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Contributions for Edition 18 of the EMEA Tax Bulletin should be with Nikki Papadopoulos at nikki.papadopoulos@bkremea.com by 6 April 2018

EMEA TAX BULLETIN

JANUARY 2018 - ISSUE 17

Dear Friends and Colleagues,

Welcome to the first edition of the EMEA Tax Newsletter of 2018. I trust that it is not too late to wish you all a happy, successful and, above all, healthy new year! The month of January, named after Janus, the Roman god of beginnings, transitions and endings, seems appropriate for a newsletter which looks back at the year just gone as well as ahead to the year to come. Accordingly, this edition features articles on our region´s annual tax meeting which was held in Amsterdam back in November 2017 as well as a summary of last year´s start of the Employment Tax Practice Group and its plans for this year. In addition, there are updates on new tax legislation in Romania, Germany and the Netherlands as of 2018, a report on Benchmarking for Transfer Pricing Purposes and other news. In addition, guest contributions from Australia and India give us an insight into recent changes to the respective tax systems. All in all, plenty of reading material!

As always, I would like to say thank you to all who have contributed to this newsletter, as well as to Nikki, Tim and Julia for putting it together again. Your input is immensely important, and we look forward to your continuing support for future editions.

We never know what the New Year has in store for us, but it will hopefully give us many opportunities to get together and exchange news and ideas. My fellow committee members and I look forward to meeting many of you in 2018!

Please let us know if there is anything the tax committee can help you with.
Petra

Petra Owen
EMEA Tax Committee Chair
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Within this edition (click to jump to page):

Major amendments to Romanian Tax Code for 2018

I.Social Charges and Tax on Income

New approach will be applied starting with 1st of January 2018.
The social contributions will migrate from employer towards the employee. The employer will be obliged to withhold and pay on behalf of employee social contributions liabilities to the state.

1.The Social Insurance Contribution due to the Social Insurance Budget at the following rates:
a) 25% pension contribution – due by employee;
b) 4% pension contribution for particular working conditions – due by employer;
c) 8% pension contribution for special working conditions – due by employer.

2. 10% Health Insurance Contribution due by employees to the Budget's National Social Health Insurance Fund

3. 2.25% Employment Work Insurance Contribution – due by the employer to the Consolidated General Budget.

Social Insurance Contributions due by individuals obtaining salaries or incomes assimilated to salaries based on a full-time or part-time individual labor contract must be equal or higher than the minimum social security contribution which is calculated by applying the rate corresponding to the specific working conditions to the minimum gross wage in Romania valid for the number of working days in the respective month.

4. Tax on salary income and income assimilated to salaries is 10%.

II. Taxation on Micro-Enterprise

Starting with 1st of January 2018, the companies with turnover lower than 1 million EUR will have the option of paying tax on income 1% or 3% (if they do not hire employees) on total income instead of 16% as corporate profit tax.

III. VAT split

Companies in procedure of insolvency and companies with certain outstanding VAT liabilities to the state for longer period than 60 days will be obliged to open a specific bank account exclusively for amount of VAT to be collected and paid.

Threshold of outstanding VAT liabilities condition for VAT split system is presented as follows:

- 15,000 lei, approximately 3,200 EUR for big tax payers
- 10,000 lei, approximately 2,100 EUR for medium tax payers
- 5,000 lei, approximately 1,075 EUR for small tax payers

If vendors do apply split VAT system, then their customers VAT payers will be obliged to pay VAT amount in vendor's specific VAT account. The lack in following this process is leading to a penalty of 0.06% per day until correction will be done within a period of 30 days and respectively 10% for a longer period.
Other type of debit operations from this VAT bank account will not be allowed except with acceptance of Tax Authority and based upon certain documentation.

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Our team of professionals are available for any clarifications or additional details required in your analysis.

Disclaimer:
The above information represents just a summary of aspects we consider relevant in the recently published legislation. This is not exhaustive disclosure of information and it is not intended to be used as advice on any particular matter. We invite all readers to contact us for further clarification of any specific issue. Euroglobal's team and its associates disclaim liability in any action taken by a third party in reliance exclusively on summarized information presented in our publications.

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Blick Rothenberg has appointed Heather Self as a partner in the corporate tax team in London

Heather has over 30 years' experience, most recently as a partner at Pinsent Masons and prior to that as the head of tax at a FTSE 100 company, an anti-avoidance adviser at HMRC and a partner at Ernst & Young.

She is a member of International Tax Review's Global Tax 50 2017, recognised for her work in setting up the 'Women in Tax' network and regularly speaks and writes on tax matters.

Heather is a Fellow of the Institute of Chartered Accountants in England and Wales and of the Chartered Institute of Taxation; she has a long-standing interest in tax policy and has previously been a member of the CBI Tax Committee for a number of years, and is a former chair of the Chartered Institute of Taxation's technical committee.

As well as an experienced speaker and media commentator, including frequent BBC radio and TV appearances and professional and academic conferences, Heather is active on Twitter and can be found commenting on topical tax issues as @hselftax.

Genevieve Moore, Head of Corporate Tax at Blick Rothenberg, said: "Heather is a great addition to the firm and brings with her a wealth of knowledge and experience from a wide range of perspectives. I am delighted to welcome her to the team."

For more information, please contact Julian Menendez from Blick Rothenberg
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EMEA BKR Employment Tax Practice Group Update

The next webinar for the EMEA BKR Employment Tax Practice Group is scheduled for Wednesday the 28th February at 10 am GMT. An email invitation has been sent to all participants who have expressed an interest to join the sessions. The topic chosen by most participants for the next session is Country registration requirements for employees and formal requirements for the employer. The session will be chaired by Vanesha Kistoo from Blick Rothenberg.

We take the opportunity to thank all participants for their feedback on the previous session. Your input is valuable; please continue to let us have your ideas and suggestions as the purpose of this practice group is to act as a forum for tax advisers from member firms to share knowledge as well as updates. There is no set format or frequency for the webinars; we would like participants get something from the sessions that is either useful for them or their clients and where possible, promote inter firm collaboration.

The last session was held on 5th October 2017. The topic was tax relief for internationally mobile employees. Attendees sent in their points on slides beforehand which were then used as the basis for the session. For the first time the group adopted a webinar format where all speakers could see the slides and speak in turn. There were participants as far ranging from Cyprus to Austria and Australia to the UK. Those who attended had a productive discussion using the slides to raise particular points and there were some good questions. The output is contained in a recording of the session, that also shows the slides, and is available in the BKREMEA Members area at Recording.

We are currently considering a joint project, perhaps

EMEA BKR Employment Tax Practice Group Update (contd.)

a survey or a document which sets out an overview of what a 'start-up' needs to consider when setting up an operation overseas. If you have any other ideas you would like to share or if you would like to participate, we would like to hear from you.

Please contact the Executive Director, Tim Morris on +44 (0)20 7544 4840, tim.morris@bkremea.com and Nikki Papadopoulos on Nikki.Papadopoulos@bkremea.com who will pass your views on.

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Australian state level tax legislation targeting foreign persons

Australian governments, both at the Federal and state level have for several years been targeting foreign individuals and other foreign investors in a range of ways. Most recently, 2017 has seen legislation at both the Federal and state levels which will introduce new provisions apply to foreign and non-resident persons or will extend laws already in place. In May 2017, the Treasurer announced several measures targeted specifically at foreign residents in the 2017-18 Australian Federal Budget.

Some of these provisions are in federal legislation and so apply to all Australia. Others were introduced by state governments. These will apply only to a particular state and may apply differently to similar provisions in other states. Having addressed the measures applying at the Federal level in a previous articles, this article addresses recent changes at the State level.

Foreign Purchaser Surcharges

As part of the State budgets delivered in May/June 2016, Victoria increased the rate of its foreign purchaser surcharge and New South Wales and Queensland introduced surcharges of their own for both stamp duty and land tax. New South Wales recently expanded the scope of both surcharges from 1 July 2017. The rates of stamp duty surcharge and land tax surcharge are as follows:

	Victoria	New South Wales	Queensland
Surcharge purchaser duty on residential property	7% from 1 Jul 2016	8% from 1 July 2017	3% from 1 Oct 2016
Land tax surcharge for the 2017 land tax year	1.5% for residential and commercial property	0.75% for residential property	None

Surcharge purchaser duty on residential property (Surcharge Purchaser duty)

The key issues surrounding the foreign purchaser additional duty/surcharge are in respect of the definition of a foreign purchaser or foreign person and the definition of residential property/land. The issues can be summarised in the following table:

Australian state level tax legislation targeting foreign persons (contd.)

	Victoria	New South Wales	Queensland
Name	Foreign Purchaser Additional Duty (FPAD)	Surcharge Purchaser Duty (SPD)	Additional Foreign Acquirer Duty (AFAD)
Start Date	1 July 2015	21 June 2016	1 October 2016
Rate	7% (from 1 July 16)	8% (from 1 July 2017)	3%
Property	Residential property	Residential land	AFAD residential land
Transferee	Foreign purchaser	Foreign person	Foreign person
Interest	Direct or indirect	Direct or indirect	Direct or indirect
Exemption Regime	Yes	No	No

As is often the case with taxes and duties that directly fund the individual States, each State has introduced its own individual mechanisms to impose differing rates, for different types of property, on different classes of purchasers.

With that in mind and to avoid over complicating an already complex area, we will focus only on our home state of New South Wales. You should get appropriate advice where the residential property is subject to the surcharges of another state.

Surcharge purchaser duty in New South Wales

The 2016 NSW Budget introduced a 4 per cent surcharge purchaser duty on the purchase of residential real estate by foreign persons from 21 June 2016. However, the 2017 Budget increased the rate to 8% for agreements entered into on or after 1 July 2017. The surcharge is in addition to the duty payable on the purchase of residential property. This surcharge will also apply to landholder transactions if there is a landholder liability and one or more of the properties owned by the landholder is classified residential and the purchaser is a foreign person who purchases shares or units in the landholder.

Foreign persons will also no longer be entitled to the 12-month deferral for the payment of stamp duty for off-the-plan purchases of residential property. A purchaser/transferee declaration must be completed when buying or acquiring land in NSW.

Permanent residents (including New Zealand citizens)

From 20 June 2017 permanent residents, including New Zealand citizens holding a Special Category visa (subclass 444), are exempt from surcharge purchaser duty on their principal place of residence, if they occupy the home for a continuous period of 200 days within 12 months of purchase. The exemption will be granted if the person declares that they will complete the 200-day residence requirement.

Calculating surcharge purchaser duty

If ‘A’, who is a foreign person, purchases a residential property for $2 million, the duty is calculated as follows:

Stamp duty payable on $2 million $95,490

Surcharge purchaser duty of 8% on $2 million $160,000

Total duty payable $255,490

Land tax surcharge in New South Wales

The land tax surcharge applies to foreign persons owning residential land. If you meet the definition of a ‘foreign person’ and you own residential land in NSW above a certain value threshold you must pay a land tax surcharge of 0.75 per cent from the 2017 land tax year onwards. This is based on the taxable value of all residential land you own at 31 December each year including your principal place of residence. The surcharge is in addition to any land tax you may already pay and you may be required to pay the surcharge even if you do not pay land tax.

The surcharge is assessed in relation to each parcel of land, and is proportional to the extent of ownership. There are no joint assessments, secondary deductions do not apply and there is no tax-free threshold applicable to the surcharge.

Foreign persons, residential land and property

Surcharge purchaser duty and the land tax surcharge

Australian state level tax legislation targeting foreign persons (contd.)

apply to foreign persons in respect of residential land or property. The definitions of foreign person and residential land or property therefore need to be considered in detail.

Residential land

Residential land does not include land used for primary production to which a land tax exemption applies. However, it includes any of the following:

a. a parcel of land on which there are one or more dwellings, or a parcel of land on which there is a building under construction that, when completed, will constitute one or more dwellings, or

b. a strata lot, if it is lawfully occupied as a separate dwelling, or suitable for lawful occupation as a separate dwelling, or

c. a utility lot if its use is restricted to the owner or occupier of a strata lot, or

d. a land use entitlement, if it entitles the holder of the land use entitlement to occupy a building, or part of a building, as a separate dwelling e.g. company title and residential flats, or

e. a parcel of vacant land that is zoned or otherwise designated for use for residential or principally for residential purposes.

The surcharge is apportioned if a building has both residential and commercial purposes by applying an apportionment factor to the land tax value.

All other land tax exemptions may apply, including those for:

- boarding houses;
- low cost accommodation;
- residential parks;
- retirement villages;
- primary production land; and
- childcare centres.

Foreign person

The following are not foreign persons:

- Australian citizens regardless of where they live.
- Permanent residents of Australia who are ordinarily resident in Australia.
- New Zealand citizens who hold a special category visa and are ordinarily resident in Australia.

However, any of the following persons can be a foreign person:

- an individual
- a corporation
- a trustee of a trust
- a beneficiary of a land tax fixed trust
- a government
- a government investor
- a partner in a limited partnership.

To determine whether you are a foreign person, you need to consider:

- the rules for the particular type of entity through which you hold the residential property; and
- whether you hold a substantial interest or you and your associates hold an aggregate substantial interest

Foreign person

An individual, who is not an Australian citizen, is a foreign person if they are not ordinarily resident in Australia. An individual is ordinarily resident if they:

- have actually been in Australia during 200 or more days in the previous calendar year (excluding the date of arrival or the date of departure), and;
- is not (or, if not in Australia, was not immediately before their most recent departure from Australia) subject to any limitation as to time for their continued presence in Australia.

A corporation is a foreign person if:

- an individual not ordinarily resident, a foreign corporation or a foreign government holds a substantial interest in it, or
- two or more persons, each of whom is an individual not ordinarily resident in Australia, a foreign corporation or a foreign government, hold an aggregate substantial interest.

The trustee of a trust is a foreign person if:

- an individual not ordinarily resident in Australia, a foreign corporation or a foreign government holds a substantial interest in the trust, or
- two or more persons, each of whom is an individual not ordinarily resident in Australia, a foreign corporation or a foreign government, hold an aggregate substantial interest in the trust.

Where a trust is a fixed trust for land tax purposes, the

Australian state level tax legislation targeting foreign persons (contd.)

beneficiaries are liable for their proportionate interests only. However, the trustee is responsible to pay the surcharge if the beneficiary defaults.
For special trusts, beneficiaries are not treated as owners and therefore they will not have to pay the surcharge. However, where any one or more of the potential beneficiaries are foreign persons, the trustee will be liable for surcharge land tax on the trust's interest in the property.

You will note that, for the surcharges to apply to a foreign person that is not an individual, an individual or individuals must hold a substantial interest in the entity or the trust. A person holds a substantial interest in an entity or trust if:

a. for an entity: the person holds an interest of at least 20 per cent in the entity; or
b. for a trust (including a unit trust): the person, together with any one or more associates, holds a beneficial interest in at least 20 per cent of the income or property of the trust.

Two or more persons hold an aggregate substantial interest in an entity or trust if:
a. for an entity—the persons hold an interest of at least 40 per cent in the entity; or
b. for a trust (including a unit trust)—the persons, together with any one or more associates of any of them hold, in the aggregate, beneficial interests in at least 40 per cent of the income or property of the trust.

The definition of associate includes:
- individuals (e.g. relatives)
- companies (e.g. substantial interest holders, holding entities, senior officers)
- partnerships
- trusts and super funds (e.g. substantial interest holders).

A relative of a person means:
- the person's spouse; or
- the parent, grandparent, brother, sister, uncle, aunt, nephew, niece, lineal descendent or adopted child of that person, or of that person's spouse (and the spouse of any of these persons).

Calculating the land tax surcharge

To assess the surcharge, calculate the taxable value of residential land, taking into account any relevant exemptions, the use of the land, and the proportion of ownership of each foreign person. The taxable value of residential land used for calculating the surcharge is the same as that used for land tax purposes. The tax liability will generally be the average of the unimproved land value for the current tax year and for the previous two tax years.

Example

'A' is a foreign person who owns land with a total land value of $2,000,000. 'A' owns both commercial and residential land.
$1,200,000 of the land held by 'A' is 'residential land'.
The remaining $800,000 is commercial land.
The land tax payable by 'A' is calculated on $2 million, which is $23,316.

The surcharge is calculated on the residential land which is 0.75% of $1.2 million = $9,000.

The implications of the surcharges for stamp duty and land tax for trusts in particular

If you are considering the surcharges for foreign persons in respect of both stamp duty and land tax you will need to take care about the terms of a trust deed, particularly if it is a discretionary trust. It is noted that where a foreign person has the potential to benefit under a discretionary trust, it may be possible for such a trust to be considered a foreign purchaser for the purposes of these additional taxes.

A revenue ruling (G10) has been introduced in New South Wales in respect of this. It exempts a discretionary trust from surcharge taxes with retrospective effect if the trust deed is amended to remove foreign persons from the list of beneficiaries at any time between the introduction of the surcharges and the present date, and otherwise within 6 months after the liability was assessed.

It is therefore critical to speak with your lawyer to determine whether restrictions are required within the deed to ensure these additional taxes are not imposed on property holdings and transactions.

By Walker Wayland New South Wales
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BKR EMEA 2017 Tax Meeting – Amsterdam

Under the Chair of the EMEA Tax Committee, Petra Owen (Hansa Partner, Hamburg), forty BKR EMEA Region Tax specialists met for this year's regional Tax meeting. This was the largest number to attend for several years. The meeting took place at a new venue, the Hilton Amsterdam Airport Schipol on Monday 27th November 2017.

The morning sessions looked at VAT and recent ECJ cases whilst in the afternoon, after a brief on the new BKR Employment Tax Practice Group, the session went into the round table discussion with a special piece on BREXIT.

Delegates from around the region

After Petra's welcome, Alan Pearce (Blick Rothenberg London), David Dana (Exponens, Paris) and Petra Owen went over 'registration obligations and VAT accounting treatment when trading in another EU Member State', which was then followed by Helen Cowley (Assons, Manchester), Stephanie Thomas (WWS, Mönchengladbach), René Peeters (Flynth, Arnhem), Marco Borioli/Giorgio Colombo (Ditrag, Milan) and Alain Forestier (Exponens, Paris) who all presented on recent European Court of Justice cases that affected their jurisdictions.

After lunch Petra Owen and Tim Morris (BKR) updated the delegates on the new BKR Employment Tax Practice Group. The rest of the afternoon was spent on the round table which gave delegates the opportunity to brief others on changes in their jurisdictions. However it was started with an update by Alan Pierce on the BREXIT situation, which led to some lively discussion and some 'crystal ball gazing' given the lack of concrete detail available at the time – one wonders if the 2018 Tax meeting will have more BREXIT detail!

Yet again the meeting gave members the opportunity to discuss tax issues in an informal professional atmosphere that allowed BKR EMEA tax experts to improve their knowledge and build up their contact base around the region.

The presentations, agenda and list of attendees are now available in the member's area at Tax Meeting 2017. If you have any questions on the 2017 Tax meeting or Future Leaders meeting, please contact Tim Morris or Nikki Papadopoulos.

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Revolution of Taxscape In India!

The article below is from BKR member firm KC Mehta & Co.

"Change is hard at first, messy in the middle and gorgeous at the end" (Robin Sharma)

A quote that perfectly describes the current situation of the Indian tax and regulatory environment. For the past few years, India has been in news, albeit for good reasons. India has emerged as one of the most favoured destinations for foreign investment in recent years. This is a clear indicator of the trust that business communities from across the world have bestowed upon India. India's selection as a spot for foreign investment was a no brainer considering the enormous amount of young and skilled workforce and the humongous customer base that India offers. However, the growth was limited considering the scepticism that prevailed in the minds of investors in terms of the ever-changing tax and regulatory environment, at times, creating a negative

Revolution of Taxscape In India! (contd.)

perception. Plus a host of retrospective tax amendments that followed the Vodafone Saga added fuel to the fire. In my opinion, that was an eye opener. An eye opener for both, the investors and the Government. The investors got a feel of what was to follow. The Government, on the other hand, got the bitter taste of criticism from all corners of the profession and industry.

A complete overhaul:
That brought in a change – a much desired change. Over the past four years, Independent India has witnessed, arguably, the biggest tax and regulatory developments in its history. The Company Law was revamped (implementation of Companies Act 2013), the hyped Goods and Services Tax (GST) has been implemented, Indian Accounting Standards (Ind AS) have been introduced which is a move towards internationally accepted accounting methodologies.

International Tax:
On the International Tax front, India has kept pace with the changing times, be it being a signatory to Multilateral Convention to Implement Tax Treaty related measures to prevent BEPS ('MLI') or joining the Multilateral Competent Authority Agreement (MCCA) on Automatic Exchange of Information (AEOI). India has been aggressively renegotiating its tax treaties to pluck the loopholes that led to cases of double non-taxation.

Administrative measures:
Being a part of the system, one can witness the changes being brought about in the administration of tax matters. Tax officers have started conducting Tax audits online, which is a big step towards a paperless tax office (which still is quite distant a goal). Resolution of tax disputes has become the focal point of the Government. Towards this end, the Government has been bringing a lot of clarity on various tax issues which had attracted long drawn litigation, thereby reducing the pendency of cases and also bringing about some kind of consistency on handling of specific issues.

Time to decode:
In November 2017, the Government has set up a new task force to draft a new direct tax legislation which shall provide its comments within six months. It would be interesting to see how the Government would bring in the new law, considering that it scrapped the talked about Direct Taxes Code back in 2015. A revamp of the direct tax legislation could pave way for a lot of advancements which will go well with the changing times and shall factor the nuances of industry which otherwise were being missed out in the old law.

Thoughts…
We are one lucky generation. A generation that is getting to witness a change that will shape the new business-friendly India! What these changes have done is they have kept the business houses on their toes and made the otherwise lazy population of India, more active. Change is definitely difficult, more so when it is impacting, at least 1.32 billion people. Right implementation of the changes along with support from the taxpayers will surely bear fruits for the economy in the long run!

As George Bernard Shaw said, "Progress is impossible without change, and those who cannot change their minds cannot change anything!"

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Benchmarking for Transfer Pricing Purposes

Benchmarking studies are a critical part of any transfer pricing documentation file or policy - such studies are mainly used to determine the arm's length range deemed to provide an estimate of arm's length price. A benchmark can be defined as the search for companies that perform similar activities as the company for which an arm's-length remuneration needs to be determined. A comparability analysis is a comparison of a controlled transaction with an uncontrolled transaction (or transactions). Controlled and uncontrolled transactions are comparable if none of the differences between the transactions could materially affect the factor being examined in the methodology (e.g. price, margin, mark-up, or profit), or if reasonably accurate adjustments can be made to eliminate the material effects of any such differences.

The OECD Transfer Pricing Guidelines provides for these five comparability factors:

- characteristics of goods and services,
- functional and risk analysis,
- contractual terms,
- economic circumstances,
- business strategies.

Benchmarking studies help elicit a range of values, i.e. the so-called arm's length range usually of prices, margins, mark-ups, profits, royalties or interest rates.

Tax administrations across Europe usually scrutinise the following transaction types of: provision of services, manufacture of products, distribution of goods, licensing intellectual property, and financing agreed between related parties. Each transaction has its specifics, and there are several database practitioners and tax administrators take advantage of when performing their benchmarking analyses. One of the most widely used databases for transfer pricing purposes is AMADEUS (owned and published by Bureau van Dijk), which contains comprehensive information on more than 21 million companies across Europe. The scale of this information can determine the arm's length range of margins, mark-ups and profits of service providers, manufacturers and distributors. While better solutions for company financial benchmarking might well be available on the market (esp. Dun & Bradstreet), we are using AMADEUS because it's exclusively used by tax administrators for tax audits.

For royalty rates benchmarking (trademarks, patents, know-how, etc.), several databases exist, with RoyaltyStat, RoyaltySource and ktMINE being market leaders. Having tried all three databases in the past three years, we subscribed for a full subscription to RoyaltyStat with an unlimited number of searches. We adopted this approach because RoyaltyStat contains by far the highest number of licence agreements for benchmarking purposes.

Unlike the benchmarking of profits, mark-ups, profits or royalty rates, for the determination of interest rates to be in accordance with the arm's length principle no benchmarking analysis will be undertaken. An interest rate in any financing transaction cannot be calculated by the comparison of interest rates in similar uncontrolled transactions. As each debtor is unique, risk of default differs from company to company and market to market. Therefore, credit rating analysis have to be undertaken for the determination of interest rates that meet the arm's length standards.

1. AMADEUS (assessing prices, mark-ups, margins or profitability)

Searching for independent comparable entities and their economic analysis is usually performed with the AMADEUS database. AMADEUS (Analyse Major Databases from European Sources) is a database of European companies that includes financial information about more than 21 million European companies, as well as legal form, date of establishment, shareholders, management, scope of business, and additional information. This database is largely used by taxpayers as well as tax administrators when seeking comparable companies to determine transfer prices.
In order to perform a search strategy, at least the following search criteria have to be applied:

- Activity – search is aimed only at companies known to be actively developing their business activities.
- Geographic factors – applied for the region in which the analysed transaction is performed, country of origin, or EU 28 region.
- Relevant market – this search criterion seeks a sample of companies which corresponds to the business activities of the participating entities in the assessed

Benchmarking for Transfer Pricing Purposes (contd.)

transaction, usually via NACE Rev. 2 classification.
Shareholders – it is necessary to exclude those companies from the searched sample which trade with their parent companies.
Subsidiaries – companies from the searched sample which trade with their subsidiaries must also be excluded.
Type of accounts – it is appropriate to select the following parameters in the search strategy: exclude companies with consolidated financial results, exclude companies with no recent financials, and include companies with a limited number of financial indicators.
Quantitative indicators – in this search the criterion of EBIT, turnover, number of employees, etc. may be defined.

Subsequently, a qualitative analysis of the selected sample of companies is conducted via a manual classification in which it is individually reviewed whether each company included in the sample is really mainly engaged in activities in the assessed transaction. After final modification, the market range of hourly rates, mark-ups, margins or profitability are calculated using financial indicators of the final sample of independent comparable companies.

2. RoyaltyStat (assessing licence fees for intellectual property)

RoyaltyStat is the most up-to-date and reliable source of royalty rates extracted from unredacted license agreements. RoyaltyStat's rates are used in transfer pricing, purchase price allocation (PPA), intellectual property valuation, and due diligence connected with litigation, business development, bankruptcy and mergers & acquisitions. RoyaltyStat provides curated data and custom-built tools to determine arm's length royalty rates and profit indicators specified in the OECD Transfer Pricing Guidelines and the United Nations Practical Manual on Transfer Pricing for Developing Countries. With over 17 years of online experience, RoyaltyStat's reliable data extraction helps to support tax audit, planning and contemporaneous documentation.
In order to perform a search strategy, at least the following search criteria have to be applied:
Region – geographic factors are applied for the region in which the intellectual property is granted, usually Europe, Americas, Africa, Asia, Oceania and Worldwide.
Industry / sub-industry – in this step a sample of licence agreements is searched which corresponds to the business activities of the participating entities in the assessed transaction.
Agreement type – in this search step the relevant license agreements are searched, which have the same agreement type as the analysed companies in the assessed transaction, e.g. copyright, franchise, know-how, mineral rights, patents, trademark, tradename, etc.
Royalty base – the sample of license agreements is reduced by implementing the criteria of royalty base, i.e. royalty base calculating royalty rate from factors such as gross profit, manufacturing cost, net profit, net sales, operating profit, per unit, etc.
Related parties – it is necessary to exclude those licence agreements from the searched sample which trade with related parties, i.e. entities with economic, personal or other ties.
License rights – this essential search step includes searched license agreements granting the same rights as in the assessed transaction, e.g. distribution & sales, label & package, lease, manufacture, market, etc.

Additionally, a qualitative analysis of the selected sample of license agreements is performed by means of manual classification in which it is individually reviewed whether each license agreement included in the sample is really mainly engaged in activities in the assessed transaction. After final modification, the market range of license fees of the final sample of independent comparable licence agreements are calculated.

3. Moody's Methodology (assessing interest rates)

Moody's methodology is one of the most reliable ways to assess interest rates for loans, guarantees, and other financial instruments agreed between related parties. Interest rate is defined by the following formula:

Interestrate=riskfreeinterestrate+riskpremium

Risk-free interest rate represents the interest that an investor would expect from a risk-free (so low as to be negligible) investment over a specified period of time. It is usually substituted for a risk-free interest rate respective IBOR (EURIBOR, PRIBOR, LIBOR, etc.) for short-term loans, and government bonds with A+ rating and higher for long-term loans. Please note that

Benchmarking for Transfer Pricing Purposes (contd.)

the maturity date of underlying assets, i.e. IBOR or government bonds, is the same as the maturity of the assessed loan.

To define the risk premium, the first step is to define the debtor's rating and then define the credit loss rate using several of the indicators published by Moody's in "Corporate Default and Recovery Rates". The resulting credit loss rate range is obtained by substituting the probability of obligor default and debt recovery into the following equation:

$$l_i(T)=D'_i(T)\times(1-r'_i(T))$$

A rating may be defined as an "independent evaluation" using a comprehensive analysis of all known risks of the evaluated entity to determine the ability and willingness of the entity to meet all its financial commitments in full. Client ratings are evaluated quantitatively and qualitatively. The rating evaluation considered five individual components that contribute to the final rating score, whereas each of these components comprises several specific criteria or indicators:

- sector (growth in the sector, profitability in the sector, competition in the sector),
- management (management experience, substitutability and succession qualification of management, capabilities and control systems),
- quality of statements and company prospects (quality of financial statements, financial and business planning, competitiveness of the company),
- structure of the balance sheet (current liquidity, debt-equity ratio, equity ratio),
- financial performance (debt service coverage, return on sales, cash flow coverage, return on equity, interest coverage).

The weights assigned to the individual elements produce a score for the individual component, and the weights of the individual components determine the final rating score. Once the final rating score is assessed, the "Corporate Default and Recovery Rates" published by Moody's are used, whereas the default rates of the respective rating grades for the respective period in years represent the probability of the debtor's default. In the event that a company enters into bankruptcy, creditors are entitled to shares in the liquidation balances; thus it is necessary to adjust the credit loss rate by the percentage of recovery rate that is intended in the case of bankruptcy, resp. by the reciprocal value of the recovery rate representing the potential loss of the creditor.

Based on the conducted independent evaluation of the debtor, the final risk premium is assessed based on the above-mentioned formula, i.e. the default rate is multiplied by the reciprocal value of the recovery rate. The sum of the risk-free interest rate and risk premium gives us a market interest rate that shall be applied between related parties.

4. Conclusion

Benchmarking studies, being the most critical part of any transfer pricing documentation, mainly used to determine the arm's length range, may be performed with the use of several databases. Both practitioners and tax administrations across Europe take advantage of the AMADEUS database to determine the arm's length range of margins, mark-ups and profits of service providers, manufacturers and distributors. In the case of determining arm's length principle of royalties for granting the rights to use some intellectual property, the global market provides several databases - with RoyaltyStat being one of the most reliable due to its by far highest number of licence agreements for benchmarking purposes. On the other hand, for the determination of interest rate to be in accordance with the arm's length principle, no benchmarking analysis needs to be undertaken; thus Moody's seems the most reliable and appropriate methodology. By means of this methodology, thanks to the analysis of several specific criteria or indicators the debtor's rating is defined; and once the final debtor's rating score is assessed, the risk premium is calculated using the Corporate Default and Recovery Rates published by Moody's. The interest rate is then calculated as risk-free interest rate plus risk premium.

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SMC Newsletter

Licence Limitation Rule ("Lizenzschranke")

With effect as of 1 January 2018, Germany introduces a new licence limitation rule (Sec. 4j German Income Tax Act). The new law seeks to limit the deduction of licences paid to entities in countries with special preferential regimes (i.e., lower taxation of licence income, so-called "licence boxes", "patent boxes", "IP regimes") which are not BEPS and G20 compliant. According to the new rule, licence payments shall only be partially deductible if

- the corresponding licence income is taxed at a lower rate than the standard tax rate ("preferential regime"),
- licensor and licensee are affiliated persons as defined in Sec. 1 Para. 2 German Foreign Tax Act, and
- the preferential regime does not meet the "nexus approach" requirements of OECD BEPS 2015

Final Reports' Action 5: "Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance".

"Nexus approach" requirement: The "nexus approach" requirement is only fulfilled if the licence payment at the level of the licensor is (i) linked to substantial economic and business activity of the licensor ("substance clause") and (ii) this link has to be included as requirement in the foreign country's preferential regime ("nexus approach"). Only if both criteria are met, the licences payments remain fully deductible.

In the event that the licence limitation rule is applicable, the licence payments will only be partially deductible whereas Germany expects an income taxation of the licensor of at least 25%.

Example: If the licensor has to pay an income tax rate of only 10% for the licence income (this is only 40% of the expected 25%), Germany will only recognise 40% of the licence fees as tax-deductible expenses and the remaining 60% as non-deductible.

If the license income is taxed at a lower tax rate than the general tax rate and if the substance requirements are not fulfilled, Germany will most likely no longer accept a full deductibility of the licence payments.

We would be happy to assist you with a review of the current situation and tax status.

In case of any questions, please do not hesitate to contact us.

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Update from the Netherlands

On 19 September 2017 the Dutch government presented the 2018 Dutch Tax Plan. Most of the proposed measures will apply from 2018. Adjustments can still be made to the proposed measures.

In addition to the Tax Plan, the coalition agreement, published on 10 October 2017, contains several announcements for future fiscal measures. These will largely apply from 2019 onwards. Below the key changes for corporate tax (corporate income tax, dividend withholding tax)

Applicable as per 2018:

Corporate Income Tax

Lower corporate tax rate bracket

The last year announced extension of the lower corporate tax rate bracket will not take place. This means the rate of 20 per cent will remain available for corporate income up to 200.000 euro.

Innovationbox

Income from research and development activities are taxed at a beneficial rate of 5 per cent in the Netherlands under the innovationbox regime. The benefit from the innovationbox is reduced the rate is increased from 5 per cent to 7 per cent.

The sound business motives test

The twofold sound business motives test that may provide evidence to the contrary of base erosion, under which interest deductions are limited, also applies to debts to affiliated companies that are actually debts to third parties. Although the Supreme Court ruled otherwise, it is now explicitly stated that it must nonetheless be shown that there are sound business motives both for the debt and the legal action.

Foreign substantial interest

From now on, a foreign entity holding a substantial interest in a company domiciled in the Netherlands may be treated as a non-resident company subject to (Dutch) corporate income tax if one of its main purposes is to help another to avoid personal income taxation. Any dividend tax withheld may be credited. Foreign corporate income tax liability in respect of a substantial interest may arise both in the event of an artificial construction and in the event of an artificial transaction. In addition, the sound business reasons reflecting economic reality will be worked out in greater detail. This is in accordance with the new dividend withholding tax anti-abuse provision.

Double taxation relief

For the purposes of determining double tax relief available to a fiscal unity, not only intra-group financing costs must be taken into account, but also intra-group user fees such as royalty, rent and lease payments. The profits for purposes of double taxation relief are calculated as if the income of the fiscal unity is not consolidated. Deductibility is based on Dutch law and standards.

Written-down debts

In the case of a fiscal unity, the write-down of a debt payable by an entity that was related to it at any point in time may not be taken into account insofar as it relates to losses incurred by a company included in the fiscal unity.

According to the State Secretary, this measure also applies if the entities are still related.

Liquidation loss rules

When determining the adjusted acquisition price, account is taken of the write-down of a debt payable by the liquidated entity insofar as this relates to losses already incurred within the fiscal unity in order to avoid double loss set-off.

Dividend withholding tax

Holding cooperative

If, in the preceding year, at least 70 per cent of the actual operations of a holding cooperative domiciled in the Netherlands consist of holding activities, such company will have a duty to withhold dividend tax. This refers to qualifying membership rights that, together with the rights of the affiliated other members, entitle the holder to at least 5 per cent of the annual profits or liquidation proceeds.

Withholding exemption

In participation situations within the EU/EEA, a dividend withholding tax exemption may be claimed. This exemption will now also be available to third countries that have entered into a tax treaty or similar arrangement with the Netherlands, and that treaty or arrangement contains a dividend article. There are some

Update from the Netherlands (contd.)

additional tax treaty domicile requirements that must be complied with.

The withholding exemption cannot be claimed if one of the main objectives is the avoidance of the payment of Dutch dividend withholding tax and relevant substance is lacking. Both constructions and transactions may be considered artificial.For intermediate holding companies to have relevant substance it is at least required that sufficient labour costs can be allocated to the intermediate holding function and that the company actually has and uses its own office space.

In accordance with Dutch tax treaty policy, the dividend withholding tax exemption is available for proceeds paid to hybrid entities.

In an amendment it is noted that this measure does not apply in cases where the hybrid entity is a resident of a third state, based on the applicable law of that third state.

Companies imposed with the obligation to withhold dividend withholding tax have a duty to disclose information if an exemption to withhold dividend tax on payments made to a recipient domiciled abroad is claimed when it concerns participation situations. If they fail to comply with this obligation in time, the tax inspector may impose a penalty of an amount not exceeding EUR 5,278.

Overview of fiscal measures Coalition agreement, largely apply from 2019 onwards

Corporate Income Tax

Reduction of CIT rate

The standard corporate income tax rate will be reduced in steps from 25 percent to 21 percent (2019: 24 percent, 2020: 22.5 percent and 2021: 21 percent). The lower basic rate (in 2017 for taxable profit up to EUR 200,000) will decrease by the same steps from 20 percent to 16 percent (2019: 19 percent, 2020: 17.5 percent and 2021: 16 percent). The goal is to encourage companies to do business within the EU and have their HQ in the Netherlands.

Limitation loss compensation

At present, a corporate income tax loss can be carried forward for compensation for nine years. The loss carry-forward period will be limited to six years. The loss carry-back period remains one year.

Limitation of depreciation on buildings

For all buildings, depreciation will be limited to 100 percent of the actual value (according to the Valuation of Immovable Property Act). Currently buildings that are used for a company’s own activities may still be depreciated up to 50 percent of the actual value.

Direct investment in real estate through Dutch investment funds

Dutch investment funds meeting all legal conditions are taxed in the Netherlands at a CIT rate of 0%. At this moment, Dutch investments funds can invest directly in real estate and still have the 0% tax rate. According to the announced measures this should no longer be possible, because of the abolition of the dividend withholding tax.

Dividend withholding tax

Abolition of dividend withholding tax

Dividend withholding tax will be abolished for regular situations. However, the withholding tax will remain applicable for dividend payments in specific cases of abuse. Amongst others this may be the case if dividend payments are made to certain low-tax jurisdictions. Anti-tax avoidance: withholding tax for interest and royalties

At the same time as the abolition of withholding tax on dividends, a new withholding tax on outgoing royalty and interest payments will be introduced in specific cases of abuse. Amongst others this may be the case if interest or royalty payments are made to certain low-tax jurisdictions.

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