Summer 2023
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Trouble down under

PwC Australia and the tax leaks scandal

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ITR

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Trouble down under

Our cover story looks at the Australian tax leaks scandal and the implications for PwC Australia. The firm is grappling with the fallout from the revelations of confidential information on tax policy being shared by email.

These emails included policy details from high-level meetings with Treasury officials. At first, it was unclear how many people had received confidential information. PwC recently named 67 recipients of emails in a letter to the Senate.

A series of high-profile resignations followed soon after the leaks. An independent inquiry has also been launched, though the story is far from over. The leaked messages go beyond Australia's sunny shores as far away as Ireland, Singapore and the US.

The last thing any firm wants is a scandal which it cannot contain and manage – least of all a firm as invested in trust as PwC. We can understand why the firm has moved quickly to remove members of staff implicated in the leaks, but this story is not slowing down.

It's possible that the Australian government will take the leaks scandal as a pretext for wrapping tax advisers in more red tape, inviting other countries to follow suit. Advisers are already facing more regulatory pressure, particularly from the EU.

A lot of senior tax professionals outside PwC who have worked with governments will be searching their minds for any possible indiscretions either in speech or in writing. WhatsApp messages and emails are not to be written hastily.

Josh White
Special projects editor

> "The last thing any firm wants is a scandal which it cannot contain and manage – least of all a firm as invested in trust as PwC"

We know what often begins as a tax scandal rarely ends with a few headlines. Many reforms have been implemented over the last decade, spurred by public outrage over tax avoidance and evasion. This could be another catalyst for stricter rules.

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MEET THE TEAM

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TraTax welcomes senior practitioner to its team

Malaysia law firm TraTax has added a special adviser for investments and incentives to its team.

Ahmad Khairuddin Abdul Rahim brings with him more than 31 years' of experience working with the Malaysian Investment Development Authority, most recently serving as the deputy CEO. His work is focused on various different areas, including policy formulation and investment promotion.

Dentons opens tax practice in New Zealand office

International law firm Dentons has expanded the offering of its New Zealand branch – Dentons Kensington Swan – with the addition of a tax practice.

This will be led by **Bruce Bernacchi**, who joins the team as a partner from GreenMount Advisory. The Auckland-based practitioner has extensive experience in the market, having previously spent more than 10 years with General Electric in various roles, as well as working for over four years with KPMG.

Bernacchi's work is focsed on a range of taxation issues, including domestic and international corporate tax matters, indirect taxes and employee tax issues. In particular. He specialises in advising private equity clients, the financial services sector and technology companies.

NGL Tax adds partner to its tax practice

Polish firm NGL Tax has added a partner to its team.

Katarzyna Czerkies-Laskowska joins the firm from private practice. She brings with her extensive experience in the Polish market, including more than nine years spent with PwC and more than seven at Deloitte.

Czerkies-Laskowska's work centres on corporate income tax issues, including transfer pricing in the retail, manufacturing, shipbuilding and transportation sectors.

Blank Rome expands tax team in New York

US law firm Blank Rome has added a private client associate to its tax practice based in its New York office.

Haley Bybee joins the team from McDermott Will & Emery, where she served for almost three years as a private client associate.

Bybee's experience includes work covering estate planning documents, the administration of estates and establishing tax-exempt organisations, foundations and trusts, in addition to a range of other matters, primarily in the private client space.

Watson Farley & Williams expands UK tax offering

International firm Watson Farley & Williams has hired a tax specialist to its London practice.

Claire Miles joins the team as a partner from Willkie Farr & Gallagher, where she worked as an associate for more than five years. She previously served as a senior associate for Watson Farley & Williams for more than a year.

Miles is a chartered tax adviser whose work encompasses a range of corporate and commercial tax matters. She has experience across M&A, corporate reorganisations, advisory and finance.

Albert Goodman appoints two tax managers to growing team

South-west England regional chartered accountancy firm Albert Goodman has recruited two managers to its expanding practice.

Based in Bristol, **Lauren Chadwick** and **Julie Harding** both join the company from Evelyn Partners, which was previously Smith & Williamson. Chadwick had been with her previous employer for more than 10 years, most recently serving as a trust manager. Harding's departure, after six years, also marks the end of her tenure as a trust manager at the company.

Both managers' work is focused on estate planning, including tax compliance, advice and accounts for family trusts, individuals and estates.

Azets acquires Baker Tilly Ireland

International outsourcing, compliance and advisory group Azets has acquired the Irish branch of international tax network Baker Tilly.

The office was rebranded as Azets Ireland and represents the first move into the country by the international group.

Azets operates across multiple offices in the UK, as well locations in the Nordics and Romania.

Galvão Villani expands tax offering with three hires

Brazilian firm Galvão Villani Navarro Zangiácomo e Bardella Advogados has added a team of three lawyers, including one partner, to its São Paulo office.

Partner **Marcia Harue Ishige de Freitas** joins the firm from Hallem Advogados, a firm she founded and worked at for over four years. She has more than 20 years of experience in the market and has a focus on corporate restructuring and estate planning.

Two associates have also joined the firm from Hallem Advogados: Jorge Luz and Gabriela Carneiro Sultani. The latter has worked with Harue Ishige de Freitas for more than 10 years, while Luz has been part of the team since 2020.

S&R Associates adds team of three to New Delhi office

Indian law firm S&R Associates has appointed a team of three lawyers, a partner and two associates, has joined its tax practice.

Partner **Ajinkya Gunjan Mishra** joins the firm from Luthra & Luthra Law Offices, where he had been for 12 years and served as a partner for the past five. His work is focused on indirect tax and trade law, including matters of GST, VAT, service tax, central and state excise, sales tax and customs matters.

Mishra is joined at the firm by associates **Avani Tewari** and **Tarusha Airan**. Both also come from Luthra & Luthra Law Offices, with Airan having been an associate there for more than a year and Tewari spending more than three years with the firm, including one year as a senior associate.

Andersen welcomes managing director to Orange County office

Andersen, the US branch of international tax network Andersen Global, has taken on a new managing director of its team in California.

Edvin Givargis joins the state and local tax practice in Orange County. He brings with him more than 20 years' experience, focusing on developing and advising on efficient tax structures and operations within a complex state framework across various state tax types.

Burgess Salmon bolsters corporate tax team

UK law firm Burgess Salmon has hired a new director to its corporate tax team.

Gillian Griffiths joins the firm's corporate tax practice from Deloitte, where she had served for more than six years as an associate director in the financial services tax team. Her previous experience includes roles in Singapore and working as a solicitor for Berwin Leighton Paisner and tax senior manager for BDO.

Griffiths' work is primarily focused on the financial services sector and on advising alternative asset managers, along with developing tax solutions and managing domestic and cross-border projects.

New firm launches in Brazil

A new firm has been launched in São Paulo under the name SouzaOkawa Advogados. It is formed of eight partners, five of whom are part of its tax practice.

Those partners are **Igor Nascimento de Souza**, **Juliano Rotoli Okawa**, **Felipe Medaglia**, **Francisco Leocádio** and **Mariana Alves Galvão Arbach**. All five of them were at Madrona Advogados prior to founding the firm, with Souza, Okawa and Medaglia all partners at the previous firm.

Dentons promotes counsel in Paris office

International firm Dentons has promoted a member of its team in France to the position of counsel.

David Lévy is a member of the Paris tax group. He specialises in French and international tax law and advises on the tax aspects of M&A, fund structuring and on structuring investments in the private equity and real estate sectors, in France and abroad.

The promotion follows the addition of Laurence Clot as a partner in July 2022 and the promotion of Jérôme Le Berre to partner in April that year.

Baker McKenzie announces global tax group chair

International law firm Baker McKenzie has secured a key hire who will be taking over as the chair of its global tax group.

Washington DC-based **James Wilson** will take the position. He has been with the firm for more than 20 years and worked in three different offices on two continents. His work is focused on complex transactions and disputes, and he is currently chair of the firm's global tax planning, transactions and tax policy sub-practice group.

Mayer Brown appoints former Treasury partner in DC

International law firm Mayer Brown has made a former Treasury attorney a partner at its tax practice in Washington DC.

Sonal Majmudar joins the team from the US Department of the Treasury, where she was an attorney with the IRS. She had spent 11 years in that role and had previous worked in the global tax team of the World Bank Group and as a lawyer with Grant Thornton and Baker McKenzie.

Majmudar has experience in transfer pricing matters, specifical negotiating Advance Pricing Agreements with US and foreign tax authorities and resolving double taxation cases through the mutual agreement procedure of bilateral tax treaties.

Andersen continues global expansion in Europe, Australia and the Americas

International tax network Andersen Global continues to expand its global footprint by joining forces with firms from across the globe.

In the US, it both increased its existing presence and founded two new offices, welcoming new employees to its Orange County operation and opening locations in Des Moines and Pittsburgh. In all, 45 new people were added to the team, with professionals from Rickmeyer & Associates and Vertical Advisors joining the California office, from Hamilton Juffer & Associates and HJN Advisors joining the Des Moines office, and from Chemel Kornick & Mooney arriving in Pittsburgh.

In Brazil, Andersen signed a collaboration agreement with Rolim Viotti Goulart Cardoso Advogados. Founded in 1993 by managing partner João Dácio Rolim, the law firm has offices in São Paulo, Rio de Janeiro, Belo Horizonte and Brasília.

In Australia, the network joined professional services firm BoardRoom, adding locations in Sydney, Melbourne and Brisbane. The company provides clients with accounting, payroll, corporate secretarial and related services to both private and public entities and has been in operation for more than 50 years.

The network made partnerships in several locations in Europe. In Austria, it signed a collaboration agreement with CHG Czernich Rechtsanwälte. Founded in 1999 and led by managing partner Dietmar Czernich, it operates from offices in Innsbruck, Vienna, St Johann and Kitzbühel.

In Switzerland, it joined mobility and professional services company Exactico. Based in Basel, it is led by managing partners **Per Melberg**, **Selim Bucher**, **Karin Verheijen** and **Alberto Perez**. Moving east, in Romania, the network signed a collaboration agreement with CMF Consulting, a valuation services firm established in 1992.

Andersen adds managing director to its US national tax team

Andersen, the US branch of the international tax network Andersen Global, has appointed a new managing director at its Washington DC office.

Cory Ellenson joins the team from EY, where he had been for more than six years. He had previously served in the IRS Office of Chief Counsel and with the Congressional Oversight Panel of the US Senate.

Ellenson brings with him brings more than 12 years of experience in federal tax controversy, including representing clients through all stages of IRS audits and appeals and resolving all IRS practice and procedure matters.

Tax partner re-joins Rodrigo Elías & Medrano

Peruvian law firm Rodrigo Elías & Medrano has announced the return of a tax and estate planning partner to its team in Lima.

José Chiarella had previously spent more than seven years as a partner with the firm, before moving to Garrigues for almost three years. He became a founding partner of Damma Legal Advisors, where he had been for more than four years before returning to Rodrigo Elías & Medrano.

Chiarella's work is focused on tax planning, international tax, M&A, project finance and advising local families on estate matters.

A&O and Shearman & Sterling reveal multi-billion merger plan

The two firms, both of which have tax offerings, would have around 4,000 lawyers in nearly 50 offices worldwide.

Ed Conlon

Allen & Overy and Shearman & Sterling plan to combine forces and create a legal powerhouse with $3.4 billion in revenue, the firms announced on May 21.

The new entity, named A&O Shearman for short, would have 3,900 lawyers and 800 partners spread across 49 offices. It would be the only global firm with US, English and local law capabilities in equal measure, the announcement claimed.

The combination would allow Shearman & Sterling, a New York-headquartered firm with some offices outside the US, to benefit from A&O's global strength. Likewise, A&O would have "increased board-level recognition and expanded access to a corporate client base in the US", the statement said.

Both firms said the plan was driven by clients who wanted global and integrated legal advice, adding that the two parties were a natural fit.

"What excites me about this merger is the complementary cultures of our two firms," said Wim Dejonghe, senior partner at A&O. "We have striking similarities across the board, and I believe we are going to be wonderful partners to one another on this journey."

Adam Hakki, senior partner at Shearman & Sterling, added that the two firms were "kindred spirits".

"We have both always placed great emphasis on attracting and retaining top talent, were early to globalise, and are relentlessly focused on quality, excellence and collaboration.

"This is truly a game-changing moment for both firms that will create an unparalleled offering for our clients," he added.

In tax, A&O boasts more than 100 specialists internationally who work across a range of disciplines including investigations and indirect tax.

Shearman & Sterling says its tax practice plays an integral role in the firm's corporate and cross-border practice, specialising in tax controversy and litigation among other areas.

The planned merger comes after failed attempts by both firms to combine with other market players.

In March, Shearman & Sterling abandoned talks over a tie-up with transatlantic firm Hogan Lovells, while A&O previously pursued a merger with another US firm, O'Melveny & Myers.

The plans are subject to an approvals process, which includes a partner vote on both sides.

The A&O Shearman deal is one of the biggest mergers in history

Why ChatGPT won't take your tax job – for now

ChatGPT can be used by tax advisers but it won't replace them just yet, evidence suggests.

Euan Healy

By reaching over 100 million users in January 2023, two months after it was launched by OpenAI, the conversational artificial intelligence chatbot ChatGPT became the fastest-growing app in history.

It has sparked a technology race where established search engines like Google – which launched its own AI chatbot, Bard, in March – are attempting to incorporate conversational AI technology into their services.

Financial services professionals, including tax advisers, are not exempt from these changes – they all use technology as part of their businesses, and their clients value it. The OECD reported last year, for example, that 75% of tax administrations had a digital transformation strategy in place.

But how will ChatGPT be used in tax, and by whom?

AI errors

When it comes to tax advice, and the potential for ChatGPT to replace tax advisers, all the evidence suggests that the technology isn't quite up to scratch, yet.

Geoff Peck, founder and chief taxologist at PawPaw Taxology, a London-based company that provides technology training to tax professionals, says that ChatGPT doesn't have the accuracy to replace professionals right now.

"It definitely has some use – it's a powerful tool – but I can't see it replacing anyone for now," he says.

ChatGPT's answers to tax queries consistently appear well-written, intelligent, and correct. But when it comes to challenging questions, the answers are quite often wrong. Forbes tested this out by posing several tax questions with varying difficulty and found that complex queries are often answered incorrectly and with outdated information.

ChatGPT also relies on users asking the correct questions. Knowing exactly what to ask in any field requires some expertise. Tax advisers don't just answer questions, they aid in identifying which ones should be asked and can spot when a client is asking the wrong question.

What's more, Peck points out that the use of AI in tax doesn't have the regulatory framework that it would need to be used to provide tax advice without the input of a professional.

"All the evidence suggests that the technology isn't quite up to scratch, yet"

ChatGPT is unlikely to substitute for the human touch any time soon

"Until it is approved legally, it's just useful information," he says.

On top of ChatGPT's tax faults, interacting with AI and eliciting the right information is much easier to do if someone knows how best to talk to an AI tool. This isn't something that most people have spent time practising. AI might need to improve dramatically to replace human tax advisers, but humans will also need to get much better at using AI.

If any doubt remains over whether ChatGPT can be relied upon instead of a tax adviser, when asked "Should I rely on ChatGPT for tax advice?", ChatGPT itself told *ITR:* "No, it is not advisable to rely solely on ChatGPT for tax advice. While ChatGPT is a sophisticated language model with access to a vast amount of information, it is important to remember that tax laws and regulations can vary depending on your location, income level, and other individual circumstances.

"It is always best to consult with a qualified tax professional who has expertise in your specific tax situation. A tax professional can provide personalised advice and guidance tailored to your unique needs and circumstances. Additionally, tax laws and regulations can change frequently, so it is important to stay up to date on any updates or changes that may affect your tax situation," it replied.

Whether it be for personal income tax issues or advice on country-by-country corporate tax reporting, the chatbot consistently recommends using qualified tax professionals.

AI advice

At the beginning of 2022, KPMG and Blue J, a Canada-based software company specialising in tax law and AI, launched a "first-of-its-kind" AI toolkit for KPMG advisers to use for predicting tax scenario outcomes. It was an attempt to incorporate AI into the working practices of professionals and make their jobs easier rather than replacing them.

AI is very good at handling repetitive, numerical tasks so, despite it not being able to replace tax advisers, it can certainly help them out. In its current state, ChatGPT can be used to streamline tax advice by providing quick answers to simple questions, helping with data entry, and generating reports.

"It's not going to replace anyone yet, but it can help people get background information and automation. That's the role it can play, that's what I use it for," says Peck.

"You can ask simple questions about areas that you might not have expertise in, and it'll tell you what it knows, but that's all," he adds.

Even if ChatGPT can't replace advisers yet, there's always a concern that when technology increases efficiency, that might mean fewer people are needed in an organisation. There's little sign that this is the case, but then again, ChatGPT is just getting started.

As tax calculations become increasingly technical, AI might become more and more useful, but human advisers can breathe a sigh of relief.

Advocate general says Commission wrong in Engie state aid case

Luxembourg did not grant illegal state aid to French utility company Engie, according to an adviser to the Court of Justice of the EU.

Josh White

Advocate General Juliane Kokott issued an opinion on May 4, finding that the European Commission had erred in its decision that Luxembourg granted French utility company Engie illegal state aid.

The Commission found in June 2018 that Luxembourg had granted unlawful state aid to Engie in tax rulings. Engie and Luxembourg decided to fight the allegations, but the General Court ruled in favour of the Commission in May 2021.

Kokott proposed that the Court of Justice of the EU (CJEU) uphold the appeal of Luxembourg and Engie against the 2021 judgment. She concluded that the Commission decision should be annulled and the General Court ruling set aside.

According to Kokott, tax rulings in themselves do not necessarily constitute illegal state aid provided they are legal nationally and open to all taxpayers. National law is the sole reference framework, she argued.

The AG also argued the Commission take a restricted standard of review when it comes to decisions by tax authorities, specifically limiting its reach to plausibility checks. Rulings that are clearly erroneous in favour of the taxpayer may constitute a selective advantage and breach state aid law.

However, Kokott stressed that the Luxembourg tax rulings granted to Engie were not erroneous, adding that such matters are for a national tax authority and not the Commission or the CJEU.

Otherwise, she said, the European Commission and the CJEU may impinge on the fiscal autonomy of EU member states when it comes to national tax policies.

15 years in the making

The case dates to tax rulings from 2008 to 2014. At the time, Engie was called GDF Suez and the group structured financial transactions through Luxembourg companies.

These rulings concerned the tax treatment of two similar financial transactions between four companies of the GDF Suez group – GDF Suez Treasury Management, GDF Suez LNG Supply, LNG Luxembourg and Electrabel Invest – all based in Luxembourg.

> "Tax rulings in themselves do not necessarily constitute illegal state aid provided they are legal nationally and open to all taxpayers"

The parent company transferred its shares to a subsidiary within the Engie group, in which the subsidiary then financed the shares through an interest-free convertible loan with an intermediary. This loan was reimbursed by the subsidiary by issuing shares equal to the amount of the loan, plus a premium involving the profits made.

The intermediary sold shares back to the parent company to finance the loan. If any profit was made, the holding company was entitled to the rights of owning the shares issued. The tax rulings also meant that only the subsidiary was taxed on a margin.

Under this structure, the subsidiary paid very little tax by deducting the interest cost while the holding company obtained shares that were not taxable.

These companies mainly acted as intermediaries for intra-group financing transactions within the GDF Suez group. The EU investigation concluded that Luxembourg's treatment of the financing structures did not reflect economic reality.

> "The EU investigation concluded that Luxembourg's treatment of the financing structures did not reflect economic reality"

After the General Court upheld the Commission's findings in May 2021, Engie and Luxembourg lodged an appeal with the CJEU.

The AG's opinion is not binding on the CJEU.

Is this a turning point for Engie?

Timeline: PwC Australia and the tax leaks scandal

PwC Australia is grappling with the fallout from revelations that its partners used confidential government information to secure new business and advise clients.

Josh White

Euan Healy

The Australian tax leaks scandal has rocked the accounting industry in the country as PwC Australia faces claims that its professionals may have benefited from sharing information on tax policy.

We know that dozens of tax professionals at the Australian branch of the 'big four' firm received the information by email, but the full extent of what happened is still unfolding.

New South Wales Senator Deborah O'Neill is leading the Senate inquiry into the scandal. She chairs the Joint Committee on Corporations and Financial Services.

Meanwhile, PwC Australia has launched an internal investigation and there is an independent inquiry that will publish a final report in September 2023. A criminal investigation into a former PwC employee has also begun.

ITR has followed the story from the very beginning. Here is our timeline of events over the last six months.

January

The scandal broke in January 2023 with the news that Peter-John Collins, former head of international tax at PwC Australia, had shared confidential information on tax policy with his colleagues.

On January 23, the Tax Practitioners Board (TPB) confirmed a report from the Australian Financial Review that it had de-registered Collins for failing to act with integrity.

Collins was a member of an advisory group involved in high-level Treasury discussions. The Australian government was developing anti-tax avoidance measures at the time. The report found he had broken confidentiality agreements made with the Treasury in 2013, 2016 and 2018.

After its investigation, the TPB concluded that Collins had shared confidential information about tax policy with his colleagues. He received a two-year ban from the

> We did have a partner breach a confidentiality agreement. That was totally unacceptable that he did that, and we've been very clear that that should never have happened

TPB on December 23 2022. This penalty was criticised by Senator O'Neill as a "slap on the wrist".

The TPB found that the information was later shared with established and potential clients. Collins left the firm in October 2022 before the TPB investigation concluded in November.

Later, on January 25, Treasurer Jim Chalmers pledged to "throw the book" at those responsible for this breach of trust. He said he was "absolutely furious" about the case.

PwC Australia acknowledged it "failed the high standards we set for ourselves as a firm". The TPB ordered the firm to improve its standards and training on potential conflicts of interest.

February

The tax leaks scandal was extended to many more tax professionals working at PwC. Michael O'Neill, CEO secretary of the TPB, told the Senate inquiry on February 15 that there were between 20 and 30 people at PwC involved in leaking government information.

Treasurer Chalmers introduced an amendment to the Tax Agent Services Act (2009) on February 16 to strengthen the TPB following the PwC Australia leaks. The Labor government also moved to close loopholes allowing de-registered tax agents to continue to operate.

March

PwC Australia CEO Tom Seymour denied that the tax leak involved up to 30 partners at the firm on March 9. He told the Australian Financial Review that the firm had a "perception issue" for not having a better system in place to manage confidentiality agreements.

"The issue for us is there's a perception issue and that's because we didn't have the right management tool in place," said Seymour. "We believe our conflict management tools ... are now actually probably the best of anywhere in the world.

"We did have a partner breach a confidentiality agreement. That was totally unacceptable that he did that, and we've been very clear that that should never have happened," Seymour told the AFR.

The leaks scandal was not going to go away though.

May

By early May, the Senate investigation was well under way and the batch of PwC emails – reaching as far away as Singapore, Ireland, the UK and the US – was about to make headlines.

Deborah O'Neill, Labor senator for New South Wales, secured the PwC emails on May 2. These messages reached at least 53 PwC members of staff and 14 clients may have benefited from the information.

The Senate went public with the emails on May 3 and PwC Australia CEO Seymour resigned on May 8, after admitting that he received emails containing confidential information. The following week, he announced he would be retiring on September 30.

Seymour admitted receiving information from Collins. After Seymour's resignation, PwC Australia said: "We have agreed with Tom that it is in the best interests of the firm and our stakeholders."

Kristin Stubbins, head of assurance at the time, became acting CEO after Seymour stepped down.

Two partners, Pete Calleja and Sean Gregory, stepped down from the Australian firm's executive board on May 10. Calleja was head of financial advisory services at PwC Australia, while Gregory was responsible for risk management at the firm.

PwC Australia announced on May 15 that an independent investigation into the firm's culture and operations had begun. Australian businessman Ziggy Switkowski, chairman of banking group Suncorp, was brought in to lead the review.

Meanwhile, the firm opened its own internal investigation and PwC Global flew executives out to Australia to take oversight of the situation.

By the following week, the Australian government was saying the scandal could bear criminal dimensions, and soon enough the Treasury had referred the Collins case to the Australian Federal Police (AFP) on May 24.

The AFP confirmed the investigation into the conduct of Collins that same day. However, questions quickly arose about a possible conflict of interest between the AFP and PwC Australia.

On May 25, the Senate revealed that the AFP relied on the firm for its internal audits. AFP Commissioner Reece Kershaw assured the Senate that the nine contracts with PwC Australia would not influence the investigation.

As a result, the Australian government directed all PwC employees involved in the tax leak scandal to step back from government work. PwC Australia suspended nine unnamed partners on May 29.

PwC stated that it had told the nine partners to "go on leave effective immediately" while the investigation takes place.

It also said that it will ringfence its federal government business to minimise conflicts of interest and appoint two independent, non-executive directors to its governance board.

"We understand that we betrayed the trust of our stakeholders, and we apologise unreservedly," said acting CEO Stubbins.

June

By the start of June, the Joint Committee on Corporations and Financial Services was planning to publish the names of the email recipients. PwC Australia named the 67 staff, including four former

> We understand that we betrayed the trust of our stakeholders, and we apologise unreservedly

> "PwC should release these names themselves, and they should do it publicly"

partners, who appear in emails linked to the tax leak scandal in a June 5 letter to the committee.

The firm also disclosed the names of the nine partners who were sent on immediate leave because of their association with the leaks.

"The four former partners include Michael Bersten, Peter Collins, Neil Fuller, and Paul McNab," wrote Stubbins. "Tom Seymour no longer has any role in our firm, and we will take appropriate action for these individuals when our investigation is complete."

Stubbins also noted that the 63 other staff who were named included anyone who had received at least one email, and that they had all been contacted and notified of their involvement. There was soon pressure from the Senate to make all the names public.

Senator O'Neill accused the firm of hiding behind the "cloak of the Senate" instead of announcing the names itself, despite providing the requested information.

"PwC should release these names themselves, and they should do it publicly," she said.

The Joint Committee on Corporations and Financial Services resumed the inquiry on June 7. At this point, the impact of the scandal was hitting the firm's contracts with certain clients.

By June 12, five major Australian pension funds representing more than A$750 billion ($507 billion) in savings had frozen contracts with PwC Australia.

AustralianSuper was the first major pension fund – with A$270 billion in assets – to freeze new contracts with PwC on June 2. Aware Super, Australian Retirement Trust, CareSuper and Hesta followed AustralianSuper's decision to freeze contracts with PwC Australia.

Legalsuper and Rest Super are reviewing their arrangements with the firm, while Cbus and Hostplus are reportedly monitoring developments closely. Most of the Australian pension industry relies on the big four firms for audit and tax services.

Each company needs two firms to handle internal and external audits separately. This may mean super funds will turn to PwC's rivals for new contracts.

The scandal is far from over.

The Australian tax leaks scandal has rocked the accounting industry

AUSTRALIA

DLA Piper Australia

Jock McCormack

Australian federal budget released with a wave of reforms

The Australian government delivered its 2023/24 Federal Budget on Tuesday 9 May 2023, demonstrating and reaffirming its strong commitment to critically important international and related tax reforms.

The key initiatives from the Budget include:

- Implementing the OECD/G20-led Pillar II solution, incorporating the 15% global minimum tax for large multinational enterprises for income years commencing on or after January 1 2024;
- Expanding Australia's general anti-avoidance rules (Part IVA) to apply, firstly, to arrangements designed to access lower withholding tax rates on income paid to foreign residents (for example, under double tax treaties) and, secondly, potentially where there is a dominant purpose to reduce foreign income tax;
- Reducing the managed investment trust withholding tax rate from 30% to 15% for eligible new build-to-rent projects;
- Extending the clean building managed investment trust withholding tax concession (10%) to eligible data centres and warehouses;
- Limiting the proportion of petroleum resource rent tax (PRRT) 'assessable income' that can be offset by deductions to 90% (of the assessable receipts), effectively introducing a 'cap' on deductions. Separately, the government will 'modernise' the PRRT from July 1 2024, following the Treasury review of the PRRT, including gas transfer pricing;
- Tightening (or clarifying) the concept of 'exploration for petroleum' in the practical application of PRRT; and
- Deferring the start date for the tax integrity measure previously announced for franked distributions funded by capital raisings from December 19 2016 to September 15 2022.

The government also continues to progress other international tax developments dealing with thin capitalisation, restricting deductibility of payments for intangibles in low tax jurisdictions and international tax transparency/disclosure. It is expected that these international tax developments will progress through parliament in the coming weeks.

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CHINA

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Income tax incentives in the Hengqin-Macau zone

China has for several years been pushing forward an economic development strategy for the Guangdong-Hong Kong-Macau Greater Bay Area. As part of this, in 2021, the Chinese government announced a plan to increase the industrial diversity of Macau, a special administrative region of China with separate regulatory and tax regimes, through building up the Hengqin-Macau cooperation zone. Hengqin itself falls under the mainland China regulatory and tax regimes. Technological R&D, high-end manufacturing, tourism, and modern finance are to be fostered, in part through several income tax incentives:

- A reduced 15% corporate income tax (CIT) for enterprises in the encouraged industries;
- A CIT exemption for 'new' foreign-sourced income received by enterprises registered in the zone and engaged in tourism, modern services and high-tech industries;
- 100% expensing, and accelerated depreciation regimes for eligible capital expenditure; and
- A maximum of 15% individual income tax (IIT) rate for the income of personnel with high-end and urgently needed skills; and another rule applicable to Macau residents working in the zone to lower their mainland China IIT burdens.

To supplement these incentives, the relevant government authorities recently announced the substantive operation requirements (applying from January 2023) and implementation guidance (retroactively applying from January 2021).

The substantive operation requirements aim to ensure that the benefits of the incentives can only be accessed by enterprises with a real economic link to the zone, and cannot be otherwise abused. The 'four elements' of these requirements (production and business operation, staff, accounting and assets) are largely consistent with the provisions introduced for the Hainan free trade port (FTP), but with a few differences.

For example, the Hengqin-Macau rule requires that individuals must pay at least six consecutive months of social security (such as pension insurance) in the Hengqin-Macau zone. By contrast, the Hainan provision needs at least 183 days of residence in a tax year to qualify for the incentives. The Hengqin-Macau rule is more in favour of enterprises and is easier to be achieved. Another difference is that the Hengqin-Macau zone sets out more specific and detailed supporting materials (such as a lease agreement for business premises, social security payment certificates) to evidence whether the above four elements are met. The evidence in Hainan FTP mainly relies on the written explanation.

In parallel, the implementation guidance also explicitly clarifies the criteria for personnel with high-end and urgently needed skills to enjoy the IIT incentives:

- Personnel with high-end and urgently needed skills must be engaged either in the encouraged industries (technology R&D and high-end manufacturing, Macau-branded industries, tourism and finance) and several other designated sectors (including the construction and medical fields);
- The personnel need to genuinely work in the Hengqin-Macau zone and must have at least a one-year employment contract with enterprises that substantively operate in the zone. The enterprises must meet the substantive requirements test;
- To be identified as personnel with high-end skills, the person is required either to be at a leading level in a field or have an annual income of no less than RMB 0.5 million ($71,000); and
- As for the personnel with urgently needed skills, they must either meet the education or professional or occupational requirements.

Apart from the Hengqin-Macau zone and Hainan FTP, several other special economic zones in China also offer regional preferential tax treatments. Businesses are urged to review the different tax treatment of each zone and even differences in and outside the zones before investment and business deployment, especially with a view to BEPS 2.0 global minimum tax.

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HONG KONG SAR

KPMG China

Lewis Lu and John Timpany

Consultation launched on the inclusion of foreign-sourced asset disposal gains under Hong Kong's FSIE regime

Hong Kong has committed to updating its foreign-sourced income exemption (FSIE) regime by the end of 2023 to cover foreign-sourced gains from the disposal of assets other than shares and equity interests. The move is a response to the EU updating its guidance on FSIE regimes in late 2022 and explicitly requiring such regimes to cover gains from the disposal of all types of assets (disposal gains).

The expanded FSIE regime in Hong Kong is expected to take effect from January 1 2024.

Key changes proposed and views sought

The Hong Kong SAR government circulated a consultation document on April 6 2023 to set out the proposed changes to the FSIE regime and seek views from stakeholders on related issues. The document focuses on the expanded scope of assets in relation to foreign-sourced disposal gains.

The proposed changes are subject to negotiations with the EU and the other existing features of the FSIE regime would remain unchanged.

The key proposed changes and the issues raised for comments in the consultation document are summarised below.

Covered assets

The EU requires all disposal gains to be covered, regardless of whether they are capital or revenue in nature and whether the assets are financial or non-financial in nature.

Although the government has explored a positive listing approach covering the following additional types of assets – (1) debt instruments, (2) movable properties, (3) immovable properties, (4) intellectual properties and (5) foreign currencies – the EU requires a non-exhaustive list instead of a definite and exhaustive list of covered assets.

Views are sought on (1) the definition of covered assets and (2) whether the above five types of assets (or any other assets) should be cited as examples of covered assets in the domestic legislation.

Computation of disposal gains or losses

The government has taken up with the EU the possibility of rebasing the costs of assets to those as at the effective date of the FSIE regime when computing the taxable amount of disposal gains so that the taxation of foreign-sourced disposal gains would not be applied retrospectively. However, the EU has concerns about the grandfathering effect of such a rebasing approach and advised that such approach has not been accepted by the EU for other jurisdictions.

The government will explore with the EU other means, such as taper relief (a mechanism by which the taxable amount of disposal gains is reduced according to how long the assets have been held), to reduce the impact on businesses if the rebasing approach is ultimately not accepted by the EU.

Views are sought on how disposal gains or losses should be computed.

Exemption or relief specific to disposal gains

The government proposes exploring with the EU the following relief measures:

- Disposal gains from traders – foreign-sourced disposal gains derived by a trader of an asset in relation to the asset as part of its income derived from substantial activities in Hong Kong (for example, gains from the sale of immovable properties by property developers) are to be carved out from the expanded FSIE regime; and
- Intra-group transfer relief – subject to certain anti-abuse measures, the taxation of foreign-sourced disposal gains from the transfer of assets between associated companies is to be deferred (i.e., no gain or loss arises upon the transfer for the transferor company and there is no step-up of the cost base of the asset transferred for the transferee company).

The transferor company and the transferee company are considered 'associated' if one is the beneficial owner of 75% or more of the issued share capital of the other, or a third company is the beneficial owner of 75% or more of the issued share capital of each of them.

Views are sought on the exemption or relief measures to be provided under the expanded FSIE regime.

For more details of other issues on which views are sought, other related issues being clarified in the consultation document and the implementation timeline, please refer to KPMG's publication here.

KPMG observations

Unlike the legislative exercise conducted in 2022 for introducing the FSIE regime, the government has taken a slightly different approach this time; i.e., launching a consultation to seek views on a number of outstanding issues before it continues to negotiate with the EU.

This revised approach is welcomed and KPMG will provide comments/suggestions on a number of issues for the government's consideration, including:

- The types of assets to be excluded;
- Justifications for the proposed rebasing approach;
- Other measures for reducing the impact of the new taxation of foreign-sourced disposal gains on businesses; and
- Better options than using 'issued share capital' to measure the degree of association for the purposes of intra-group asset transfer relief in light of the recent dispute in the *John Wiley* case (see KPMG's article here for more details of the case).

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The new Job Creation Law and tax relief for electric vehicles

'New' Job Creation Law

On December 30 2022, the Indonesian government issued Government Regulation in Lieu of Law Number 2 of 2022 (Perppu-2), as an amendment to the original Job Creation Law. The issuance of Perppu-2 is triggered by Constitutional Court Decision No. 91/PUU-XVIII/2020 which instructed the Government to amend Law No. 11 (the Job Creation Law). On March 31 2023, Perppu-2 was passed into Law No. 6 of 2023 (Law No. 6).

Law No. 6 replaces Law No. 11, and therefore it amends the tax laws most recently adjusted by the Law on Harmonization of Tax Regulations. There are no significant changes in the content of the taxation section.

This law became effective on March 31 2023.

VAT on the transfer of foreclosed assets

On April 11 2023, the Minister of Finance issued Regulation No. 41 of 2023 (PMK-41) regarding the transfer of foreclosed assets by creditors to collateral buyers. PMK-41 is the implementing regulation of Government Regulation No. 44 (GR-44). In GR-44, the transfer of foreclosed assets by a creditor to a buyer is considered delivery of rights to taxable goods under an agreement, and therefore is subject to VAT.

PMK-41 requires that the VAT is collected at a specific rate, i.e. 10% of the prevailing VAT rate, or an effective rate of 1.1%, on the transfer of foreclosed assets to a buyer. The VAT is collected when the creditor receives payment from the buyer.

Creditors that are firms subject to VAT are obliged to issue VAT invoices and report them in the monthly VAT returns. Input VAT on the acquisition of taxable goods and/or services related to the transfer of foreclosed assets cannot be credited by the creditor. On the other hand, buyers of foreclosed assets that are firms subject to VAT are allowed to credit the input VAT in accordance with the provisions of the tax laws and regulations.

This regulation became effective on May 1 2023.

Certificates of Origin

Minister of Finance Regulation No. 35 of 2023 (PMK-35) establishes several new provisions that facilitate the import of goods and services through cooperation between Indonesia and various other countries. These provisions were previously scattered across different laws and regulations. Once PMK-35 becomes effective, any procedural matters related to the submission of Certificates of Origin (COO) and/or Declarations of Origin (DAB) and the imposition of import duty tariffs on imported goods based on agreements or international accords must comply with this new regulation.

Among other things, PMK-35 reduces the timeline for submission of COOs and DABs from 30 days to one to five days.

This regulation became effective on April 28 2023.

VAT incentive for battery based electric vehicles

The Minister of Finance has issued Regulation No. 38 of 2023 (PMK-38) which provides VAT incentives for battery-based electric vehicles. Under PMK-38, a portion of the VAT due on the sale of specified four-wheeled vehicles and buses will be borne by the government. The period covered is from April to December 2023. Deliveries of battery-based electric vehicles can enjoy this benefit provided that the vehicles are newly registered and meet the domestic content requirement.

Any VAT that has is borne by the government must be repaid if the battery-based electric vehicle sold does not meet the requirements.

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Indonesia's hopes for pillar one

Septian Fachrizal, TP analyst at the Directorate General of Taxes, outlines how Indonesia is relying heavily on the successful implementation of pillar one.

Septian Fachrizal

Indonesia has been putting its faith in the OECD's pillar one as the preferred solution for taxing the digital economy in light of direct taxation.

As a country with a considerable number of internet users (224.01 million users in 2022, based on Statista data), Indonesia desires its piece of the cake. In essence, pillar one (under the Amount A rule) will reallocate the residual profits of large multinational enterprises (MNEs) to market jurisdictions where the businesses have no physical presence.

Earlier this year, Indonesia's director of international taxation, Mekar Satria Utama, was appointed as a member of the OECD Inclusive Framework (IF) steering group. This means that Indonesia's role in the OECD's plans on pillar one will be more noticeable, especially in setting the agenda and priorities for the project.

As part of the steering group, Indonesia will be involved in its regular meetings to discuss progress on the pillar one project, primarily working on the completion of the draft of the Multilateral Convention (MLC) in preparation for its signing in July 2023.

The steering group provides direction to the IF, especially on the open issues concerning the MLC draft taking into account the input of comments from the public consultation documents.

Shortly after the October Statement in 2021, Indonesia included a commitment to support pillar one in Article 32A of its newly amended Income Tax Law, Law No.7 Year 2021, concerning Harmonization of Tax Regulations (HPP). Further, in Government Regulation No.55 of 2022 (GR-55), several relevant provisions insinuate the optimism regarding pillar one implementation.

Under Article 49f and Article 52 of GR-55, the Directorate General of Taxes is authorised to implement provisions in bilateral and/or multilateral agreements in the field of taxation with tax authorities of partner jurisdictions to overcome challenges resulting from the digital economy.

Further, Article 53 of the regulation provides room for Indonesia to tax MNEs that meet certain criteria stipulated in the agreement, as they are considered to fulfil subjective and objective tax obligations in Indonesia.

> **"As a country with a considerable number of internet users... Indonesia desires its piece of the cake"**

Indonesia's support for pillar one implementation can also be seen in its 2022 G20 Presidency. Pursuant to the G20 Bali Leader's Declaration, November 15-16 2022, Indonesia and other G20 countries are committed to supporting the finalisation of pillar one by signing the MLC in the first half of 2023.

Global development to anticipate

At a press conference in Paris on February 20 2023, French economy and finance minister Bruno Le Maire claimed that not only the US but also India and Saudi Arabia are holding up pillar one implementation. He then pursued the European Commission to prepare to resurrect the Digital Services Tax (DST) as the tool to tax the digital economy if G20 countries failed to achieve agreement on pillar one.

In another event, on February 21, the former director of the OECD Center for Tax Policy and Administration, Pascal Saint Amans, participated in an interview conducted by PwC's news platform, Policy on Demand. After highlighting Le Maire's statement, he addressed the next fundamental question of whether the US would sign the MLC of pillar one, which requires a majority of 67 Senate votes for treaty ratification.

He is of the view that it is therefore very unlikely that the US will sign the MLC. It is worth noting that Pascal stepped down from his seat in the OECD at the end of October 2022 after 15 years at the organisation, leaving the pillar one work unfinished.

Previously France, along with Spain, Italy, Austria, Turkey, and the UK, decided to enact a DST in their national laws as a unilateral measure to tax the revenue of the digital economy money-maker MNEs. However, those DSTs triggered the US's concerns, leading to the US threatening to impose trade sanctions on the countries involved.

Those countries then, in October 2021, reached a political compromise with the US to fade out the DSTs once pillar one was fully implemented globally and to credit the money collected from the DSTs during the transition period against the Amount A of pillar one allocated.

The widespread introduction of DSTs forced the US to dip its toe in the pillar one ongoing global discussion – partial

Will Indonesia gain from pillar one?

involvement in pillar one was a means to stall the spread of DSTs around the globe.

However, the US Senate opposes pillar one on the basis that since most of the pillar one in-scope MNEs are US-headquartered, if implemented, pillar one will make the US relinquish much of its tax base to market jurisdictions.

It is an open secret that the US Senate is not in the same boat as the OECD with regard global tax deals. On February 10 2023, the US Senate sent a letter to the OECD secretary-general, Mathias Cormann, striking a hit against the OECD's efforts to address taxation of the digital economy.

The letter stated that the OECD had failed to ensure fairness in cross-border taxation for the digital economy. Instead, the global tax deal reflects a tenuous political negotiation that relies heavily on US concessions. As the country that provides 20% of the OECD's annual budget, the US is not certain to continue funding the organisation for a project that harms US interests.

Canada seems ready to take an alternative approach if pillar one fizzles out. It has proposed unilateral DST and legislation is pending in parliament, which, if passed, will enter into force on January 1 2024. In addition, the existing DSTs around the world would still be active, and countries like the UK, France, Austria and Italy could keep collecting the tax without the obligation to credit it against Amount A of pillar one allocated.

Despite all those issues, the OECD's Task Force on the Digital Economy, as mandated by the IF countries, is still finalising the details of Amount A of pillar one rules and seeks to conclude the text of the MLC by mid-July this year.

In the meantime, the first ministerial meeting of the 2023 G20 under India's Presidency, conducted on February 24 2023, maintains the stance from G20 Indonesia to endorse the swift implementation of pillar one.

Electronic transaction tax and the US investigation

In 2020, Indonesia introduced the Electronic Transaction Tax (ETT) as a unilateral measure aimed at addressing the challenge of taxing the digital economy in light of direct taxation through Government Regulation in Lieu of Law No. 1 Year 2020 (Perppu-1), which then was adopted as Law No.2/2020. ETT is a tax imposed on certain electronic transactions, specifically transactions involving electronic systems, applications and/or platforms.

Pursuant to Article 6, paragraph 12 of Perppu-1, the ETT shall be regulated by or based on a Government Regulation. However, up until now, the implementing regulation has yet to be either launched or formulated.

The US Trade Representatives (USTR) raised concerns about the ETT and recognised it to be an Indonesian version of a DST.

> “If pillar one reaches a global consensus, Indonesia will be entitled to additional tax revenues from giant MNEs”

On June 2 2020, the USTR launched an investigation of Indonesia regarding DSTs under Section 301 of the US Trade Act.

The USTR focused on various aspects of DSTs, including whether these taxes discriminate against US companies, are unreasonable as tax policy, or restrict US commerce.

The investigation report dated January 13 2021 pointed out that although implementing regulations had not been adopted, the ETT would raise several concerns if it were put into effect. First, as reported in the investigations on the DSTs of other countries, the USTR is concerned that an ETT would discriminate against US companies.

There is one interesting point to note: the USTR challenged the thresholds set on the DSTs of other countries as the ground to justify the discriminatory aspect of the DSTs.

On the other hand, it seems that the threshold set for the ETT would not reflect the discriminatory aspect in the USTR's view. However, the text of the ETT regulation may itself indicate the ETT is discriminative, because Article 6, paragraph 1 of Perppu-1 stipulates that the DST only applies to non-resident tax subjects.

Other USTR findings are that the ETT may be inconsistent with international tax principles and that it would create a greater burden on US commerce.

Legal constraints

Having a legal instrument that supports pillar one on the one hand and the legal basis of the ETT on the other seems to indicate that Indonesia has a backup plan if pillar one flunks. Is this true?

The answer is most likely no. There is a legal constraint to activate the ETT under the existing law – Perppu-1 – as Indonesia's plan B if pillar one fails. The Indonesian Constitutional Court has ruled that Perppu-1 will no longer be applicable once the pandemic status in Indonesia ends.

If Indonesia wishes to impose any other forms of the ETT, a new law will be needed. Pursuant to Article 23A of the Constitution of Indonesia (UUD 1945), taxes and other levies that are coercive for state needs are regulated by law. In the Indonesian hierarchy of law, that law is the second highest level after UUD 1945.

To enact a law, the bill needs to be included in the national legislation programme, unless it is proposed in response to public demand or emerging issues.

In fact, there is no bill concerning Indonesia's plan B in the national legislation programme 2020–2024, and proposing a bill that is not included in the programme may be more challenging, as it may not receive the same level of priority or support from government agencies and stakeholders.

Thus, it is reasonable to say that, currently, Indonesia does not have a backup plan for taxing the digital economy and this leaves the country with hope solely in the thriving global implementation of pillar one.

Concluding remarks

It will be interesting to watch the development of pillar one in the months ahead, to see whether or not its MLC comes into force by December this year. In Indonesia's situation, if pillar one reaches a global consensus, Indonesia will be entitled to additional tax revenues from giant MNEs.

On the contrary, if pillar one is no longer on the table, the new Article 32 of HPP and the relevant provisions of GR-55 may be obsolete accordingly, rendering them dead letter provisions unless the world comes up with another multilateral solution.

‘HMRC, catch me if you can!’

Charlotte Sallabank and Christy Wilson of Katten UK look at the Premier League’s use of ‘dual representation’ contracts for tax matters.


Charlotte Sallabank


Christy Wilson

The Premier League has recently come under criticism once again for aggressive tax avoidance, tending toward tax evasion in some people’s view. This time the use of ‘dual representation’ contracts has been criticised.

It is known that the Premier League often uses these contracts when an agent is involved. The basic framework of the dual representation contract is that the agent is paid half their fees by the club and half by the player.

The result of this split is that the club will pay half the fees plus VAT to the agent – the club can recover that VAT. The player will pay the other half of the agent’s fees plus VAT. If the player were to pay the full amount of the agent’s fees, the player would have to pay the entire VAT bill and would not be able to recover any VAT.

Additionally, the payment of the fees on behalf of the player is a benefit in kind — and so it is subject to income tax and national insurance contributions. If the club pays only half of the fees on behalf of the player, this reduces the income tax and national insurance liability of the club/player compared with what would be due if the club were to pay the entire amount on behalf of the player.

The issue with this contract structure is that it is hard to see how it is in keeping with the commercial reality of the situation. It is perhaps pushing the boundaries to say that an agent acts on behalf of both the club and the player. In truth, the agent works on behalf of the player to negotiate their contract and act in their interests.

In most commercial contexts it would be a direct conflict of interest if the agent were genuinely to act on behalf of both contracting parties as they have competing interests. The effect of this apparently contrary approach is that the contracts are drawn up to minimise the tax liabilities of the parties involved.

The ‘dual representation’ contracts of the Premier League constitute part of the wider conversation around tax avoidance. This topic is often covered in the press and regularly sparks strong responses. There seems to be a general feeling that tax is easy for big companies or rich individuals to avoid and that there are very few steps that HM Revenue and Customs (HMRC) can take to prevent such avoidance.

There is also a lot of misunderstanding around the topic, as legitimate tax-saving measures (such as loss relief) have been branded ‘tax avoidance’ measures by the press and even members of government.

One of the most ‘Googled’ questions that comes up when one is researching tax avoidance is ‘How can HMRC catch me?’ The answer to that question is that HMRC has lots of ways to catch you. Here are some of those ways:

- Spotlights – HMRC publishes information about certain schemes that it believes are being used to avoid paying tax. These Spotlights highlight different regimes (for example, remuneration trusts used to reduce profits and disguise income), explain why the regimes avoid tax and discourage people from using them – pointing out that they may be faced with litigation, penalties and/or interest on the unpaid tax.
- Disclosure of tax avoidance schemes (DOTAS) – This is a regime that provides

HMRC with information about potential tax avoidance arrangements at an earlier stage. The legislation applies to 'notifiable arrangements' that have as a main expected benefit the obtaining of a tax advantage that has any one of the 'hallmarks' (for example, if the promoter would like to keep confidential the way in which a tax advantage is secured).

- Follower notices – Follower notices are issued when HMRC is enquiring into the taxpayer's return or claim on the basis that the return or claim would result in a tax advantage and HMRC is of the opinion that there is a final judicial ruling that is relevant to the taxpayer's tax arrangements.
- Accelerated payment notices (APNs) – These are given by HMRC after a follower notice or DOTAS. APNs will state the amount of tax due as a result of the tax advantage being counteracted by HMRC.
- Notification of uncertain tax treatment – A taxpayer must notify HMRC if they have an uncertain tax treatment that has a tax advantage of more than £5 million and the taxpayer's turnover is at least £200 million and balance sheet total is at least £2 billion. A tax treatment is uncertain if it goes against HMRC's known position or if it deals with a new type or product or business structure where there are various ways it could be treated under current legislation.
- Disclosure regimes – there are many different disclosure regimes that are intended to gather information on taxpayers (and intermediaries) so that tax authorities (including HMRC) have the power to investigate whether tax avoidance arrangements may be in place.

Premier League clubs have come under criticism for dual contracts

- There are UK-specific disclosure regimes such as mandatory disclosure rules (MDR). These rules came into effect in April 2023 and follow on from the DAC6 measures that the UK had previously applied. A report to HMRC will be required where there is a cross-border arrangement for which it is reasonable to conclude that it is designed to circumvent the Common Reporting Standard (CRS). Equally, a report will be required where opaque offshore structures are used. The information collected by HMRC through the MDR will be shared with partner jurisdictions.
- There are also international measures such as the CRS (mentioned above) and the Foreign Account Tax Compliance Act (FATCA). The CRS is a global standard for the automatic exchange of financial account information between governments. This regime is similar to the FATCA, which requires foreign financial institutions (and certain other non-financial foreign entities) to report on the foreign assets held by their US account holders – or be subject to a withholding.
- BEPS 2.0 – This is a framework put together by the Organisation for Economic Co-operation and Development and involves two pillars. Pillar One deals with reallocating certain amounts of taxable income to market jurisdictions – this results in a change in effective tax rates. Pillar Two aims to ensure that income is taxed at an appropriate rate and includes a number of mechanisms to ensure this tax is paid.
- Specific tax avoidance legislation – most tax legislation will contain specific measures which prevent behaviours in respect of the relevant legislation that could result in tax avoidance.

Overall, there are many ways in which HMRC can obtain information in order to assess whether or not a taxpayer is participating in tax avoidance. The issue in the context of the Premier League is that if it is so well known that these tax avoidance regimes are taking place, why does HMRC let it happen?

It has been reported that the amount owed by the Premier League to HMRC could be about £420 million (the profits of the Premier League in 2022 were £479 million).

One approach that HMRC could take is to introduce sector-specific measures.

For example, the construction industry was known for participating in lots of 'cash-in-hand' jobs and not all the tax that was due was being passed to HMRC. As a result, the Construction Industry Scheme was introduced, which meant that contractors would deduct money from a subcontractor's payments and pass it to HMRC. These deductions counted as advance payments towards the subcontractor's tax and national insurance.

The frustration with tax avoidance lies in the fact that there are situations in which it is clear that tax avoidance is occurring but HMRC is not seen to be tackling the issue. Perhaps HMRC is working on the Premier League problem quietly in the background.

In fact, there was a recent case (Sports Invest UK v HMRC [2023]) in which the First-tier Tax Tribunal held that a payment by an Italian football club to a UK-based football agent for a player transfer related solely to services supplied to the club and was not partially third-party consideration for services supplied to the player — and as such it was not subject to UK VAT.

It is quite likely that this case will be appealed by HMRC. Going after well-known tax avoidance arrangements will send the signal that HMRC can, very probably, catch you.

Q&A

Ørsted's head of tax on the risks to renewables

Karl Berlin talks to Josh White about meeting the Fair Tax standard, the changing burden of country-by-country reporting, and how windfall taxes may hit renewable energy.

Josh White

Tax transparency is fundamental for multinational enterprises today. No business can afford to take its reputation for granted when it comes to tax.

Danish renewable energy company Ørsted, the world's biggest offshore wind farm developer, became one of the first international groups to be awarded the Fair Tax Mark outside the UK in December 2022.

The Fair Tax Mark was created by the UK-based Fair Tax Foundation to set a global standard for ethical tax practices.

Karl Berlin, vice president and head of tax at Ørsted in Copenhagen, tells *ITR* about what businesses can expect from greater tax transparency and international reform. He also comments on the risks of windfall taxes for green energy, and much more.

Before joining Ørsted in 2017, Berlin was head of tax at Maersk Drilling for five years. He has more than 16 years of experience working in tax and the energy sector. In his current role, he oversees tax management and strategy.

To what extent did you have to change some of your structures and practices to meet the Fair Tax standard?

Not at all. We had effectively started the process with our new tax policy in 2018 and we were applying it consistently and expanding our tax transparency. This policy included quite a lot of explanation of the application of our tax policy.

We started reporting aligned with the GRI207 [Global Reporting Initiative] in 2020 and we decided to get an ISRS 4400 statement for our stakeholders. All of this helped prepare us for the Fair Tax Mark.

Preparing for country-by-country reporting [CbCR] takes a lot of time. A lot of man hours went into setting up our CbCR. But once in place, it's a fairly automatic process which meant we were pretty much ready for the Fair Tax Mark when we decided to apply for accreditation.

We didn't have plans for the Fair Tax Mark when we started working with our approach to tax, but we did it because we thought it would help us with our work to support the company and work with policymakers to design a better tax framework for the green energy transformation.

Some multinational companies have gained greater understanding of their business models through the Fair Tax accreditation process. Was this the case for Ørsted?

Absolutely. The work on tax transparency has helped us as a tax team to better understand our company. When we describe why the tax cost is an effect of our business, we have to understand our business, the value drivers and the operating model of our company. We have to understand what we put out there.

We have to understand how our business works, and digging into policy work has helped us gain this understanding of our company. So, I think other tax departments would find it helpful to go through this process.

Ørsted is the world's biggest offshore wind farm developer

What do you make of the EU's plans to make public CbCR mandatory?

I know that some investors are asking for mandatory disclosures. This might be helpful, but I think a better strategy is investor pressure on public companies to adopt public CbCR.

Public CbCR in the EU will disclose what goes on in European jurisdictions, but you still wouldn't have the information from outside the EU on everything else going on. So, what are you going to use that information for?

It's a sustainability issue. Those kinds of initiatives will probably be more successful if there is a drive from within the company to become more transparent and there are requirements from stakeholders in and outside of the company. Then you will go into it with all the energy you can muster.

Another example would be the UK requiring companies to publicly disclose their tax strategy and, [for] most companies that do this, their tax strategy looks identical to every other report out there. They do it because it's a legal requirement and their hearts aren't really in it.

What's the business case for greater tax transparency?

Tax transparency helps investors and analysts to assess whether a company has control over their risks and opportunities. Reading a CbCR file can help investors spot things that look odd. It's a sanity check that 'yes, you're in control of this'.

When it comes to tax, it's not about paying more or less, but the right amount, and, at the end of the day, tax is a cost to the company to pay tax.

If you see tax as an operational expenditure [opex], it's probably one of the largest categories. So, it's interesting that a lot of companies do a lot of explaining around opex and FTE [full-time equivalent] costs, but then for tax they just have a black box.

It's about helping investors make more informed decisions, as well as greater accountability. Ultimately, it helps reduce risks for businesses and reduces unknown factors for investors. As for some tax risks, it can take them from 'unknown unknowns' and make them into 'known unknowns'.

For example, when we announced that we had been hit with a tax reassessment form the Danish authority in December 2020, financial analysts could assess our position and whether it would affect the outlook of the company.

The consensus among analysts was that they didn't see the reassessment as something that would negatively impact the future profitability of the company. We apply the 'more likely than not' principle when dealing with risks.

When applying judgement and estimates, there is of course a risk that you may be wrong, but being open and transparent about what kind of judgements and estimates you make, and how you arrive at them can enable investors and analysts to assess whether you've appropriately reflected your risks in your accounts.

What kind of unique tax challenges exist for a company like Ørsted?

The energy windfall taxes we see now is one unique tax challenge for our industry. We're in favour of the windfall taxes in general, but they have to be intelligently designed to target the windfall profits and not what might just be perceived as a windfall.

For example, many utilities have hedged their sales and volumes, which means that they might actually not be realising any windfall profits, so you have to look at the group as a whole over a longer period.

How have the windfall taxes affected your industry so far?

I think it is profoundly problematic that we all know we have to transition to renewables and, if you then add a windfall tax to renewables, what we have is a very well thought-through tax regime to promote investment in fossil fuels and not renewable energy.

There are all kinds of investment allowances for fossil fuels, which you don't have for the renewable sector. It's a new sector and it struggles from time to time. I think the stepmotherly treatment of renewable energy compared to fossil fuel energy is a profound problem.

Look at the industry as a whole – maybe we need a tax regime supporting the green transformation, just as we had for oil and gas when it was legislated in the 60s, 70s and 80s, promoting investment and growth. You still have that for fossil fuels to promote growth and investment, but not for renewables.

The levels of return on investments in oil and gas can look much better than investments in renewables, because of beneficial tax regimes, but also because the fossil fuel industry has been unable to externalise the cost connected with pollution. Taxing pollution and offering similarly well-thought through tax regimes for renewables would level the playing field and probably also turn the tables.

There is a real risk that renewable energy companies will end up paying more in tax than the oil and gas sector. It's difficult to say because of different accounting standards and the windfall taxes won't be factored into effective tax rates for us, but this may be the case in many countries.

Ørsted's annual report came out in February, showing the company reported strong operational profits in 2022. Is this due to an increase in the offshore wind energy market?

The large part of the underlying business work was doing very well, and we also had a divestment in 2022, which is a part of the reason for this strong profit rate.

The purpose of the tax department is partly to provide certainty to external and internal stakeholders. We are involved in all kinds of projects, including investments and divestments, to ensure we have optimised and robust tax structures which are reliable.

We work to apply the best-in-class tax reporting to ensure trust among the investor community, the analyst community and the civil society in which we operate. We are quite progressive and participate actively in the debate on international tax policy.

When we identify a legislative risk, we engage with policymakers early on to develop a better tax framework for the green transformation. The financial results in the report are not just down to our tax strategy, but our tax work is in effect a reflection of our business performance.

Despite us performing very well last year and very well this year, our hedging strategy has not been super successful. We've had unrealised losses on our hedges. These losses have gone into the Danish taxable income.

We ended both 2021 and 2022 with a tax loss in Denmark. So, we are not paying tax in Denmark because of a peculiarity in Danish tax law. It's not an ideal situation if you pair it with the restrictions on losses carried forward for future purposes.

You can carryforward losses, but you can only reduce future profits down to 40%. When prices change and we make gains on these hedges, we won't have made any money but there will be tax due on profits we never made. There are more tax restrictions for lossmaking companies now.

Why is Ørsted facing such a high tax burden in the UK?

We haven't paid much tax in the UK historically because we have had large capital allowance pools from our many large investments. But, as more parks become operational and have been up and running for a while, the tax depreciation caps have flipped.

We invested a lot of money in the UK, carried forward a lot of losses and we're now paying more and more tax. You can only reduce your future tax burden by 50% in the UK, if I'm not mistaken.

> **"One problem in the UK tax regime is differentiating between long-life assets and non-long-life assets"**

One problem in the UK tax regime is differentiating between long-life assets and non-long-life assets. We've got an 18% capital allowance for non-long-life assets and a 6% allowance for long-life assets. This is not working for our industry.

Because the industry was so young and immature, most wind farms were not expected to exceed 25 years, but this has changed. As technology has improved, most new wind farms are expected to last a long time – over 25 years.

This has a massive impact on the business case. The UK could do more on tax relief and capital allowances for renewables. It's time to take a look at capital allowances for wind farms.

What is your view of the Business in Europe: Framework for Income Taxation initiative?

It's too early to say. We're generally supportive of aligned international measures. A lot of non-aligned domestic initiatives would be an absolute nightmare to navigate. It would increase the risk of double or even triple taxation.

Greater alignment of international measures is a much better alternative. The 15% minimum corporate tax rate was bound to come in eventually.

Tax is not just a cost to the company, it's a part of the social contract. We are highly dependent on the societies where we operate. We have to accept that we help fund the societies that we depend upon.

I absolutely think the EU should follow the OECD approach on profit allocation rules. Both pillar one and pillar two will be quite complicated and entail a lot of administrative work, but this is much better than the alternative of different national measures.

If we take a UK example, when we first saw the diverted profits tax implemented and I was working for Maersk Drilling at the time: they were concerned that a lot of offshore drilling rigs were leasing to UK companies and extracting profits from the UK.

All of the rigs were owned in countries with tax treaties with the UK and all the arrangements were in line with the arm's-length principle. However, the UK was concerned a lot of profits ended up not being taxed in the UK.

The UK was not happy with this. A restriction on right of deduction on lease payments was imposed, but this created distortions in the tax regime. You can't get tax relief where you own the rigs or in the UK as a result.

Ørsted reported an increase in its tax equity contributions. This is mainly from production tax credits, is it not?

That's in the US, where we got the green tax credits for investment in renewables. It's a small, niche market. It's about investors with a tax appetite. Basically, they get a tax credit to offset their normal tax burden for investing in renewable energy.

It's working pretty well for us because we get access to a greater pool of funding and the investors get a tax credit. This actually predates the Inflation Reduction Act [which came into effect in August 2022], but the act has improved the US tax credit regime for renewable energy.

The US is leading the way right now on renewables, and other countries could do a lot more. There is more support for the green transformation now, but it's not enough.

Karl Berlin was speaking in a personal capacity and not on behalf of Ørsted in this interview.

Transparency principles for international tax reform

Richard Murphy and Andrew Baker make the case for tax transparency as a public good and how key principles should lead to a better tax system.

Richard Murphy

Andrew Baker

It is more than 25 years since the OECD and the EU Code of Conduct Group on Business Taxation Group started their combined assault on the international tax abuses perpetrated from what they described at the time as 'tax havens', and which are now more commonly known as 'secrecy jurisdictions'.

It is also more than 20 years since the tax justice movement began in late 2002. Since then there have been many matters on which significant advance has been made in the field of international tax, not least because of the cooperation between these quite different organisations and the cross-fertilisation between them. There is, however, one notable aspect to all those achievements, which is that they are almost exclusively within the international tax arena.

That focus on international tax abuse has been appropriate for much of the past 25 years. However, as further progress in this area runs into obstacles, some tax policy specialists have begun to consider whether the achievement of better tax management requires that attention be given to the domestic as well as the international tax agenda by the promotion of a more universal approach to tax transparency.

Tax transparency is defined as the disclosure and publication of quantitative and qualitative data about the tax system that a society needs to hold decision-makers to account and to reach informed judgements on how the tax system of a jurisdiction is performing.

Tax specialists believe this new focus on tax transparency enhances taxpayers' morale and their willingness to pay tax. Tax transparency does, therefore, increase tax revenue. It also strengthens the legitimacy of the tax system and the sense that the system is fair.

By promoting due process, tax transparency increases public trust in the tax system and enriches public debate on its performance. This would also help improve democracy in the country. As a result, it should enable public bodies and revenue authorities to perform their duties and functions better.

Tax spillovers

Our own engagement with this issue started with a reconsideration of the concept of tax spillovers, which is an approach to tax system appraisal first developed by the IMF in 2014.

The IMF's intention in undertaking its work was to deliver a better understanding of the ways in which the corporation tax system of one country might undermine the corporation tax systems of other countries. Its approach was endorsed by many civil society organisations at the time that it was first published.

However, this approach also ran into obstacles, not least because securing sufficient relevant and reliable data for use in the econometric models that the IMF used proved to be particularly problematic.

Some further studies of this type have taken place since 2014. None was particularly convincing because of problems in the data used. As a result, this avenue of research appeared to have closed until we proposed a different approach to it.

The approach that we took to tax spillover analysis as a means for delivering tax transparency was originally developed at the request of Oxfam, but it was later published as an independent academic study and it is different from the approach adopted by the IMF.

We suggested a new form of tax spillover analysis based on a qualitative as well as a quantitative explanation of why and how tax systems fail to achieve their objectives. As a result, we considered why some tax policies and procedures generated risks and often unintended consequences that undermined different tax bases, both domestically and internationally.

In doing so, we suggested that this approach had two advantages over that used by the IMF.

First, it captures many of the things missed by more quantitative approaches that are reliant on official data and established data sets.

Second, we felt this work would help with the appraisal of the source of risks and contradictions within tax systems, how policy decisions and procedures generated those risks and harms for other tax systems, and how those inconsistencies created internal risks that could undermine the overall functioning of the domestic tax system.

To undertake tax spillover assessments of this sort, we suggested that the collective experience and skills of tax professionals drawn from a variety of disciplines could be used to appraise the likelihood that one part of a jurisdiction's tax system might undermine the effectiveness of another part of that jurisdiction's tax system.

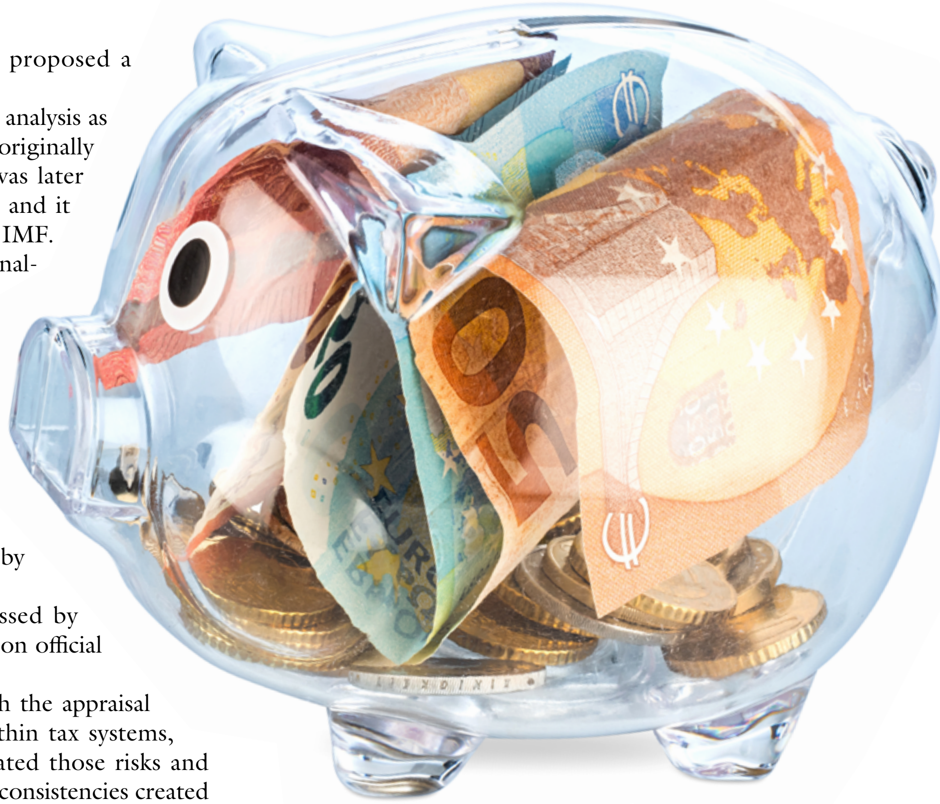
For example, such an approach could be used to appraise the risk that the capital gains tax system of a jurisdiction undermined its income tax system. In addition, those same people could be asked to appraise the likelihood that an aspect of the jurisdiction's tax system might be undermined by the tax system of another jurisdiction – or of course, that this process might work in reverse.

The system that we proposed was holistic. It was deliberately designed to view tax systems and the supporting mechanisms that underpinned a tax authority, its legitimacy, its opportunity to access data and its chance of cooperating internationally as a whole.

Our intention was deliberate. We wished to avoid the singular or silo approach to the consideration of tax abuse in a particular tax that has been a characteristic of much of the work that we had observed within regulatory organisations and within civil society when looking at tax abuse issues as they exist within and between jurisdictions.

We instead noted that those undertaking tax abuse were likely to use all the available opportunities to reduce their tax, in which case it was likely that they would work across the boundaries between tax systems and that they would exploit the administrative, record-keeping and other loopholes that a tax system might create that provide them with opportunity to abuse.

As a result, we developed a framework for appraising spillovers, which enjoyed some academic success and was supported by a wide range of tax justice NGOs. It was also noted by some international financial organisations.



Tax transparency may enable better corporate tax policy

GIFT and the public good

The consequence was that we were introduced by the World Bank to the Global Initiative for Financial Transparency (GIFT), of which they were one of the sponsors. Consequently, our work in this field has expanded quite considerably.

Using the holistic approach developed in our work on tax spillover analysis we developed our thinking in a 2021 paper published by GIFT entitled 'Making Tax Work'. This turned out to be a primer for the work that developed as a joint effort between us and the GIFT team, so that in August 2022 GIFT was able to publish what it calls its 'Transparency Principles for Tax Policy and Administration'.

These principles promote tax transparency as a public good in its own right. Importantly, the approach recognises that it will not be possible to properly appraise the risks within any tax administration, or between it and other tax systems, unless appropriate data is available. Providing that data is the ultimate goal of this work.

The standard suggests that this process should supply the information required to ensure that a tax system works for the benefit of all stakeholders of a tax system, including:

- Legislators, both in and out of government.
- Tax administrators and other government officials.
- Voters.
- Those who pay taxes.
- Those who are affected beyond the jurisdiction.

Specifically, it is suggested that the stakeholders of a tax system require the information that allows them to:

1) Understand how the tax that people have to pay is determined.

2) Understand the administrative procedures that prescribe how taxes are paid.
3) Assess whether the taxes people are expected to pay are fair compared with the contribution required of others within the society of which they are a part.
4) Determine whether all of those who should pay taxes actually do so.
5) Evaluate what alternative options for raising revenues exist.
6) Understand how the tax system compares with those of similar jurisdictions.
7) Know how the taxes that are collected are used by government.

Some aspects of this approach need to be highlighted. It is our suggestion, and that of GIFT, that to be transparent and accountable a tax system must include a statement of the key goals and objectives of the tax system and a statement of what the jurisdiction's policy and administrative frameworks are designed to achieve.

It is our contention that without these statements it is not possible to appraise the performance of the tax system – and yet details of these goals and objectives, and the assumptions and data that underpin them, are rarely made available.

Likewise, information on revenues raised is often incomplete or is not timely and is not made public with the level of detail needed to enable informed debate. This is most especially true when it comes to the comparison of outcomes and expectations, because without detailed budgets and performance targets the appraisal of issues such as tax gaps is very hard.

This situation undermines confidence in the tax system itself and in the tax administration, because the extent to which such failures are the result of underfunding – meaning the administration cannot collect all the tax owing – cannot be properly appraised.

Similarly, the cost of tax allowances and reliefs that reduce tax yields is generally either unavailable or less available than corresponding information on the expenditure side of the fiscal equation. This makes little sense if the fiscal process is to be properly managed.

It was to make good these deficiencies in a way that encourages higher standards of tax system management and appraisal that the GIFT principles were written. Their ultimate goal is to ensure that public resources are used to advance the public interest.

In that sense they seek to assist delivery of the goal of many international agencies working in this area and to advance the interests of those civil society organisations dedicated to tax justice.

Principles of tax transparency

The principles themselves are organised into groups that are described as basic, intermediate, advanced and aspirational as to their ambition.

> “This situation undermines confidence in the tax system itself and in the tax administration”

Basic principles have these objectives:

1) To reinforce stakeholder rights to participation in tax decision-making.
2) To require that governments should publish their objectives for the tax system, usually annually.
3) That these objectives be supported by timely and sufficiently detailed budget data by tax.
4) Taxes must be codified in law backed by an accountable legislative process.
5) Taxpayers must be able to access tax law and have an appeal process available to them if they think the law has been inappropriately applied.
6) All taxpayers must have a right to confidentiality with regard to their affairs unless specific circumstances require otherwise.

Intermediate principles build on these foundations and add that:

7) Governments must place tax policy within a broader fiscal, economic, and social framework.
8) Governments should publish a set of accounts disclosing taxes paid at least once a year, which should include prior year data and comparisons with budgets, with variances being explained.
9) Tax administrations should be accountable, with the mechanisms for that accountability being apparent.
10) Governments should collaborate with international and regional financial institutions and tax administrators to meet their international reporting obligations.

Advanced principles take the system further and require that:

11) Governments report which taxes that are legally owed go unpaid, as a first step in preparing a tax gap estimate.
12) Governments should publish information on the amount and beneficiaries of tax incentives such as reliefs, allowances and exemptions and justify their continued existence on a regular basis.
13) The data underpinning tax transparency should be subject to verification by an independent agency.

Finally, the aspirational principle of tax transparency is that:

14) Governments should use assessment tools such as tax gap analyses and tax spillover assessments to enhance their own and stakeholders' understandings of the risks and vulnerabilities within the tax system, and to inform potential reform debate.

As is apparent, the principles loop back to the tax gap and tax spillover analysis that has been a feature of much of our work in this area. There is good reason for that. Tax spillover assessment is about encouraging a reflective society-wide debate about how the tax system is performing and how that performance might be improved. That approach supports the tax transparency agenda in promoting dialogue on what the tax system is achieving and how it is doing so.

This should then suggest ways the tax system can be made more effective as an instrument of public, social and economic policy that can enable societies to better use tax to meet the challenges they face. This includes everything from securing a prosperous, inclusive future to reducing inequality and transitioning to a sustainable net-zero economy. We think this is why the principles need to be in widespread use.

EGYPT

Saleh, Barsoum & Abdel Aziz – Grant Thornton Egypt

Yasmine Hammad

Stay ahead of the curve: assessing and managing TP risk – part one

Following the work of the OECD/G20 Inclusive Framework on BEPS in actions 8–10, and Egypt's membership of the Inclusive Framework, the Egyptian tax authorities have dedicated much of their recent attention to building capacity in TP, resulting in an overhaul of the Egyptian TP regime and legislative framework.

The TP landscape in Egypt has changed quickly in the past few years and tremendous developments have taken place in the audit environment, including a noticeable change in the nature of TP inquiries and issues challenged by the tax authorities, mirroring the overall upskilling of TP capabilities.

Given the significant developments, TP risk assessment has gained more importance on the tax authorities' side, and has been the foundation of critical decisions pertaining to the commencement of tax and TP audits.

This article discusses the importance of TP risk assessments for companies, while part two addresses the key considerations to be aware of to be prepared for TP inquiries and audits from the tax authorities.

The pathways of a TP audit in Egypt

Typically, within the Egyptian Tax Authority, a TP audit could take place:

- As part of the corporate income tax audit; or
- On a standalone basis, regardless of whether the corporate income tax audit has commenced.

If undertaken as part of the corporate income tax audit, it is likely that the corporate income tax auditor will make the relevant enquiries following high-level risk assessment criteria. If certain risks are identified in that assessment, the auditor will refer the case to the TP unit, which will assess potential adjustments to be taken into consideration with the overall audit results.

Alternatively, in the latter case when a standalone TP audit takes place, it will always be the outcome of a detailed TP risk assessment process in which high TP risks are identified that require the commencement of a TP audit.

With the automation process currently happening at an Egyptian Tax Authority-wide level and encompassing all business processes, including submissions and audits, a risk assessment module has been built into the tax authority's systems, according to which, TP risk assessments will be conducted for file selection. The module will essentially consider risk assessment criteria similar to those currently looked into ahead of audits.

The weight of TP risk assessment from the tax authorities' perspective

From a tax authority's perspective, a thorough TP audit can require the dedication of considerable resources, which in many cases are seen as scarce due to the limited number of specialised TP auditors. The audit process typically involves the review of large amounts of information, which in most cases will require the full attention of a number of auditors, conducting a number of meetings, the review of numerous documents and records, site visits if relevant, the analysis of financial and economic data, research and review of benchmarking information in databases, a serious effort to understand the taxpayer's business and how that business generates profit, and discussion and negotiation with the taxpayer.

In short, commencing a thorough TP audit is a serious commitment for a tax administration. Accordingly, TP risk assessments are highly rated by tax authorities to ensure resources are being efficiently utilised.

Risk assessment criteria: TP risks typically looked into by the tax authorities

TP risk generally arises from one of the following factors;

- Risk arising from recurring transactions;
- Large or complex one-off transactions;
- Data revealed from country-by-country (CbC) reports – this is particularly relevant to Egyptian-parented groups as their CbC reports are readily accessible to the tax authorities, with no need for exchange of information; or
- A company's behaviours towards governance, and its ability to adhere to the compliance requirements.

The above broad factors translate to a number of specific practical risks, such as the following:

- Significant or increasing transactions involving payments to related parties in low-tax jurisdictions or tax havens, which, from a tax authority's perspective, may suggest a risk of transfer mispricing.
- Material transactions constituting a large portion of the company's revenues or costs, depending on the nature of the transaction. Examples include companies selling huge volumes of products or services to related parties that contribute a significant portion of the company's total revenues.
- Profitability trends – the level of profitability of a company could be compared to industry norms or comparable companies by the tax authorities. Where CbC reports are accessible, the profitability of local entities as opposed to wider group performance may be assessed. When a large deviation is found, this may be a strong indicator of a high TP risk. Likewise, an inconsistent profitability trend and/or consistent losses over a number of years raises another risk flag.
- Excessive debt that exceeds the amount which a company could borrow if it were an independent entity, or excessive interest expenses may be an indicator of a TP risk. Excessive interest payments to non-residents are of particular concern for many countries.
- TP policies involving significant year-end adjustments, particularly those involving true-down adjustments at a local entity level.
- Business restructurings, as these may involve internal reallocation of functions, assets or risks among the group. Transactions resulting from restructurings, such as transfers of intangibles to related parties, and the associated TP implications are typically prioritised by tax authorities, as these arrangements will typically have consequences for years to come.
- Development, enhancement, maintenance, protection, and exploitation (DEMPE) functions-related risks, such as the case of a resident entity owning intangible property but attracting a low or no royalty, or the presence of arrangements involving payments for intangibles.
- The quality of the contemporaneous TP documentation, and here two factors should be considered:
  i) The quality of the business's processes and documentation; and
  ii) The commercial outcomes of related-party dealings.

For example, a business that is consistently in a loss-making position and has a low quality of documentation is at the highest risk of a TP audit.

The documentation package essentially encompasses corporate tax return disclosures, master file and local file documentation, and the CbC reporting package (where applicable), together with supporting documentation such as related-party agreements. Specifically, the lack of related-party agreements or the misalignment of those with the actual conduct of the transaction, and the overall documentation flow, is another risk area.

See below for part two, which explains the key considerations for companies, and how TP healthchecks can help companies to mitigate risk.

Stay ahead of the curve: assessing and managing TP risk – part two

As indicated in the previous article, TP sometimes becomes burdensome for companies, particularly those with huge related-party volumes, or those new to the TP process and life cycle as a whole. More often than not, assessing your TP overall practices and potential risks is a necessary exercise, rather than a nice-to-do one, to be able to anticipate those issues that may trigger an audit and accordingly prepare for potential enquiries/challenges from the authorities.

Key considerations for companies

Companies are therefore advised to run a TP healthcheck to consider:

- Whether your related-party transactions are priced at arm's length;
- Whether arm's-length policies are in place but not being correctly implemented, leading to transfer mispricing;
- Whether any of the TP risks described in the first article in this series apply to your related-party dealings and any required actions; and
- An assessment of the quality of your entire documentation process.

The outcome of this exercise will help you to determine whether your TP policies and practices should be revisited or improved to avoid the likelihood of a TP adjustment if the company is under audit.

TP healthchecks: how can you assess and potentially mitigate your TP risks?

TP healthchecks are an effective tool for companies to manage TP controversy, whether before or during audits.

Managing TP controversy during audits

It is often the case that companies consider performing this exercise, in the form of an audit package assessment, when they receive enquiries from the tax authority, or when their file is officially selected for a TP audit. The exercise helps companies to understand their overall compliance/risk position and the likelihood to conclude an audit with clean versus adjusted results.

Yet, by that time, it is most likely the case that for certain issues, potential corrective actions identified as a result of the assessment cannot be performed due to timing, or documents already submitted to the tax authority.

Managing TP controversy before audits

In light of the increased scrutiny from the tax authorities in the field of TP, some companies run TP healthchecks ahead of any enquiries from the tax authorities, and companies are strongly recommended to run a TP healthcheck if they have not done so recently. The healthcheck should assess potential risk areas that may give rise to an adjustment in the event of an audit, and ensure a proper risk mitigation plan is in place to ultimately be prepared as and when an audit occurs.

This, in a way, could serve as a dispute prevention mechanism by proactive planning and preparation to minimise disputes, documenting and preparing evidence and defence files, and developing strategic controversy-aware TP policies.

While TP is fact- and circumstance-based, and associated operations/transactions vary widely in many forms and at many levels, an in-company TP healthcheck generally follows a common structure, typically run with the help of your TP adviser, and involves the following steps:

- Collecting quantitative data from various resources, including corporate tax returns, statutory financial statements, and company reports;
- Identifying risk factors by analysing the collected quantitative data;
- Where needed, reviewing and assessing the existing TP supporting documentation, primarily encompassing documentation reports, and related-party agreements;
- Assessing alignment of TP policies with the arm's length principle, and whether those are correctly implemented;
- Reviewing qualitative information and gathering additional information from public resources;
- Review and detailed quantification of potential risks;
- Assigning a risk rating per identified risk category and proposing a risk mitigation strategy/potential corrective action, as needed, such as a change in TP policies and calculating tax provisions; and
- Developing an action plan for risk mitigation.

Key takeaways

The TP landscape in Egypt is fast evolving, and is largely aligned with the global standards and how other countries within a group would be required to conduct their TP. Companies therefore need to monitor those developments closely to ensure the implementation of sound TP practices and reduce the likelihood of TP scrutiny from the tax authorities.

Egypt has dramatically modified its legislative framework and audit practice, including developing a TP audit process that starts from a thorough risk assessment upon which critical audit decisions are based. With such capabilities, companies in Egypt are advised to take their compliance seriously and assess their overall TP positions.

It is therefore crucial that companies take a step back and consider whether their related-party transactions are priced at arm's length, review and analyse those transactions, and consider whether changes are required to existing TP policies, to assess if pricing is expected to give rise to adjustments in the event of an audit.

It is suggested that companies start looking at the processes and documentation that already exist to review their risk factors, think about risk mitigation strategies and/or potential corrective actions, and develop a suitable action plan for their business. They should look at resource levels in each area, and existing and needed processes.

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From BEPS to ESG: how the role of country-by-country reports has been revamped

Several years after the introduction of the reporting model known as the 'country-by-country report' (CbCR), its function and role have evolved, particularly in the European framework.

The reporting model initially responded to the purpose of the OECD/G20 BEPS project as a tool available to tax administrations for tax risk assessment in respect of multinational enterprise (MNE) groups. It has since become an element for increasing the transparency of MNE groups, also affecting their reputation.

The OECD's BEPS project

The CbCR originated as part of the BEPS project. The Action 13: 2015 Final Report provided rules concerning TP documentation and a set of disclosure standards for MNE groups to improve tax transparency as part of the minimum standards of the action plan that all countries adhering to the BEPS Inclusive Framework (IF) are required to adopt in their domestic legislation.

The rules contain an obligation for the ultimate parent entity (UPE) of MNE groups with annual consolidated group revenue equal to or exceeding €750 million (approximately $821 million) to provide annually, in a common template, aggregating information to be submitted to a relevant tax authority. Information is then exchanged between tax authorities.

The CbCR should be used appropriately by tax administrations for high-level TP risk assessment purposes and in evaluating other BEPS-related risks.

Focusing on the content of the CbCR, the model comprises three tables.

In Table 1, the UPE should include all the tax jurisdictions in which constituent entities (CEs) of the MNE group are resident for tax purposes and report revenues split between related and unrelated parties, profit (loss) before income tax, income taxes paid and accrued, stated capital, accumulated earnings, number of employees, and tangible assets.

In Table 2, the UPE shall indicate every CE by tax jurisdictions and flag their main business activities.

In Table 3, the MNE group can include any further information considered necessary or that would facilitate the understanding of the information provided in the other tables.

The last passage of the BEPS project related to CbCRs is within the pillar two model rules (the GloBE Rules). The GloBE Rules also provide for the possibility of safe harbours to reduce administrative burdens, where specific operations of MNE groups are considered to be taxable above the minimum rate.

On December 20 2022, the OECD released guidance on safe harbours and penalty relief.

Among others, the BEPS IF has agreed on the design of a Transitional CbCR Safe Harbour as a short-term measure that would exclude MNE groups' operations in lower-risk jurisdictions from the scope of GloBE in the initial years.

The Transitional CbCR Safe Harbour is based on CbCR data for calculating MNE groups' revenue and income on a jurisdictional basis. The GloBE Rules and the rules for CbCRs have a similar scope, and there are similar rules for identifying CEs and allocating income to a jurisdiction under a CbCR and the GloBE Rules. The CbCR is a proxy for excluding the low-risk jurisdictions from the compliance requirements of the GloBE Rules.

The Transitional CbCR Safe Harbour uses the CbCR as a risk assessment tool to establish whether a top-up tax liability results under the GloBE Rules. This use of the CbCR is deemed to be consistent with the Action 13: 2015 Final Report.

The EU directives

Within the EU, Directive (EU) 2016/881 (DAC 4) extended the scope of the mandatory exchange of information by including the automatic exchange of information on the CbCR for MNE groups with total consolidated revenue equal to or higher than €750 million. The rules are in line with the OECD standards.

According to Directive (EU) 2021/2101 (the Public Country-by-Country Reporting Directive), MNE groups with consolidated revenue over €750 million will be required to disclose CbC data for their operations in member states (MS). In addition, they would be asked to disclose how much tax they pay on the business they conduct outside the EU. Publication will be required for the first financial year starting on or after June 22 2024. MS shall adopt domestic provisions by June 22 2023.

The directive was introduced to achieve a higher level of transparency and ensure public scrutiny of corporate income tax information by enabling citizens to assess the contribution of MNE groups to the welfare of society in each member state by taxes paid.

Public reporting does not satisfy the same purpose as information sharing between tax authorities. In terms of content, the information to be reported to the public is less detailed than the information to be submitted confidentially to tax authorities (exclusion of a split of revenue between a third party and a related party, stated capital and tangible assets).

ESG reporting: GRI 207

Public transparency on tax is also an important part of companies' corporate social responsibility.

Tax-related ESG reporting has been increasingly introduced in many countries.

The Global Reporting Initiative (GRI) is one of the international organisations that produce voluntary sustainability standards. Its standards are widely accepted as good practice for reporting on ESG topics.

In 2019, the GRI also released a tax standard, GRI 207: Tax. One of the requirements of the new standard is CbC reporting (Disclosure 207-4). This standard can be used by any company, regardless of size, to report information about its tax-related impacts on the economy, the environment, and people if it has determined tax to be a material topic.

The standard is applicable for reports published from January 1 2021.

In terms of content, the information to be disclosed is the same as the Action 13: 2015 Final Report, except for stated capital and accumulated earnings.

Companies should also report additional information for each tax jurisdiction (for example, total employee remuneration, taxes collected from customers on behalf of a tax authority, industry-related and other taxes or payments to governments, significant uncertain tax positions).

Based on the above, it is clear that the purposes indicated by the rules of CbC reporting over time have fostered the rise of its new functions, both in terms of tax liability (BEPS) and as a measure of the impacts of MNE groups' tax practices on society (ESG metrics).

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ITALY

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Investing in Italy: opportunity of applying advance investment rulings

The Italian tax revenue agency provided further clarifications on the advance tax ruling on new investments (ATRNI) with Circular No. 7 of March 28, 2023.

Here's a summary of the applicable law on new investments:

- The ATRNI enables resident and non-resident investors, willing to realise long-lasting and relevant investments in Italy, to obtain a preventive opinion from the Italian Revenue Agency regarding the tax treatment applicable to business plans and related extraordinary operations.
- The ATRNI was introduced in Italy with Article 2 of Legislative Decree No. 147/2015 (the so-called "Internationalization Decree"). It is addressed to the Revenue Agency and prepared by investors who intend to make major investments in Italy, worth above €15 million, with significant and lasting employment effects.
- The ATRNI's main goal is to give more certainty to economic operators in determining fiscal burdens connected to Italian investments, and to reduce tax uncertainty in the planning of foreign investments.

With the issuance of Circular No. 7

of March 28, 2023, the Italian Revenue Agency provided further clarifications on the subject matter:

- The definition of relevant investment: it should encompass any project for the realisation of an economic initiative having a lasting nature. Activities aimed at restructuring a company in crisis, optimising, or improving the efficiency of an existing business structure, or the participation in the assets of a company must be considered included. This is provided that the eligibility requirements to access the procedure are met. The value of the investment must not be less than €15 million.
- Regarding investments consisting of acquisitions of assets or participations, if the acquisition refers to a foreign entity, the "link with the Italian territory" requirement can be met by the investor being located in Italy. It is always necessary to quantify the value of the investment through the data of the resident buyer's balance sheet, and verify the employment-related impact and the positive economic effects on revenue in Italy.
- For asset or share deals that are not acquisitions of assets or participation in the assets of resident companies, or that do not imply the existence of a permanent establishment in Italy: any economic initiative that is capable of determining the inflow of financial resources into Italy and, in any case, capital, is considered relevant. For example: operations of "re-entry" of activities previously located abroad or the return of the same subjects, or the transfer to Italy of the tax residence of foreign subjects.

Furthermore, among the various topics covered, the Circular No. 7 provides significant clarifications on the so called "preemptiveness" of the ruling application. It includes an in-depth discussion on the deemed permanent establishment of a non-resident entity in Italy. The Italian Revenue Agency emphasises that having already started the execution of the business plan is not preclusive to the submission of the ruling's application. However, the ordinary deadlines for filing the declaration related to the tax period in which the investment plan started shall not have expired. In fact, a filed application is only considered 'prior to the expiry date' prior to the ordinary deadline for filing the first return related to the tax period in which the deemed permanent establishment to be assessed occurs.

Particularly interesting are cases in which the foreign entity carries out a pre-existing activity in Italy (with reference to the date of submission of the application for a ruling aimed at assessing the existence of its permanent establishment in Italy). In essence:

- A new investment plan whose object can be considered related, in several respects, to the pre-existing activity;
- An investment plan subject to so-called 'progressive implementation', the preliminary stages of which, prior to the start of the actual business, have already been completed; and
- An amendment of a pre-existing business.

In such cases, for the purpose of assessing the preemptiveness of the application, we may consider only 'new' facts and circumstances compared to the situation in previous tax periods.

If an investment plan is subject to a progressive implementation (activities related to the start of the enterprise's own activity), the element of novelty regarding the existence of the permanent establishment must be assessed based on the main activity carried out. This takes into consideration the clarifications provided by the Commentary to the OECD Model Convention. The application cannot be considered preventive in those cases in which the foreign company, which is already operating in Italy, carries out its activity in continuity with the past. For example, when there are changes in existing contracts that are irrelevant because they are not significant to the presence of the foreign entity in the territory of the state (e.g., contract extensions or assignment of new orders for activities already carried out, in identical ways, in previous tax periods).

The Circular also offers clarity on the interaction of the new investment policy with the prior agreement procedures (for example, Art. 31-ter Presidential Decree 600/1973).

Priority (in processing the application) will be granted to those taxpayers:

- Who file an application for an investment ruling on new investments; and
- Who, for the same business plan, also intend to enter into an advance pricing agreement (pursuant to Article 31-ter of Presidential Decree No. 600/1973) to define relevant matters, like TP.

Considering the recent clarifications from the Italian Revenue Agency sheds light on some of the long-lasting uncertainties about the ATRNI, an increase in submitting rulings to secure the applicable tax treatment on new investments in Italy is expected.

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LUXEMBOURG

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Accounting for crypto assets in Luxembourg: a guide

The recent turbulence in the US banking system has presented yet another opportunity for the crypto market. Despite this challenging environment, the financial industry has seen a growing interest in this asset class. Major banks are forming specialised groups dedicated to blockchain technology and cryptocurrency, while institutional investors – particularly those focused on alternative funds – find the efficiency of fund tokenisation attractive.

In the EU and in Luxembourg in particular, there have been new developments in the crypto asset world. The Commission de Surveillance du Secteur Financier updated its FAQ Virtual Assets–Undertakings for collective investment on April 6 2023. Essentially, the FAQ states that Luxembourg alternative investment fund managers investing in virtual assets through one or several target funds are not required to apply for an "Other-Other Fund-Virtual assets" licence. At the EU level, there should be progress following the EU Central Bank's decision to launch the implementation phase of its central bank digital currency project in Q3 2023.

Crypto assets are increasingly prevalent and the trend is likely to persist. However, this new asset class raises an important question: how should crypto assets be accounted for under the Luxembourg GAAP?

Currently, there is no specific Luxembourg guidance or regulation for the accounting treatment of crypto assets. It is thus difficult to anticipate what might be an acceptable accounting treatment under Luxembourg GAAP.

However, we can draw examples from France and international standards such as the IFRS. In 2019, the Autorité des normes comptables (ANC) in France issued guidance (under French GAAP) on the accounting treatment of cryptocurrencies, while the IFRS committee also provided guidance on the topic.

Below are examples of different classifications that might apply to crypto assets.

Intangible asset

Most crypto assets could fit into the definition of intangible assets found in IAS 38. This approach was validated by the IFRS committee with respect to cryptocurrency on the grounds that:

- It is capable of being separated from the holder and sold or transferred individually; and
- It does not give the holder the right to receive a fixed or determinable number of units of currency.

This could, in principle, apply to all crypto assets held for long-term investment purposes, and specifically to those for which IAS 2 does not apply (see inventory below). Moreover, under French GAAP, the ANC validated this approach (although not for all crypto assets) with the possibility of amortising and/or depreciating the assets.

Inventory

If an entity (broker-dealer) intends to sell crypto assets in the regular course of business, or for resale in the near future, they can apply IAS 2 to treat the crypto assets as inventory. This approach was validated by the IFRS committee as well.

Cash or cash equivalent

Crypto assets like bitcoin and stable coins are increasingly used as a medium for the exchange of goods and services. El Salvador became the first country to make bitcoin legal tender in September 2021, offering financial incentives to those who use cryptocurrency for payment. Major companies are following suit, with brands like Balenciaga and Gucci, under the Kering group, accepting crypto payments. The partnership between Shopify and crypto.com allows merchants to accept payments in up to 20 different coins. More restaurants also are accepting such payments, including popular chains like Subway, Starbucks, and Taco Bell.

However, even if some cryptocurrencies can be used as a means for exchanging goods or services, the IFRS commmittee concluded that cryptocurrencies are not cash (or a cash equivalent). This was because they do not have the characteristics of cash as described in paragraph AG3 of IAS 32.

Closing thoughts

As the prominence of crypto assets grows, the industry would benefit from guidance on the accounting treatment of such assets. Players in this space will need to exercise professional judgment and expertise, not just for accounting but also for tax and legal purposes. This is fundamental for those wishing to capitalise on the potential opportunities and navigate current and future challenges in this evolving landscape.

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NORWAY

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Withholding tax on dividends from Norwegian companies to Irish common contractual funds

On February 15 2023, the Norwegian Tax Appeal Board repealed the decision to refuse a refund of withholding tax to an Irish common contractual fund (CCF).

The Tax Appeal Board disregarded a previous statement from the Ministry of Finance that Irish CCFs were regarded as tax transparent for Norwegian tax purposes and instead found that the Irish CCF was comparable to a Norwegian entity covered by the Norwegian participation exemption method. The taxpayer was therefore entitled to a refund.

The Tax Appeal Board reiterated – in accordance with the Supreme Court judgment in the case of *Statoil Holding* (Rt. 2012 p. 1380) – that it is the Norwegian classification of the fund that is important when determining whether it is comparable to a Norwegian entity, not its classification in Ireland.

Considering *Statoil Holding* and more recent practice, the Tax Appeal Board observed that the statement from the Ministry of Finance emphasised factors that seemed to be of less importance for the comparability assessment today. Thus, it reached a different conclusion.

Background

A CCF is an unincorporated body established by an Irish management company pursuant to which investors participate and share in the underlying investments of the CCF.

The fund can be established as an undertaking for collective investment in transferable securities (UCITS) pursuant to the Irish European Communities Regulations 2011, or as an alternative investment fund. In this case, the fund was established as a UCITS, and organised as an open-ended co-ownership.

The sub-funds received NOK 855,221 (approximately $80,000) in dividends from Norwegian public limited companies and were subject to a withholding tax rate of 25%, which corresponded to NOK 213,805. The sub-funds applied for a refund of the full amount under the Norwegian participation exemption method, which was denied by the Norwegian tax office, because it viewed the fund as being tax transparent for Norwegian tax purposes and therefore not entitled to a refund.

The decision was appealed and later repealed by the Norwegian Tax Appeal Board.

The Norwegian participation exemption method

As a starting point, dividends paid to foreign shareholders are subject to withholding tax at 25%. However, the dividends are exempt from withholding tax under the Norwegian participation exemption method if certain requirements are met.

In order for the dividends to be exempt from withholding tax, the fund must:

- Be comparable to a Norwegian entity entitled to the Norwegian participation exemption;
- Be tax resident in a European Economic Area (EEA) country; and
- Be regarded as genuinely established and conducting real economic activity (the substance test).

There must also be an agreement enabling the request of information between the state of residency and Norway.

Assessments by the Tax Appeal Board

The Norwegian Ministry of Finance has previously stated that Irish CCFs should be treated as tax transparent for Norwegian tax purposes (UTV-2007-1858). The tax office felt bound by this statement. Consequently, the CCF was not regarded as comparable to a Norwegian entity covered by the participation exemption method.

The Tax Appeal Board, however, considered *Statoil Holding* and more recent practice. As a starting point, the classification of whether the fund is regarded as a separate taxpayer (meeting the comparable test) or tax transparent is carried out in accordance with Norwegian law. Key factors in the assessment are the liability structure, decision-making authority, and the investors' rights and obligations in the fund. Against this background, the Tax Appeal Board carried out a detailed analysis of how the CCF was structured.

It was found that investors in Norwegian mutual funds (covered by the Norwegian participation exemption method) and Irish CCFs have limited liability for the fund's obligations (limited to the invested amount), an argument that was considered decisive in the *Statoil Holding* judgment. Accordingly, the Tax Appeal Board concluded that the Irish CCF was comparable to a Norwegian entity covered by the participation exemption method.

With regard to the requirement of being tax resident in an EEA country, a CCF can be characterised as a hybrid fund, a separate taxpayer in Norway, but transparent for tax purposes in Ireland. The tax resident requirement does, as a starting point, refer to the domestic law of the other state, which creates challenges for hybrids that are not resident pursuant to the tax rules in the other state (i.e., tax transparent).

Previously, these were considered not to be covered by the participation exemption method, but this has been moderated as a result of *Statoil Holding* and more recent practice. In a Ministry of Finance statement from 2015 (UTV-2015-721), it was considered sufficient that the hybrid is established in accordance with company law in the EEA state. The CCF therefore also fulfilled this requirement.

The connection to an EEA country was considered evident through the management company, which was carrying out the investment activity and acted on behalf of the fund. The management fund and custodian were based in Ireland. Accordingly, the Norwegian Tax Appeal Board concluded that the fund was considered tax resident in an EEA country.

Lastly, the CCF was found to fulfil the substance test. Formerly, the requirement was interpreted strictly under Norwegian tax law, as a result of a statement in the preparatory works to the Norwegian Tax Act which created uncertainties with regard to whether foreign funds could be considered genuinely established.

However, a statement from the Ministry of Finance and subsequent administrative practice have indicated that it is sufficient that the management company of the investment fund meets the substance requirement on behalf of the fund, which is in line with interpretations from the European Court of Justice.

Therefore, the Norwegian Tax Appeal Board concluded that the fund had sufficient substance through the management company, which was genuinely established and conducted real economic activities on behalf of the fund in Ireland.

Consequences

All the requirements for applying the Norwegian participation exemption method were fulfilled, meaning that the dividends should have been exempt from withholding tax. The taxpayer was therefore entitled to a refund of the full amount.

Besides clarifying that Irish CCFs should be entitled to the Norwegian participation exemption method if meeting the above criteria, the decision also indicates that some older legal sources (regarding the participation exemption method) should no longer be given weight.

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POLAND

MDDP


Magdalena Marciniak and Marta Klepacz

Benchmarking studies – do Polish tax authorities accept group analysis?

Benchmarking studies are a well-known topic in most tax jurisdictions. Just like anything else in life, there is no common understanding of how it should ultimately look.

One cannot ignore differences between individual legal regimes where various security instruments are applied on the basis of TP.

These differences may become problematic when compiling a 'universal analysis' that will meet the legal requirements of each country.

When in Rome, do as the Romans do. When in Poland...

An example: in Poland, a benchmarking study is a mandatory element of a local file for all transactions subject to statutory TP obligations. This is the first and main difference between Polish regulations and most other jurisdictions. Therefore, even if benchmarks are prepared at the group level, they will likely only cover the main (and not all) transactions.

Another important aspect is when international capital groups prepare top-down and then share a universal benchmarking study with all subsidiaries. Their aim is to unify the TP policy in a given group, but also to reduce expenses incurred by individual entities (a single top-down analysis is prepared instead of several). Polish taxpayers often receive benchmarking studies from the group.

So, can they be used safely? How do Polish tax authorities approach the matter?

Keep calm and protect yourself

If an entity decides to use a group-prepared benchmarking study, it should be familiar with its specifics, identify possible threats and pay special attention to address them.

First, these documents are far more general than those that are developed individually for specific transactions between specific entities. In addition, the selected comparability criteria are often not adapted to the characteristics of a transaction featuring a Polish entity.

Requirements are also imposed by Polish tax authorities. One of the assumptions is that the benchmarking study strategy must consider the Polish market. Often, when a transaction is related to revenues of a Polish entity, e.g., a service provider, the authorities want to verify the local market.

The authorities are also eager to scrutinise the universal analysis that covers several or a dozen types of transactions where a similar number of entities is involved that are often based in different countries.

Moreover, Polish regulations clearly specify the elements to be included in the benchmarking studies report. Check carefully whether the group analysis contains all of them.

It is perfectly understandable that a capital group has a global perspective on such problems and wants its services or products to be used as comprehensively as possible. However, the fact is that economic conditions in the country where the entity operates are crucial for achieving the most adequate financial data. So, preparing global benchmarks for domestic operations involves a certain risk (an excellent example may be the inflation differences between individual countries, even in the EU itself where inflation reaches 20% in Poland, and only a few percent in other countries). Therefore, a single analysis cannot justify the profitability of entities operating in two different economic realities.

In turn, when inspecting business entities regarding TP, Polish tax authorities focus mainly on benchmarking studies and the results that have been established.

Need of reporting

Finally, taxpayers must be aware that benchmarking studies in Poland also serve as the basis for completing the TPR form. It is used to report information such as:

- Applied criteria;
- Results from the benchmarking study;
- Level of profitability or other indicators achieved in the tested transaction; and
- Applied statistical measures – experience shows that group studies often feature ranges calculated with the use of different statistical measures and it is not clear which one is recognised as 'arm's length'.

To sum up, group benchmarking studies are naturally acceptable, but taxpayers must not ignore the specificity of Polish regulations. They must also be aware that the benchmarking studies are among documents the most frequently challenged during tax audits. Additional explanations may be necessary, for which taxpayers should be well prepared in advance.

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ROMANIA

EY Romania


Andra Cașu and Teona Braia

A revamped R&D tax incentive framework for 2023

In the EU, the past 10 years brought an increased offering of R&D tax incentives for taxpayers, especially since the Council of Ministers set the 'Barcelona Goal' of spending 3% of European GDP on R&D and innovation. This target was reaffirmed in 2020 by the Council via its new European Research Area conclusions. Thus, many EU countries further incentivised business investments in R&D, intending to foster innovation by introducing and upgrading their tax incentives legislation.

Moreover, considering the current economic context with high inflation rates and governments seeking to reinvigorate economies after the pandemic, countries needed to revamp their R&D incentives. This is also the case for Romania, where at the end of 2022, the national tax authorities brought certain amendments to the R&D specific legislation.

R&D tax incentives in Romania

The R&D tax incentive framework is not new, as it was introduced via Romanian tax legislation in 2010. However it went through several amendments up until 2022, and currently it provides the following available options:

Corporate income tax (CIT):

- A super deduction of 50% of the eligible expenses incurred for R&D activities;
- Taxpayers can apply an accelerated depreciation regime for assets used in R&D projects (i.e., 50% of the tax value is depreciated during the first year and this is applicable for fixed assets and intangible assets as well); and
- A full exemption from corporate income tax for the first 10 years of business, applicable for companies performing exclusively R&D activities.

Personal income tax (PIT):

Employees performing R&D eligible activities are exempt from personal income tax (at a rate of 10%).

To benefit from this set of tax incentives, the eligible R&D activities should fulfill the following conditions:

- They should be carried out in order to obtain research results, which can be harnessed by the respective company;
- They should be carried out on national territory (i.e., Romania) and/or in the member states of the EU or in the countries belonging to the European Economic Area;
- They should qualify as applied research and/or technological (experimental) development and be relevant for the activity carried out by the taxpayer; and
- They should pertain to a project, containing at least the following elements: the objective of the project, the timeline, the financing sources, the category of the result (e.g., studies, schemes), and the innovative character.

The OECD Frascati Manual is used as a reference from a definition perspective, especially with respect to the five criteria (novelty, creativity, uncertainty, systematic, transferrable) that are tested to accurately qualify an activity as R&D.

The expenses eligible for the additional 50% deduction for CIT purposes include among others:

- Depreciation expenses in relation to assets used in R&D activities;
- Personnel expenses;
- Maintenance and repair expenses; and
- Operating expenses and overheads (based on direct allocation or on an allocation key).

A revamped R&D tax incentive framework in Romania

Although legislative norms for the application of R&D tax incentives were issued in 2016, certain clarifications have been delayed (such as regarding the certification of R&D projects by technical experts appointed by taxpayers). However, the legislation was amended and significantly supplemented at the end of 2022, showing that the Romanian authorities are open to encouraging Romanian taxpayers to benefit from such incentives. The main relevant amendments brought in the legislation are:

- A new detailed procedure issued for certifying R&D projects;
- The R&D experts are designated by the Ministry of Research, Innovation and Digitalization and are included in REXCD database; and
- Certification from a designated R&D expert is mandatory as of 2023 for large taxpayers (and recommended for all other taxpayers for tax inspection purposes).

Final thoughts

Romania revamped its legislation and procedures for applying R&D tax incentives and provided taxpayers with updated rules. These include a clear procedure on how to assess and certify that the activities performed are R&D, together with clear access to qualified R&D experts that can provide such certification. The Romanian R&D tax incentives represent a great way for companies to optimise their tax position and improve their cash-flow, thus the R&D sector is highly relevant from a business perspective going forward in Romania.

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SPAIN

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Clarifications on the VAT refund scheme for non-EU travellers

The VAT refund scheme for non-EU travellers is regulated in Article 147 of the VAT Directive. The reality is that these transactions are actually considered as exports, but since at the time of the transaction the supplier of the goods (normally the shop where the goods are purchased) is not certain that the goods will leave the EU territory, the supplier must charge VAT on the sale, which will then be refunded to the purchaser of the goods if it is proven that the goods have indeed left the EU territory.

In summary, the system works as follows:

- The traveller domiciled in a non-EU country goes to a shop located in the EU, where they purchase a number of items;
- The seller charges them the corresponding VAT on the supply;
- When the traveller leaves the EU territory, they must present the goods and the purchase invoice to the customs office of departure so that the exit can be recorded; and
- The traveller is then required to return the invoice to the supplier and the supplier is obliged to refund the VAT paid.

Some countries that are important tourist destinations, such as Spain, have very advanced and sophisticated VAT refund systems for travellers. These are managed through the use of new technologies, they rarely require paper documents, and they allow VAT refunds to be obtained quickly and efficiently. This is not the case in other member states which continue to use more traditional procedures.

In Spain, from January 1 2019, the VAT refund system for travellers is based on a mandatory electronic documentation system. The refund is obtained through the management of what in Spain is called the "electronic refund document", which must be digitally validated at the customs office of departure of the goods at specific electronic counters for this purpose and which allows communication at that moment with the tax administration for the approval of the refund.

According to Spanish regulations, the proof of export that will give rise to the right to a refund of the VAT paid on the purchase of the goods is, in any case, this electronic refund document.

The VAT Directive and a problematic scenario

The problem occurs, and the Spanish lawmakers do not seem to have taken this into account, when the goods leave the EU territory at a customs office not located in Spain (which is perfectly possible, considering the right to free movement within the EU), where the electronic documents cannot, in all likelihood, be validated because it is a purely Spanish requirement. Since it is the Spanish administration that must decide on the payment of the refund, if the requirements established by it are not met, in a strict sense, the refund may be refused.

However, the system for refunding VAT for non-EU travellers is provided for in Article 147 of the VAT Directive, and this article requires as proof of departure of the goods the invoice or an equivalent supporting document, endorsed by the customs office of departure. This should be sufficient proof to justify the exit of the goods from the EU territory and to secure approval of the refund.

Any additional processes that may be introduced to make VAT refunds more efficient are always welcome but can never be an obstacle to getting refunds paid. This is precisely what happened in the case of Spain when the exit of the goods did not take place through a Spanish customs office.

Maintaining these additional requirements in the case of Spain would create a discriminatory situation between travellers who leave the EU territory through a Spanish customs office and those who do not, something that is not admissible under EU law and which the Spanish administration has finally clarified, stating that in these circumstances, the duly certified invoice or another document of proof should be a sufficient means for obtaining the refund.

The need for harmonisation

The above reinforces the idea that harmonisation is needed on the VAT taxation of certain activities in the tourism sector, such as the Tour Operations Margin Scheme.

Also, a harmonised procedure for refunds for non-EU travellers would be desirable. This has been on the European Commission's agenda for some time. It is understandable that it is not the most urgent issue right now due to more important commitments such as the VAT in the Digital Age (ViDA) proposal. However, even if the ViDA proposal is a milestone for VAT, there are still important VAT issues on the table that require attention.

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Last word
EU tax disputes make the case for reform

The European Commission wanted to make an example of US companies like Apple, but its crusade against 'sweetheart' tax rulings may be derailed at the CJEU.

Josh White

EU leaders may have to get to grips with the need for reform if the European Commission loses its court cases over state aid claims. US technology company Apple and French utility group Engie are fighting the Commission in separate transfer pricing disputes at the Court of Justice of the EU.

If the Commission loses its appeals, the EU may have to take one of two courses: reform state aid law or implement new tax rules. The latter may be more likely, but there are many obstacles to overcome before the EU can consolidate 27 different corporate tax systems.

Giving up and walking away is politically impossible. The Commission has investigated multiple companies and fought several cases at the CJEU. If the Commission retreated at this point, many people would be wondering 'what was the point?'

What's more, there are still live state aid cases and investigations with multinational companies including Amazon, IKEA and Nike. However, the CJEU has sided with the taxpayer several times and there are good reasons to suspect the Commission may have to rethink its strategy.

Signs of defeat

Italian carmaker Fiat won its CJEU case against the Commission in November 2022. Much like in the cases of Apple and Engie, the Commission argued that Luxembourg had breached state aid law in its tax rulings that were favourable to Fiat.

The Commission had argued that the Luxembourg authorities had used the wrong approach to the arm's-length principle to approve an advanced pricing agreement with Fiat Chrysler Finance Europe, previously known as Fiat Finance and Trade.

Nevertheless, the CJEU ruled that this finding was incorrect. This case may be a sign of things to come for companies doing business in the EU.

In the latest case, Apple and Ireland managed to overturn the Commission's decision at the European General Court in July 2020. The Commission found in 2016 that the Irish government had granted Apple illegal state aid in the form of tax rulings.

After the General Court ruling against this finding, the Commission waged an appeal with the CJEU. Originally, the Commission was demanding that the Irish government collect €13.1 billion ($14.1 billion) in back taxes from Apple. This disputed bill has since reached €14.3 billion.

But Apple's state aid case is about much more than money. The Irish government may see the EU decision as an encroachment on the country's sovereignty, while other higher-tax countries view the Irish system as letting businesses avoid paying their fair share.

Similarly, the Engie case has implications for the balance between 'pooled' sovereignty in the EU and national autonomy. It's why these cases cannot be seen in complete isolation from each other.

Advocate General (AG) Juliane Kokott issued an opinion on May 4, finding that the Commission had erred in its decision that Luxembourg granted Engie illegal state aid. Tax rulings in themselves do not necessarily constitute illegal state aid provided they are legal nationally and open to all taxpayers, according to Kokott.

Kokott stressed that the Luxembourg tax rulings granted to Engie were not erroneous, adding that such matters are for a national tax authority and not the Commission or the CJEU. Otherwise, she said, the Commission and the CJEU may impinge on the fiscal autonomy of EU member states.

This opinion may be a sign of a shift in favour of taxpayers and national governments. The Commission cannot expect the CJEU to just rule in its favour every time, but the Engie case could be pivotal for the EU.

We do not have an opinion from an AG in the Apple case yet, but AG Giovanni Pitruzzella will issue his opinion in November. This could still mean the CJEU will rule against the taxpayer, but a mixed result for the Commission – losing one case and winning on appeal – would be bad enough.

> “These judgments may set back the EU’s crackdown on corporate tax avoidance until Europe is more united on tax policy”

These judgments may set back the EU’s crackdown on corporate tax avoidance until Europe is more united on tax policy and when a national tax ruling counts as illegal state aid. Either way, a victory in court may not substitute for political change.

State aid has become a major source of tax controversy