company tax rates. The report was in favour of cutting the present 30% rate to 25% to encourage investment in Australia and to increase international competitiveness. This has proved too radical for the government however. Instead, for companies generally, it plans to reduce the rate to 29% from 1 July 2013 and to 28% from 1 July 2014. For small companies, defined as those with an annual sales turnover of not more than AU\$2m, it proposes to reduce the rate to 28% from 1 July 2012.

From 1 July 2012 there will be a new resource super profits tax (RSPT), chargeable on companies which exploit Australia's non-renewable resources, other than those companies which are

already subject to the petroleum resource rent tax (PRRT). RSPT will be charged at 40% and will be a deductible expense for company tax purposes. Companies currently subject to PRRT are likely to be given an option to switch to RSPT.

In the area of employer compulsory superannuation contributions newly announced intentions by the government actually go against Henry Review recommendations. The report favoured maintaining the rate at 9% of employees pay, but in fact it is now due to increase to 9.25% from 1 July 2013, 9.5% from 1 July 2014, and then by 0.5% each year until it reaches 12% on 1 July 2019. Furthermore, from 1 July 2013 contributions must be paid in respect of employees aged up to 75, instead of 70 as at present.

## **MOLDOVA**

### **Zero Tax Rate to End**

Since 1 January 2008 companies operating in Moldova have enjoyed a zero rate of corporate tax. This has applied both to net income and to capital gains. Previously a rate of 15% applied for 2006 and 2007. The government now plans to bring the zero rate to an end however. If its proposals are adopted the corporate tax rate will be 10% from 1 January 2012.

Although no tax is currently charged on profits, companies are nevertheless required to file returns and to declare their income and gains. Another of the government's new proposals, for large companies only, is for a mandatory requirement that tax returns are filed electronically. Large companies are currently defined for this purpose as those which pay annual taxes to the government, including payroll taxes, of more than MLD3m, equivalent to about €200,000, but this definition is now under review.

## **NEW ZEALAND**

### **Changes to Company Tax and GST Rates**

The government has announced its 2010 Budget and the measures proposed have quickly become law. They include significant changes to the rates of company tax and goods and services tax (GST).

Company tax is currently charged at 30% and this is set to reduce to 28% from 1 April 2011, which is the start of the 2012 tax year. The reduction mirrors that planned in Australia (see above), but will occur earlier in New Zealand.

The rate of GST, currently 12.5%, will increase to 15% from 1 October 2010. This means that international groups which have trading entities in New Zealand, or which import goods into the country, have only limited time in which to plan for the increase. Issues which may need to be addressed include pricing, accounting, budgeting, and possibly a review of the terms of any long term contracts.

The increase in the GST rate will inevitably impact upon the general public, but to compensate there will be reductions in the rates of personal income tax from 1 October 2010, including a cut in the top rate from 38% to 33%.

Other news from New Zealand is that the non-resident withholding tax will no longer be applied to dividends paid to non-resident entities which hold their shares other than in a portfolio capacity. Dividends paid to non-resident portfolio investors will be exempt from the tax if it would otherwise be levied at a rate of less than 15%. In each case the exemption is dependent on the dividend qualifying for the imputation credit, which in turn is dependent on the corporate income tax paid by the company.

## **PORTUGAL**

### **Tax Increases to Combat Budget Deficit**

The government's austerity measures to reduce its budget deficit include increases in the rates of corporate income tax and value added tax (VAT).

Corporate income tax is currently charged at 12.5% on the first €12,500 of annual taxable income and then at 25%. The new rule is that annual taxable income in excess of €2m will be taxed at 27.5%.

VAT, currently charged at reduced, intermediate and standard rates of 5%, 12% and 20% respectively, will be increased from 1 July 2010 by one percentage point across the board. In Madeira and the Azores Islands the intermediate and standard rates of 8% and 14% will similarly increase by one percentage point.

There will be small increases also in the personal income tax rates.

## **RUSSIA**

### **New Transfer Pricing Regulations to be Introduced**

Russia's current transfer pricing code is to be replaced completely by new legislation which is now making its way through the parliamentary processes and which is expected to take effect from 1 January 2011.

The new regulations will be more detailed than those they replace and they will conform more closely to the OECD's Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

They will apply to transactions between related parties, and the definition of related parties will be much wider than it is at present, with the tax authorities having the discretion to treat parties as related in any circumstances in which arm's length pricing for the transactions between them is likely to be compromised.

All transactions between related parties will be covered, including, in addition to goods and services, financial transactions such as loans and other credit arrangements, and the licensing of intangible

property. There will be a particular focus on commodities transactions, including oil, petroleum products, metals and precious stones, and there will be a special scrutiny also of transactions with entities located in a prescribed list of low-tax jurisdictions.

It will be a requirement of course that prices for transactions between related parties meet the arm's length standard. The three currently approved alternative methods of arriving at an arm's length price – comparable uncontrolled price (CUP), discounted resale price, cost plus – will continue, and three other methods will be added for use in defined circumstances. The authorities will regard CUP as the primary method, and they will expect it to be applied in all cases in which there are at least four comparables of prices charged between parties which are not related.

Strict documentation requirements will be imposed, initially to businesses which have transactions with related parties to a value in excess of RUB100m in a calendar year, but with this threshold steadily reducing to one of RUB10m a year.

The new rules include provision for transfer pricing audits by the federal tax authorities. The penalty for transgressing the rules will be as high as 40% of the additional tax found to be payable.

Advance pricing agreements (APAs), under which businesses negotiate acceptable pricing policies in advance with tax authorities, will be permissible, but only from 2012, and only for large businesses. APAs will generally have a three-year term, with a possible two-year extension. The penalty for breaching the terms of an APA will be RUB1.5m.

## **SINGAPORE**

### **New Productivity and Innovation Credit Can Cut Tax Bills**

The Singapore government is introducing a productivity and innovation credit (PIC) to encourage businesses operating there to maximise their use of modern technology.

The PIC will be a series of enhanced tax reliefs for six distinct categories of expenditure: research and development carried out in Singapore; the registration of intellectual property; the acquisition of intellectual property; design work carried out in Singapore; software and equipment which leads to greater automation; and the training of staff.

The enhanced tax reliefs will apply in each year of assessment from 2011 through to 2015. In each year, and for each of the six categories, the first S\$300,000 of expenditure will qualify for a 250% tax deduction. The balance of expenditure each year on research and development will qualify for a 150% deduction, whilst for the balance of expenditure in each of the other five categories there will be an immediate 100% tax write-off.

As an added boost, the S\$300,000 caps for 2011 and 2012 can be combined, so in each of the six categories of expenditure a 250% tax deduction will be available for the first S\$600,000 of expenditure whenever in 2011 or 2012 it is incurred.

Businesses which are unable to benefit from enhanced tax deductions, for example because they have relief available for past trading losses, and businesses which are in need of an urgent cash injection can obtain non-taxable cash grants instead of the PIC, subject to conditions.

The forthcoming PIC represents a significant improvement on the tax reliefs currently available. For example expenditure on the acquisition of intellectual property, which can include patents, trademarks and copyrights, has at present to be amortised equally over five years, while for expenditure on the production of designs there is generally no tax relief at all.

## **SPAIN**

### **Tax Law Changes Benefit Non-resident Entities**

Pressure from the European Commission has obliged the government to amend Spain's non-resident income tax law to bring it into compliance with the EU principle of the free movement of capital. Previously the law discriminated against EU based entities which derive income from Spain in that it taxed them more heavily than comparable Spanish resident entities.

As now revised the law treats residents and non-residents alike, and this will bring significant benefits to some entities which are based in an EU state other than Spain and which receive income from Spain. Specifically, EU based pension funds, undertakings for collective investment in transferable securities (UCITS), and corporations which receive income from Spain but do not have a permanent establishment there, as defined for tax purposes, will all now qualify for lower Spanish taxes.

Pension funds receiving dividends from Spanish companies will continue to have deducted from them at source a withholding tax of 19%, but this can now be reclaimed, so positive action is required.

Similarly, UCITS in receipt of dividends from Spain will continue to have the 19% tax deducted at source but by law now their actual liability is 1%, the same as that charged on comparable Spanish investment institutions, and they can reclaim the balance of 18%.

EU based corporations and other entities which receive income from Spain but which do not have a permanent establishment there, as defined for tax purposes, must now be given the same tax relief for their expenses as comparable Spanish entities, and they will be taxed on their net income rather than on their gross income. A permanent establishment implies a trading presence, so this amended rule is likely to benefit those in receipt of passive income from Spain, for example real estate rentals.

The new rules for taxing non-residents have been made retrospective to 1 January 2010. Since they correct a discrimination which is not permitted within the EU there may be a case for claiming tax refunds for earlier periods also, subject to statute of limitation constraints. Those potentially affected may wish to take advice in this regard.

## **TUNISIA**

### **Reduced Corporate Taxes as an Incentive to Public Flotation**

The incentive given to Tunisian joint stock companies (SAs) of reduced corporate taxes if they arrange to have their shares listed on the Tunisian stock exchange, an incentive previously scheduled to end on 31 December 2009, has now been extended to 31 December 2014.

The requirement is for a minimum of 30% of the company's shares to be listed and for them to remain listed for at least five years.

For companies which qualify, the corporate tax rate, generally 30%, is reduced to 20% for five years, beginning with the year in which the public flotation occurs.

If shares are withdrawn from listing before the expiry of the minimum five-year period the reduced rate concession is withdrawn retrospectively and interest is charged on the additional tax which becomes payable.

Telecommunications operators and hydrocarbon production and distribution companies, which are taxed at a special rate of 35%, are not eligible for the incentive.

## **UK**

### **New Scheme Aids Foreign Lenders**

When a UK company pays interest to a foreign loan creditor it is required under UK law to deduct a withholding tax of 20% and account for it to the tax authority, HM Revenue & Customs (HMRC). Where the payment is to a loan creditor based in a country with which the UK has a double tax treaty however this requirement under domestic law may be modified by the terms of the treaty. Under some of the UK's treaties with other countries the withholding tax is removed, whilst under others the rate of the tax is reduced.

For those lending funds from abroad to a UK company there is a liquidity benefit in their receiving their interest gross, or at a reduced rate of withholding tax. HMRC has always insisted however that the parties to a loan are not at liberty to simply implement the exemption or the reduced rate provided for by a treaty. Instead it has been necessary for the loan creditor to make a formal application to HMRC, with HMRC then authorising the UK company to apply the "treaty rate" only after making extensive checks that the loan qualifies for the benefits of the treaty. This process can

take months. In the meantime, tax must be deducted at 20% from payments of interest.

HMRC has now moved to improve this situation with the introduction of a double taxation treaty passport (DTTP) scheme. Foreign corporate lenders based in a country with which the UK has a double tax treaty can apply on a form DTTP1 for a "treaty passport". If successful the lender will be allocated a unique DTTP number and included in a publicly available register. A UK company borrowing from a foreign lender with a treaty passport can file a form DTTP2 with HMRC, and this will generally lead to a direction from HMRC that the nil or reduced rate of withholding tax provided for by the relevant treaty may be applied. Form DTTP2 must be filed within 30 days of the date of the loan.

The new scheme takes effect for loans from 1 September 2010, but applications for a treaty passport can be made now. The scheme will apply both for intra-group financing and for loans between unconnected parties. Foreign corporate lenders potentially eligible for a passport should consider making an application. They might also wish to amend their loan documentation so as to require borrowers to file a form DTTP2 within 30 days of the date of the loan. They will then be doing all that they can to avoid or to reduce UK withholding tax.

## **USA**

### **HIRE Act Increases the Scope of Withholding Tax**

The Hiring Incentives to Restore Employment (HIRE) Act has now become law. It is a package of measures, designed primarily to encourage businesses to hire and retain new employees, but with revenue raising features also, based on increased reporting requirements for the owners of foreign financial assets, and an extended obligation on US entities making payments abroad to deduct and account for withholding tax.

Currently withholding tax at 30% must be deducted from payments abroad of "fixed or determinable annual or periodical income", which is widely defined to include for example dividends, interest, rents and salaries. There are some statutory exemptions from the requirement, including for bank deposit interest, and it can also be modified by the terms of bilateral double tax treaties with other countries.

The obligation to deduct withholding tax does not currently apply to remittances abroad of capital gains, but the HIRE Act provides that for payments made after 31 December 2012 to foreign financial institutions the tax must be deducted from the gross proceeds of the sale of assets which give rise to US source dividend or interest income. There will be an exemption for assets owned on 18 March 2012, which is two years after the Act becomes law. The withholding tax requirement will be extended also to payments to

foreign financial institutions of interest on deposits with foreign branches of US banks.

Financial institutions which will be affected by these changes may wish to note that there is a facility by which they can enter into an agreement with the Internal Revenue Service (IRS) that they will be exempted from the withholding tax in return for the supply to the IRS of information concerning accounts held by one or more US persons or by foreign entities owned as to 10% or more by US persons. Information will not be required in connection with accounts held by specified categories of US entity, including corporations with publicly traded stock, tax exempt organisations, and federal, state and local government bodies.

#### **Disclaimer**

Baker Tilly International is a worldwide network of independent accountancy and business advisory firms united by a commitment to provide exceptional client service. Baker Tilly International provides no professional services to clients but acts as a member services organisation. Baker Tilly International Limited is a company limited by guarantee and is registered in England and Wales.

International **TAX INSIGHT** is designed for the information of users. Every effort has been made to ensure that at the time of preparation the information contained is accurate. Information within International **TAX INSIGHT** is not designed to address a particular circumstance, individual, or entity. Users should not act upon it without seeking professional advice relevant to the particular situation. No responsibility for loss, however arising, to any person acting or refraining from acting as a result of any material in this publication will be accepted by Baker Tilly International Limited.

© 2010 Baker Tilly International Limited, all rights reserved.

Baker Tilly is a trademark of the UK firm, Baker Tilly UK Group LLP, used under licence.



#### **WorldHeadquarters**

2 Bloomsbury Street  
London WC1B 3ST  
United Kingdom

**T.** +44 (0)20 7314 6875

**F.** +44 (0)20 7314 6876

**E.** [info@bakertillyinternational.com](mailto:info@bakertillyinternational.com)

[www.bakertillyinternational.com](http://www.bakertillyinternational.com)