Global Tax News

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A round-up of recent developments from major governments and tax administrations:

Egypt

The Egyptian tax authority (ETA) in association with the Organization for Economic Co-operation and Development (OECD) issued transfer pricing guidelines (Guidelines) on 29 November 2010. The Guidelines provide taxpayers with guidance on the application of the arm´s length principle in pricing their intra-group transactions as well as outline the documentation taxpayers should maintain as evidence to demonstrate their compliance with the principle.

Spain

The General Budget Act for 2011 modifies the Spanish Non-Resident Income Tax Law in respect of the requirements to apply the European Union (EU) Parent Subsidiary benefits, aligning Spanish domestic legislation with EU principles as expressly required by the European Court of Justice (ECJ).

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Royalty payments made by Spanish entities to EU-affiliated entities will be subject to 0% withholding tax as from July 2011 after completion of the transitory period provided by the Royalty Directive.

The Act also declares that the financial goodwill amortization facility of foreign subsidiaries does not apply to acquisition of European Union entities taking place after 21 December, 2007. (Note that refund procedures may take place as a consequence of the retroactive effects of the Law, although it is unclear if, when, and how such procedures may begin.

United States

Non-US corporations doing business in the United States through a US branch or subsidiary corporation (inbound corporations) should be aware of a new US tax requirement that under certain circumstances will require disclosure on the US tax return of US tax positions that are treated as "uncertain" in audited financial statements (AFS).

On 7 December 2010, the IRS and Treasury issued the 2010-2011 Priority Guidance Plan (the Plan). Of the 310 projects that the IRS and Treasury intend to complete by June 2011, 44 are international projects. This is a marked increase in international projects from the 2009-2010 Priority Guidance Plan, that identified 20 international projects out of 315 overall projects.

The Plan provides an overview of the issues that the IRS and Treasury intend to address over the next seven months. As they have done in prior years, the IRS and Treasury state that they will update and reissue the Plan periodically to reflect additional guidance that they intend to publish, to allow for consideration of comments received from taxpayers and practitioners on additional projects, and to respond to developments arising during the plan year. The Plan also indicates items that have already been published.

Most of the international tax items included in this year's Plan are new international tax projects, reflecting the IRS and Treasury's goal of providing published guidance addressing the significant legislation enacted over the past several years. For example, several of the new international tax projects address guidance necessary to implement the FATCA provisions in the Hiring Incentives to Restore Employment Act1 (the HIRE Act) and the various international tax provisions in the Education Jobs and Medicaid Assistance Act2 (the Education Jobs Act). This Alert lists the international tax projects included in the current year's Plan.

The Netherlands

In the center of Europe´s economy

Companies continue to be drawn to the Netherlands as a location for their corporate headquarters, thanks to its robust economic, tax, regulatory and infrastructure environment.

A recent study by Ernst & Young cited four dominant factors behind companies' decisions to locate their headquarters in the Netherlands: proximity to markets/customers; transport and accessibility; quality and availability of labor; and taxes. On all four factors, the Netherlands scores high marks. Located in the center of the three largest economies in Europe _ Germany, France and the UK – the country boasts a high-quality transportation infrastructure. The expansion of European Union (EU) membership to Central and Eastern European nations in 2004 and 2007 contributed further to the attractiveness of the Netherlands as a location for implementing and developing pan-European strategies. The World Bank´s Doing Business report ranks the Netherlands 30th in the world in terms of ease of doing business. It scores highly for the ease of trading across borders – it

The Netherlands provides a 100% exemption provides a 100% exemption for dividends and capital gains from subsidiaries

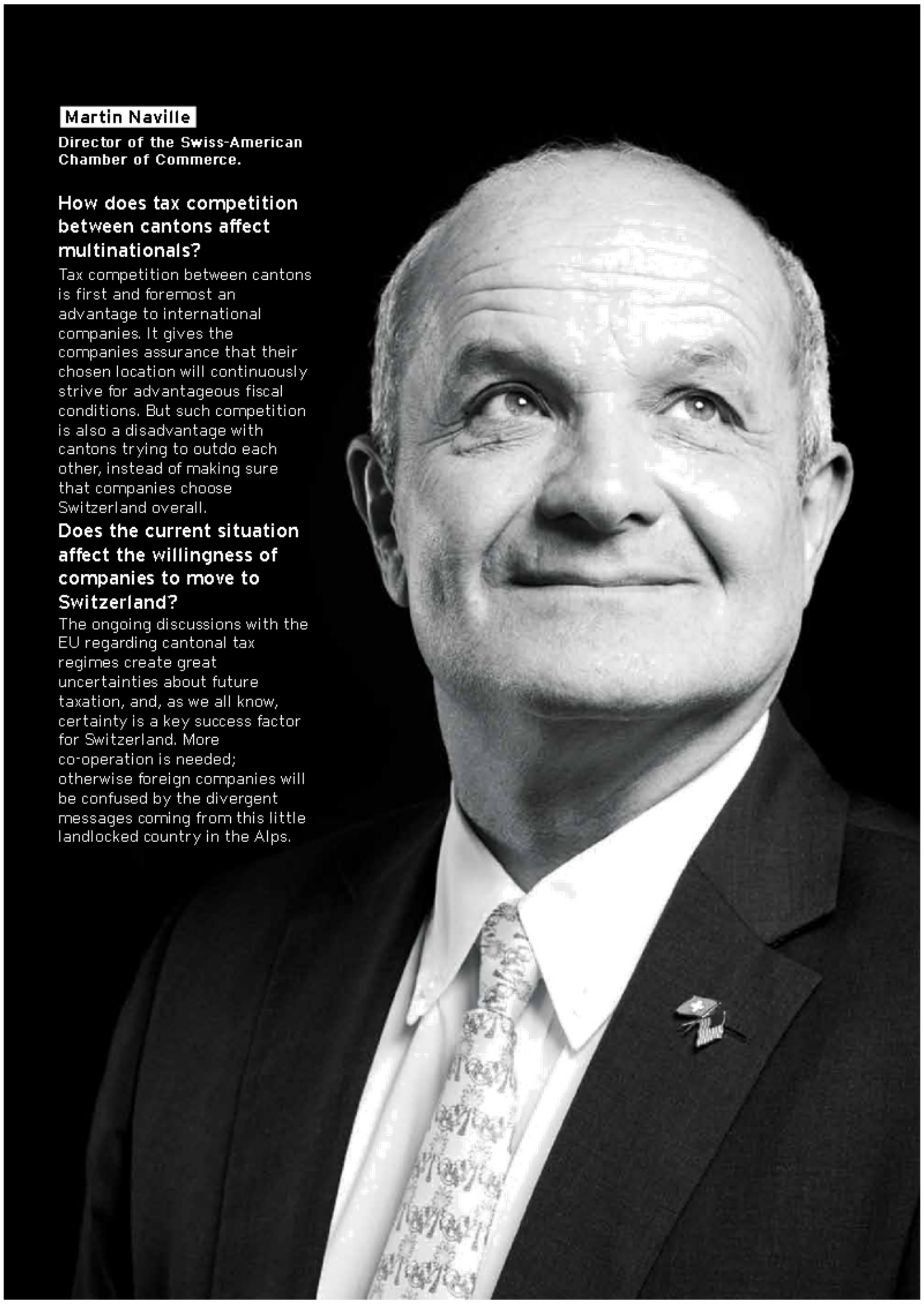
Is ranked 13th in the world. On the tax front, the Naetherlands has a 25.5% base corporate income tax and a lower 20% for smaller companies, which are bellow the equivalent rates in many of its EU partners. Dividends from subsidiaries will be generally excluded from the basis for taxation. This Dutch participation exemption system for avoidance of double taxation has over the past few years found followers in many of the governments around the globe, with the United States being one exception. Yet for the many companies that choose the Netherlands as their headquarters location, it is the country´s highly skilled, multilingual and well educated labor force in a population of 16.5m that holds particular appeal. Not only does an estimated 87% of the Dutch workforce speak English, they also speak many of the European languages of core markets in the region, including French and German.

The country´s long history if international trade and commerce permeates the Dutch culture, making any transition or move to the Netherlands an easy one for most executives.

How low can they go?

Tax competition between Swiss cantons has created an attractive environment for corporate but doubts are growing over whether this approach is sustainable over the long term.

Tourist, for a long time, have been traveling to the picture postcard medieval city of Lucerne to enjoy the spectacular scenery and well-preserved medieval buildings. Even Mark Twain paid a visit in the 1870s and wrote about it in his travel book A Tramp Abroad. More recently, however, the canton of Lucerne has been attracting a new type of visitors – multinational companies in search of a low rate of tax. In September 2009, voters in the canton of Lucerne approved a revision of their tax legislation that would cut the corporate income tax from January 2012 to a record low of 4% to 6.5%, depending on the municipality. "We view tax relief as an investment in our canton´s competitivences," explains Hansruedi Buob, senior manager at the Lucerne Tax Office. He is convinced that, besides attracting new taxpayers, a consistent tax policy oriented towards promoting the attractiveness of Lucerne as a location will also provide significant benefit for private individuals and companies already resident there. In some other parts of central Switzerland, this tax offensive caused considerable unease. The neighboring canton of Obwalden, which previously offered the lowest taxes in Switzerland as well as a flat personal income tax rate, quickly found itself under pressure to follow suit. The cantonal government in Obwalden is now contemplating cutting corporate tax rates even further from 2012 in order the complete with Lucerne. "Only the top position garners favorable publicity, which you don´t get if you´re ranked third or fourth, "says Marianne Nufer-Brändle, head of the tax authority in Obwalden. In other words, Obwalden does not want lose its crown as the Swiss canton with the lowest tax rate to Lucerne.



In recent years, Obwalden´s low tax policy has had a significant effect on its register of companies. Indeed, as Nufer-Brändle points out, the number of registered companies in the canton rose from 2,000 to 3,500 in the four years since the first income tax cut to 6.6%.

Other cantons are gaining in popularity such as Fribourg with is tax regimes governed by a flexible Administration. Schaffhausen offers a combination of proximity to the international airport and the city of Zurich, a low corporate tax rate and a quality of life enhancedby both its geographical location and its cultural history. This combination is enticing an increasing number of relocating companies.

The European Commission taxes notice

Competition between cantons to attract companies with low tax rates has been ongoing for a number of years. This downward pressure on taxes has created a highly competitive tax environment in the country as a whole that has led to a large number of multinationals relocating either their global or European headquarters to

Switzerland. Indeed, the foreign trade development organization OSEC Business Network Switzerland says that competition between cantons is “one of the main reasons why Switzerland is such an attractive location. “According to Martin Naville, Director of the Swiss-American Chamber of Commerce (AmCham) and co-author of the study “Foreign Companies in Switzerland – The Forgotten Sector”, foreign firms in Switzerland already account for around 10% of Switzerland´s economic output. More than 50% of foreign head offices are American, including the oil drilling group Transocean, whose global headquarters has been based in the canton of Zug since 2008. Over the years a number of French and German firms have also migrated to Switzerland, with one early mover being logistics group Kühne+Nagel, which was formerly based in Hamburg. Among the Asian firms with the BRIC countries (Brazil, Russia, India and China) also seen as having great potential for growth.

In addition to being able to vote on their own tax rates, Swiss cantons also offer tax holidays and tax privileges. Tax holidays are based on certain rules and regulations and require a formal decision by the government, because they are granted for macroeconomic reasons. The European Commission has been highly critical of some aspects of the tax privileges defined in the tax laws of the cantons. In February 2007, it informed Switzerland that it considered certain cantonal tax privileges in favor of holding companies, mixed companies or domiciliary companies to be unlawful state aid. The EU announced its intention to reach an agreement with Switzerland on a regulation to put an end to differential tax treatment of domestic and foreign income in Switzerland as well as the non-taxation of non-investment income generated by holding companies in the cantons. Since then, Switzerland and the EU have held several talks on cantonal tax privileges aimed at correcting the perceived distortion of competition. To date, however, no results from these negotiations have been announced.

“The differential treatment of profits depending on whether they are generated in Switzerland or abroad under the mixed company regime and certain aspects of the holding company regime are certainly questionable, “says Dominik Bürgy, Managing Partner Tax at Ernst & Young Switzerland and Vice-Chairman of the Swiss Chamber of Certified Accountants and Taxes Experts. “This is all the more reason for Switzerland to become proactive in adjusting the tax privileges in their current form 5o that they are more ostensibly aligned with EU standards.”

Deterrents to corporate migration

Uncertainty over how this dispute will be resolved in deterring some companies from relocating to Switzerland because they fear that they will lose these special privileges. “At present, there is a great deal of legal uncertainty as to how the tax dispute with the EU can be settled,” says Peter Baumgartner, Director of Swiss Holdings, a body that represents multinationals based in Switzerland. Some commentators in Switzerland fear that an agreement with the EU requiring the cantons to abandon or adjust their special rules would also lead to an axodus of corporate to other jurisdictions. But Búrgy of Ernst & Young believes that these concerns are overestimated. “In my view, the risk of emigration may be mitigated by a combination of a low regular tax burden with EU-approved tax privileges, which at the same time will also continue to attract new corporations,” he says. But while few companies may be willing to leave Switzerland, the numbers arriving have declined, with 54 making their way in 2008 and just 15 in 2009. The financial crisis has certainly added to uncertainty, with companies putting all major plans on hold while they dealt with the more pressing concerns of liquidity and, in some cases, solvency.

Martin Naville of AmCham points to the replacement of a law know as the “Lex Bonny” in 2008 as another important reason why corporate migration to Switzerland has slowed considerably. Previously, this law allowed cantons to give companies that relocated to economically weak regions a reduction in their tax base. But under the new Federal Act on Regional Policy that replaced Lex Bonny, state guarantees were abolished and industry-wide financial aid became integrated into the multi-year programs of the cantons.

In the longer term, most commentators agree that Swizerland will continue to be at the forefront of international tax competition and, for this reason, is likely to remain a highly popular destination for multinationals seeking a new headquarters. From a macroeconomic perspective, Switzerland has low levels of debt, which means that it has much greater fiscal flexibility as compared most of the large European countries, where debt levels have mushroomed as a result of stimulus packages and bank bail-outs. This in turn, is likely to lead to higher taxes in those countries, and this will make Switzerland appear even more competitive by comparison.

But while the influx of firms is broadly welcomed in Switzerland, it does have a knock-on-effect in terms of costs. According to recent study by the Zurich University of Applied Sciences, residential property prices around Lake Geneva have tripled since 2000 and those in the Zurich region have doubled, with vacant rental properties being scarce. A similar effect has been registered in the central Swiss cantons of Schwyz and Zug, where property specialist at state agent Wüest & Partner have even noticed native Swiss citizens being crowded out, because they can no longer afford to live in their home towns.

The political wind dies appear to be changing slightly in the face of such developments. Some politicians, who until now have been unqualified supporters of tax competition, are reasing the possibility of a rethink. There have been unqualified supporters of tax competition, are raising the possibility of a rethink. “There have been isolated voices calling for a “more healthy level” of tax competition and representatives of the higher tax cantons are requesting that the Government set a minimum tax rate. The rationale for doing this would be twofold: first, it would protect the cantons from a ruinous “race to the bottom”, and second, it will avoid conflicts over revenue sharing. Currently, structurally weak cantons receive equalization payments from financially powerful neighbors, even if they have previously enticed companies away from other cantons. With excepted changes the mix of cantons giving and receiving such payments may change substantially.