

WTS ICT Service Line Newsletter

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Argentina



New precedent on the conflicts between domestic GAARs vs treaty law

In the long-standing conflict regarding the appropriate harmonisation of domestic general anti-avoidance rules ("GAARs") vs treaty law, the Argentine Tax Court sided with the Argentine Revenue Service ("ARS") in an attempt to enhance the goals and principles contained in the Argentine Double Tax Conventions ("DTC/s").

On 28 September 2022, the Argentine Tax Court ruled on the "Empresa Distribuidora La Plata" ("EDELAP" or the "company") case, in which the Tax Court had to analyse whether the benefits of the Argentina-Spain DTC were applicable to an Argentine company with Spanish shareholders. According to treaty law, asset tax powers were only vested in the contracting state where the shareholders were located. Indeed, Article 22.4 of the Argentina-Spain DTC, in force at the time of the events, provided that: "(...)Shares, stocks or equity participation in the capital of a company, may be taxed only in the contracting state where the shareholder is resident".

On the other hand, the Argentine Personal Assets Tax ("PAT") provided that equity interests in Argentine companies held by non-resident aliens, in general, were subject to an annual tax burden of 0.5% or 0.25% (depending on the taxable year), which was applicable on the net-equity value of their equity participation. The same tax applies to Argentine resident individuals — other than local companies — who are required to exclude their equity participations in Argentine companies from their annual PAT tax returns. The companies who issued the stock or shares were responsible for collecting and paying the tax to the government.

In this case, EDELAP considered that its shares owned by Spanish holding companies were not subject to the PAT, due to DTC Article 22.4. However, the ARS understood that there was no substance attached to such Spanish holding companies, so they should consider properly constructing the treaty law.

To rule on this matter, the Tax Court applied the domestic general anti-avoidance rule of the "economic reality principle" (provided in the Argentine Tax Procedure Law) and determined that the Spain-Argentina DTC should not apply to the Spanish shareholders, as they were part of an unsubstantiated internationally triangular transaction. In fact, according to the Tax Court, the Spanish shareholders, whose shareholders were Uruguayan holding corporations, were created for the exclusive goal of profiting from the DTC. In practice, the Tax Court applied the so-called "principal purpose test". Therefore, just the same as the Supreme Court in the "Molinos" case, the Tax Court decided once again to deprive a resident of a contracting state from the treaty benefits by applying a domestic general anti-avoidance rule that was not included in the DTC.

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Consequently, it is of utmost importance to scrutinise the substance of foreign holding companies prior to applying treaty law, despite the fact that the DTC wording may not yet include limitation of benefit rules or even principal purpose test standards expressly agreed by the contracting states. To illustrate further, this same outcome would be applicable for income tax purposes, at the time of determining whether a foreign holding company would profit from the reduced rate of withholding tax generally included in the OECD Model Convention Section 10. The fact that treaty law ranks above domestic legislation does not impair per se the application of domestic anti-avoidance rules.

Austria



UAE shareholders now face Austrian withholding tax on dividends

1 March 2023 saw the amended protocol to the double taxation agreement between the United Arab Emirates and Austria (DTA UAE – AUT) enter into force (the amended protocol applies to all covered transactions carried out after 1 January 2023). Whilst the protocol has various implications for residents of Austria (e.g. the credit method is now used instead of the exemption method to avoid the double taxation in Austria), the changes regarding withholding tax (WHT) on dividends mainly affect residents of the UAE.

Before the amended protocol became effective, the following provision was included in Art. 10 (1) DTA UAE – AUT:

"Dividends paid by a company which is a resident of a contracting state to a resident of the other contracting state shall be taxable only in that other contracting state."

The new provision in Art. 10 (1) DTA UAE – AUT reads as follows:

- "a) Dividends paid by a company which is a resident of a contracting state to a resident of the other contracting state may be taxed in that other state.*
- b) However, dividends paid by a company which is a resident of a contracting state may also be taxed in that state according to the laws of that state, but if the beneficial owner of the dividends is a resident of the other contracting state, the tax so charged shall not exceed 10 per cent of the gross amount of the dividends.*
- c) Notwithstanding the provisions of sub-paragraph b), dividends paid by a company which is a resident of a contracting state shall be taxable only in the other contracting state if the beneficial owner is:*
- I. that other state itself, a political subdivision or local authority thereof or a qualified government entity, or*
 - II. a company (other than a partnership) which holds directly at least 10 per cent of the capital of the company paying the dividends."*

Before the amended protocol came into effect, all dividend payments from companies resident in Austria to legal entities and individuals resident in the UAE were exempt from Austrian WHT. Due to the protocol, dividend payments from Austrian companies to individuals who are tax residents of the UAE are now subject to 10% WHT. The state itself, UAE authorities and qualified UAE government entities as well as UAE corporate shareholders holding at least 10% of the shares of the distributing Austrian entity are still exempt from Austrian WHT on dividends. Hence, corporate shareholders holding less than 10% in the Austrian company are also subject to WHT.

On the one hand, individuals resident in the UAE holding at least 10% of the shares of an Austrian company should therefore consider the set-up of a holding structure to still apply the tax treaty benefits. On the other hand, Austrian companies need to carefully monitor their UAE shareholders to determine the proper tax treatment of the dividend payments. Formal requirements stipulated in Austrian law must be obeyed. In this context, it must be noted that the foreign holding company must fulfil substance requirements in order to obtain a WHT reduction.

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As long as the UAE corporate tax law, which will be effective from 1 June 2023, does not introduce a WHT on dividends, the new Art. 10 (1) DTA UAE – AUT itself does not affect dividends paid by companies that are resident in the UAE to Austrian shareholders. However, as long as Austrian shareholders cannot exempt the dividends received (e.g. by applying the participation exemption regime), the UAE dividends will still be fully taxable in Austria in any case.

Brazil



Proposed changes to the Brazilian rules on the tax deduction of royalties

Although provisional measure 1152/22 (MP 1152) is generally known for introducing new Transfer Pricing rules in Brazil, aiming at an alignment with the OECD standards, it also provides for relevant new rules on the deduction of royalties for Corporate Income Tax (IRPJ) and social contribution on profits (CSLL) purposes.

The limits and requirements adopted by Brazil for the tax deduction of royalties in connection with the use of trademark, patents, manufacturing processes and formulas and fees for technical, scientific, administrative or similar assistance have been a controversial issue in recent decades, mainly when due/paid to foreign beneficiaries. The predominant reason for discussions is the fact that rules that set such limits and requirements date back to the late '50s and early '60s and have not been updated despite all changes in the technological, business and global scenarios.

According to these rules, for the purposes of IRPJ, royalties for the use of patents for inventions, processes and fabrication formulae and trademarks due or paid to foreign beneficiaries may be deducted, provided they: (i) are supported by agreements registered with the Central Bank of Brazil (BACEN) and the Brazilian Patent and Trademark Office (INPI); and (ii) do not exceed percentages varying from 1% to 5% of the net revenues derived from the sale of products manufactured or sold with the use of the licensed technology. The applicable percentage is defined by an ordinance enacted in 1958 according to a list of manufacturing activities, sectors and products which has not been updated, creating certain challenges and doubts for the definition of applicable limit. As of 2023, registration with BACEN is no longer required.

Currently, these requirements and limits for the deduction of royalties do not apply to the CSLL.

Furthermore, Brazilian Transfer Pricing legislation currently in force expressly excludes royalties from its scope.

In this scenario, MP 1152 introduces important changes, by setting rules on intangibles and including such royalties within the scope of the Brazilian Transfer Pricing rules, and also by revoking the above-mentioned old requirements and limits and establishing some new deduction rules.

According to MP 1152, the deduction of royalties and fees for technical, scientific, administrative or similar assistance for IRPJ and CSLL purposes will not be allowed when they are paid to low tax jurisdictions or beneficiaries subject to privileged tax regimes, which are listed by the Brazilian Revenue Service.

Moreover, such royalties and fees may not be deducted in the calculation of IRPJ and CSLL if paid to foreign related parties and the deduction of such amounts results in double non-taxation in any of the following cases: (i) when the same amount is a deductible expense for the related party; (ii) if the amount deducted in Brazil is not considered as taxable revenue of the foreign beneficiary under the rules of the jurisdiction where such beneficiary is located; and (iii) in case the amounts are used to finance, directly or indirectly, deductible expenses of related parties, leading to the situations described in previous items.

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The new rules imposed by MP 1152 will be mandatory as of 2024, but the taxpayer may choose to apply them in 2023. MP 1152 is currently being analysed by the National Congress, which may approve, amend or even reject it. After voting by the National Congress, it should be sanctioned by the President to be converted into law.

The progress of MP 1152 must be monitored to assess, with greater clarity, the actual impacts for royalties.

Hungary



Termination of the double tax treaty between the United States of America and Hungary

On 8 January 2023, the six-month grace period lapsed from the notification of the United States to Hungary regarding the termination of its double tax treaty (treaty). Since the United States did not withdraw its notification, the termination is considered to be final.

Background

8 July 2022 saw the United States Department of the Treasury notify Hungary regarding its termination of the double tax treaty between the United States of America and Hungary, which had been in force since 1979.

Based on the official statements of the US Government, the explanation for the termination of the treaty was the veto of Hungary on the introduction of global minimum tax, which defines a uniform 15% (effective) tax rate for multinational companies of the participating member states. Hungary ultimately agreed to introduce global minimum tax, however, the United States did not withdraw the termination of the treaty.

The effects of the termination

Hungarian companies with investments in the US

Based on the treaty, the taxation of income of Hungarian companies from the United States was quite favourable, the withholding tax (**WHT**) was 0% for interest and royalty payments, and it was 5% or 15% in the case of dividend payments. With the termination of the treaty, the WHT payable in the United States will increase to 30%. Nevertheless, 90% of the tax paid in the US can be credited against the corporate income tax payable on such income in Hungary.

Another favourable factor of the treaty was that the income of permanent establishments of Hungarian companies in the United States was exempt from Hungarian corporate income taxation. Without a treaty in place, this exemption would no longer exist.

Hence, the income of such permanent establishments would be taxable in Hungary with the possibility to credit 90% of the tax paid in the US.

US companies with investments in Hungary

In most cases, the termination of the treaty would not result in a significantly higher tax burden for US companies with investments in Hungary, as Hungary does not impose WHT on payments between companies (including dividend, interest as well as royalty). Although there would be some exceptions: when US companies sell their direct shares in their Hungarian subsidiary which is considered as a company holding real estate. If the US company generates profit from this transaction, then 9% Hungarian corporate income tax is payable after the old treaty is no longer in effect.

Effective date of the termination

The termination is effective on 8 January 2023. Nonetheless, with respect to taxes withheld at source, the treaty shall cease to have an impact on 1 January 2024. Regarding other taxes, the treaty shall cease to have effect with respect to taxable periods beginning on or after 1 January 2024.

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Theoretically, it would be possible for the two countries to conclude a new double tax treaty (or to reinstate the previous one), but as there is currently no negotiation about a new treaty, it is highly unlikely that it would happen until the end of the year.

Italy



International tax amendments in the Italian Budget Law for 2023

Costs related to transactions with non-cooperative jurisdictions

The Budget Law for 2023 has reintroduced, with amendments, a provision, dating back in its initial formulation to 1992, according to which expenses and other costs arising from transactions with counterparts resident or established in jurisdictions that are deemed to be non-cooperative for tax purposes are deductible only where certain conditions are met.

More specifically, the deduction is limited to the fair market value of goods or services purchased. In essence, the provision has effects similar to those of Transfer Pricing rules, but also applies to third-party transactions.

Any excess amount is deductible only where the Italian entity can demonstrate that the underlying transaction has a sound economic rationale.

Costs incurred are in any case subject to the specific reporting obligation in the tax return.

The jurisdictions concerned are those that have been identified in Annex I to the EU List of Non-cooperative Jurisdictions for Tax Purposes. The list presently consists of 16 jurisdictions, including, among others, two of recent introduction and non-negligible importance in Italian cross-border trade, namely Costa Rica and Russia.

New rules on real estate investment structures in Italy

The Budget Law for 2023 has extended the Italian source jurisdiction with respect to capital gains deriving from real estate structures owning properties in Italy.

Under the new rule, capital gains derived by foreign investors from the sale of shareholdings in entities deriving their value (even indirectly) mainly from real estate located in Italy are considered as taxable in Italy.

The new provisions:

- › do not apply with respect to capital gains realised by EU-regulated collective investment funds;
- › do not take into consideration property owned by entities whose business activities consist of building or selling such properties or ones directly used for business purposes.

Few Italian treaties provide for the source taxation of capital gains deriving from the sale of Italian shareholdings, so the new domestic provisions will have a limited application in the short term, but the scenario will change significantly once Italy has ratified the MLI, which allocates source taxation on capital gains in a way similar to the new Italian rules.

Substitute tax on foreign undistributed profits

Foreign-source profits, derived from jurisdictions with preferential tax regimes (i.e. effective tax rates lower than half of the virtual tax rate applicable if the distributing entity was an Italian resident), can be exempt from Italian corporate income tax in the hands of the Italian resident recipient entity through the payment of a substitute tax.

The substitute tax is applicable at a rate of 9% and applies only to undistributed profits resulting from the financial statements for financial year 2021 of the foreign entity. The substitute tax is further reduced to 6% where the profits are repatriated within the deadline for the payment of the balance of corporate income tax due for financial year 2022 (i.e. by 30/06/2023 for calendar-year adopters) and then retained by the recipient entity for a subsequent period of not less than two financial years.

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Nigeria



Updates in international corporate tax (ICT) in Nigeria

The ever-evolving nature of tax law in Nigeria results in regular updates in Nigeria's ICT regime. Here, we consider some of the recent and proposed changes to Nigeria's ICT laws.

Reversal of the unilateral withholding tax (WHT) rate

Since 1999, Nigeria has unilaterally implemented a WHT rate of 7.5% on dividends, interest and royalties (DIR) paid by residents of Nigeria and beneficial owners of DIR resident in countries which are double taxation treaty partners to Nigeria. With effect from 1 July 2022, the Federal Inland Revenue Service (FIRS) announced the discontinuation of this policy and implementation of a WHT rate of 10% on DIR, and 5% on royalties payable to individuals except in respect of certain relevant treaty countries. In essence, the rates specified in the tax laws shall apply, except where it exceeds the maximum rate specified in the tax treaty; in which case, the rate specified in the tax treaty shall apply.

The Nigerian Startup Act 2022

In October 2022, the Nigerian President assented to the Nigerian Startup Act 2022. The act makes provisions for the exemption of qualified startups from the payment of income tax for a total period of five years. Notably, the act also encourages foreign and local investment in the ownership of a qualified startup. It provides that any person, angel investor (local or foreign), venture capitalists, private equity funds, etc. who invests in a qualified startup is entitled to an investment tax credit equivalent to 30% of the investment provided that such credit shall be applied to any gains on investment which are subject to tax.

Furthermore, qualified startups which are involved in the export of products and services are deemed eligible to export incentives and financial assistance under the Export (Incentives and Miscellaneous Provisions) Act. Significantly, upon disposal of assets by an investor, the gains which accrue to such investor are exempt from capital gains tax, provided the assets have been held in Nigeria for a minimum of 24 months.

The Sentinel Payment Gateway

The FIRS announced the automation of tax payments on online gaming using the Sentinel National Payment Gateway and Electronic Solution. The gateway is a transaction processing system that enables integrated payment service providers to deduct taxes at transaction points and remit the tax deducted directly to the government. Significantly, while it is not mandatory for non-resident companies offering online gaming services in Nigeria to be registered in Nigeria, they must connect to the gateway for the purpose of collecting and remitting taxes for online gaming activities.

Relevant proposed changes to the Finance Bill 2022

Finally, the Finance Bill seeks to codify the taxation of companies which derive revenue from gaming or lottery businesses. Also, in line with Nigeria's climate change and Green Growth commitment at the United Nations Climate Change Conference, the Bill proposes on the one hand to incentivise companies utilising associated and non-associated gas by offering a 50% investment tax credit on their qualifying investment for the purposes of research and development and, on the other hand, to deter gas flaring by providing that medium and large companies that flare gas in Nigeria would be liable to 50% corporate tax, above the 30% nominal income tax rate.

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Pakistan



Changes in the capital gains tax regime

Advance tax on the sale of shares of private and public unlisted companies

The Federal Government has enforced certain taxation measures through promulgation of the Finance (Supplementary) Act, 2023 [the "Act"], effective from 24 February 2023. These measures include amendment to Section 37 of the Income Tax Ordinance 2001 [the "Ordinance"], relevant to the taxation of capital gains on the sale of shares other than listed shares. According to this amendment, the persons acquiring shares of private companies and public unlisted companies are required to deduct advance tax from the gross consideration paid for these shares. The amount of tax deduction is calculated at the rate of ten per cent (10%) of the value calculated based on the fair market value (FMV) of shares as per the method prescribed under the income tax rules, but without reduction of liabilities.

The tax deducted from the consideration is required to be deposited with the Federal Government within fifteen (15) days — which shall be considered an adjustable advance tax for the seller. Default in complying with the new requirements shall attract penalties and default surcharges of the ordinance.

The person disposing of the shares is required to file prescribed information relating to the transaction with the Commissioner Inland Revenue within thirty (30) days of the transaction. The Commissioner has been empowered to call for relevant information through notice earlier than thirty (30) days. An application for specific exemption from withholding tax can be filed with the Commissioner where applicable.

Off-market settlement of securities

Capital gains on the disposal of securities are currently chargeable at fixed tax rates applicable as per section 37A of the Ordinance. The securities include shares of a public company, voucher of Pakistan Telecommunication Corporation, Modaraba Certificate, an instrument of redeemable capital, debt securities, units of exchange-traded funds and derivative products. These tax rates vary based on the nature of the security, holding period and date of its acquisition. The Act has excluded those transactions of securities which are disposed other than through registered stock exchange or settled through the National Clearing Company of Pakistan Limited (NCCPL). Accordingly, said transaction will be chargeable under the (amended) Section 37 of the Ordinance.

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Poland



Another twist in the interpretation of "beneficial ownership"

As of 2022, Polish CIT regulations contain a new definition for beneficial owner (BO). To be considered a beneficial owner, the payee inter alia needs to carry out genuine business activities in the country of residence. The examination of the genuine business activity of the payee now requires an assessment of the 'nature and scale' of the activity carried out with regard to the concerned receivables.

The Polish Ministry of Finance has not published any tax guidance which could support the Polish WHT agents in the practical adoption of the amended definition. However, during 2022, the Voivodship Administrative Court in Lublin ('the Court') examined complaints against the refusals to issue preference opinions (which exempts WHT agent from the mandatory "pay & refund" mechanism), presenting its own assessment of genuine business activity criteria.

According to the court, the following circumstances speak against genuine business activity:

- › lack of personnel or hiring just one part-time employee and members of the board performing similar activities for other group entities;
- › close organisational, financial and personnel links between the taxpayer and other entities, and the fact that the taxpayer's activity background (premises, personnel, administration) is closely linked to the group to the extent that the other entities provide the taxpayer with all the elements necessary for its existence and for undertaking activities;

- › the lack of ownership of the assets used to carry out the declared activity and the performance of the activity using, together with several other entities, a relatively small office;
- › lack of proportion between the amount of initial capital and the level of assets and liabilities of the taxpayer;
- › very low costs for the office rent, not incurring the salary costs of the employees the taxpayer declares to employ, but only incurring the costs of consultancy services.

According to the court's position, the taxpayer should have a minimum management capacity even if activities are outsourced, to verify the works presented by external parties, and to be able to make investment decisions. In each case, the court has also examined the circumstances of the business in detail, including analysing the taxpayer's financial statements in terms of its assets and expenses.

Verification of beneficial ownership under the above rules is even more relevant, since the Supreme Administrative Court ("SAC") in the judgement of 31 January 2023 (ref. II FSK 1588/20) indicated that **the obligation of a WHT agent to verify the beneficial owner (BO) status of the dividend's recipient, although it does not result directly from the conditions of the exemption, is justified in view of the Directive 2011/96/EU.**

SAC indicated that the verification of the BO status should consider the payer's capabilities and does not imply an obligation to conduct proceedings as with the tax authorities. When assessing due diligence, the WHT agent's situation should be taken into account, in particular: its position in the trade, the legal structure in which it participates, and the existence and type of links between the entities: personal, capital, organisational or the level of business professionalism.

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Finally, **SAC approved a look-through approach**, i.e. applying WHT exemption/preference when dividend is paid to an intermediary entity, if the beneficial owner of the dividend is known and is headquartered in the EU or EEA.

Senegal



Banking sector: the introduction by the GTC (general tax code) of the deductibility of losses on doubtful or disputed debts through the initial finance law for the year 2023

For a long time, a main concern of banking and financial institutions, the tax deductibility of losses on debts, had finally been enshrined in Senegal by decision of the Minister of Finance No. 01719/MEFP/CAB/CT JK of 4 March 2019.

However, to provide more legal certainty to the actors and especially to comply with community legislation, in particular the 2020 WAEMU Directive on the harmonisation of the tax regime of credit losses, the Initial Finance Law for the year 2023 (IFL) adds a point 10 to Article 10 of the GTC, enshrining the deductibility of losses on debts recorded by lending institutions.

This reform allows, at least with regard to this issue, the reconciling of the prudential standards in the banking sector with those of tax, since the provisions of the instruction

of the BCEAO No. 026-11-2016 of 15 November 2016 have always stipulated to banking companies to write off debts classified as doubtful or disputed at the end of the fifth accounting period from the transfer to the doubtful debts account.

However, for the benefit of the tax deductibility of credit losses enshrined in the IFL 2023, banking and financial institutions are required to meet certain substantive and formal requirements:

Substantive requirements

- › The debt must be granted in compliance with the prudential framework to which credit institutions are subjected;
- › The debt must be qualified as doubtful or litigious, in accordance with the provisions of the Banking Chart of Accounts (BCA);
- › The debt must remain uncollected at the end of the fifth accounting period from the date of its transfer to the doubtful or disputed debt account.

Formal condition

- › A detailed statement of loss must be attached to the corporate tax return, specifying the identity of the debtor, the date the loan or credit was granted, the original amount, the amount still to be recovered, the amount written off, the nature and value of the collateral, the date the debt was transferred, and the stage of the collection procedure.

Exceptions

However, it should be noted that this deduction does not apply to:

- › debts against the state, public bodies and debts granted to related parties as defined by the banking regulations.
- › debts for which no collection action has been taken as well as those for which collection actions, although carried out, have been abandoned without failure recorded by a ministerial officer, either because a settlement agreement, in whole or in part, has been reached between the creditor and their debtor, or for any other reason resulting from the desire of the credit institution to put an end to the legal proceedings.

In a nutshell, this new measure is very consolidating for the taxation of banking institutions, but it is deplorable that it has not been extended to the institutions in the micro-finance sector (IMF), which are confronted with the same problems as the banking institutions on the issue of credit losses. Indeed, in the same way, the IMF is also obliged to write off certain bad debts but without benefiting from this preferential tax regime.

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Spain



Tax measures introduced in Spain for 2023

The Spanish Government has approved several tax measures which have come into force in 2023. The main measures regarding corporate income tax are summarised below:

- › A reduced rate of 23% (instead of the general rate of 25%) is applicable to companies with a group turnover of less than 1 million euros. The special rate is not applicable to asset-holding companies.
- › Entities that are part of a tax group will only be entitled to offset 50% of the losses made in a financial year against profits made by the group entities during the same financial year. The remaining 50% shall be included in the tax base of the tax group in equal instalments in each of the first 10 following tax periods. This is a temporary measure applicable to financial year 2023.

This measure applies in addition to the already existing limitation to offset losses. In this regard, tax losses can be offset up to the higher amount between one million euros and a percentage of the taxable base which depends on the taxpayer's turnover, i.e. turnover of less than 20 million euros: 70%, turnover between 20 million and 60 million euros: 50% and turnover of at least 60 million euros: 25%.

- › Certain economic activities carried out in the Balearic Islands will benefit from some tax incentives during the financial years 2023 to 2028.
- › Startups can benefit from several tax benefits; i.e. (i) reduced rate of 15% during the first four years where the company obtains a positive taxable base, (ii) no obligation to file instalment payments during the first two years after the company obtains profits and (iii) special rules regarding the deferment of tax debts can be applied.

It must be noted that this measure has been introduced by the law known as "Start-ups Law", which introduces measures not only regarding corporate income tax, but also rules that benefit the startups' investors and employees. In this connection, (i) the stock option benefits for employees are better than the general ones, (ii) investors can benefit from a tax credit and (iii) the law has added flexibility to the in-patriate regime for individuals – amongst others, it allows "digital nomads" to apply the regime.

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