Thursday, September 12

Seminar I: Recent developments in international taxation

Chair: Chloe Burnett (Barrister, Selborne Wentworth Chambers, Australia)

Panel Speakers: Ruth Mason (Professor of Law, University of Virginia, United States), Jos Beerepoot (Tax Director, ABN Amro, Netherlands), Dominic Robertson (Tax Partner, Slaughter and May, United Kingdom)

Secretary: David Lewis (Barrister, Selborne Wentworth Chambers, Australia)

Guest Speakers: John Avery Jones (Pump Court Tax Chambers, United Kingdom), Stig Sollund, (Director, Ministry of Finance, Norway), Michael Keen (Deputy Director of Fiscal Affairs, IMF, United States)

The panel deliberations kicked off with **Ms. Ruth Mason** arguing that the unilateral Digital Services Tax (DST) enacted by some European countries could face a legal challenge on the ground that it violates "fundamental freedoms" guaranteed by EU, that it tantamounts to proxy national discrimination and that EU countries can't discriminate against European subsidiaries of American companies. Ms. Ruth also talked about the possibility of a challenge in WTO to the DST, and said in jest that France's 'GAFA' tax leaves nothing to imagination... that it is but an attempt to target companies from 1 country, i.e. United States. She added that taxes like GAFA hit mainly the US MNEs while leaving out domestic companies. On the potential argument by some that a unilateral DST could be seen as being 'extra-territorial' in nature, she opined that so is the US FATCA. She then turned to the controversial provision in the new US tax code - BEAT, and wondered if it violates Article 24 (non-discrimination) or as a few American legal experts have argued, does it fall within the Article 9 (1) exception to non-discrimination?

The panel then discussed several recent case laws from different jurisdictions. The Australian Court verdict in the case of Indian tech co. Satyam (now Tech Mahindra) was cited as an example of countries 'retreating to domestic law.' In this instance, the Court rejected the company's arguments that the treaties should be interpreted in a reciprocal manner (since in India the treaties can't increase the tax burden) and held that in Australia, a treaty can cause imposition of tax and is not solely for 'relieving' purpose.

Guest speaker and veteran tax professional **Mr. John Avery Jones** (who reminisced about the Rotterdam Congress he attended as a delegate exactly 50 years back in 1969) then discussed a UK Court of Appeal decision in the case of a South African resident 'diver' working as an employee in the UK sector and which Article should apply - Business Profits or Income from Employment? The Court of Appeals, by a majority, held that the deeming legislation (an employed diver working in the UK North Sea sector is treated as self-employed for tax only) did change the nature of the income and hence ruled that the same was business profits and not taxable. The dissenting ruling held that the deeming legislation only changed how the income was taxed and categorised the income as one from employment. All the judges though were in agreement that what matters is the nature of income, not how it is taxed.

The panel then did some crystal ball gazing on what 'Arms Length 2.0' would look like, in the context of the following moves that indicated a shift away from the transactional arm's length test:

1. BEAT & GILTI

2. Formulary and profit-split "pillars" proposals

3. BEPS Action Plan 4 on Interest deduction limitation

4. Transfer Pricing of Intra-group loans

Panel chair **Ms. Chloe Burnett** opined that all the measures will have to co-exist and that it is becoming a 'crowded' space. Ms. Ruth Mason called the USA's BEAT and GILTI provisions a result of American dissatisfaction with the results of the traditional Arm's Length method. She also pointed out that US considered a 'per country approach' and finally rejected it, calling it 'complex.' She said in jest *"When Americans say something is complex, better take them for their word."* She then framed a broader question for everyone in attendance, wondering aloud .. *"Is there any limit to how complicated we are going to let international tax get?"* She lamented that international tax is getting difficult to administer and quipped that laws that are difficult to administer, cannot be held accountable politically.

Mr. Dominic Robertson then enlightened the delegates on proposal papers presented by two global corporate giants - Johnson & Johnson and Uber on how to allocate profits among different jurisdictions. He termed the Uber proposal as a 'formulaic Residual Profit Split Method', premised on allowing market jurisdictions to calculate residual Marketing Intangible Profit (MIP). As per the Uber proposal, the residual MIP would be calculated after splitting out:

a) Deemed Routine Profit

b) Product Intangible Profit (formulaic based on level of R&D and IP ammortisations)

c) MIP attributable to DEMPE functions (80% of MIP)

The residual MIP would then be split pro-rate based on revenues, between markets, with a greater than $25 million net revenue of the corporate.

Ms. Chloe Burnett opined that the transactional ALP is 'alive and well' but wondered if in the future it would be reserved for 'Rolls Royce' cases, i.e. only exclusively reserved for the big corporate giants, while all the other small cases would be applied mechanical rules. An audience poll revealed where things may be headed... 2/3 of the delegates who voted, felt that in 10 years time, mechanical rules will be more in vogue and only 34% batted for the future relevance of Transactional Arm's Length Principles . **Mr. Jos Beerepoot** remarked with more than a tinge of sarcasm when he vented his thoughts on the subject of Transfer Pricing, when he said "Transfer Pricing is an art of fooling yourself in the most sensible way..."

On the subject of 'Transparency', Mr. Jos shared with the delegates the recent guidelines issued by the Dutch Banking Regulator "Good Practices Issues", that requires Financial Institutions to determine the 'tax integrity risk' of clients, including risk on tax evasion and tax avoidance. This assessment by the Financial Institutions could lead to them exiting clients. Mr. Jos gave his take on these new regulations, saying that *"if after a couple of years we (Banks) have not exited clients, questions will be asked by regulators on whether all our clients are well behaved."*

An interesting Court ruling also made its way into the transparency discussion, as a Kenya Court, on a petition by Tax Justice Network, struck down the Kenya-Mauritius tax treaty. While the treaty provisions were challenged as being prejudicial to public finances, the Court struck them down on procedural grounds.

Mr. Michael Keen representing the Fiscal Affairs Division at IMS, shared some interesting statistics on profit shifting and tax competition. He felt that the subject of tax competition deserves more discussions and is something to be taken note of. He also weighed in on the digitalization debate, observing that it is emblematic of deeper issues within the international tax system. He quipped, *"No one really agrees where value is created."* On the general assumption that formulary apportionment will be better for developing countries, Mr. Keen stated that IMS study actually shows to the contrary. He also made an observation in passing that many large MNEs appear to have negative residuals (profits). In conclusion, Mr. Keen opined that after decades of immobility, one is now seen plethora of ideas on international tax rules and cautioned that while it may be time for great creativity, one however needs to think through carefully.

D T S & Associates
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DTS & Associates Take:

In today's session, the recent development in international taxation, the discussions revolved around many interesting topics. One of the topics that the panel discussed was recent international tax rulings, like Australian Court ruling in Tech Mahindra. In that case, one of the key arguments rejected by the Australian Court was that 'treaties cannot levy tax.' However, India has a specific law that provides that treaty provisions or domestic tax law, whichever is more beneficial, can apply. Therefore, you can override domestic law and use the treaty in India, but ironically when the same argument was used in Australia, it was rejected by the Court. It is baffling how a developed country like Australia [which is also a member of OECD] can reject a principle laid down OECD itself!

Talking about OECD, they brought in a theoretical discussion on transfer pricing under the garb of arm's length principle (ALP) and 5 different definitions on how to calculate arm's length profit. However, now they are themselves afraid that ALP is not going to work in case of digital economy. Now they are coming up with discounted cash flow and number of other methods like PSM [which is not acceptable to USA]. The PSM itself will lead to a lot of mechanical calculation and as if we are not already in a complex world of international tax, they are making it more complex!