PKF Global

PKF worldwide tax update

MARCH 2023

LOCAL KNOWLEDGE, GLOBAL EXPERTISE

The content of this PKF Worldwide Tax News has been compiled and coordinated by Stefaan De Ceulaer (stefaan.deceulaer@pkf.com) of PKF International. If you have any comments or suggestions please contact Stefaan directly.

Contents

Welcome

In this first quarterly issue for 2023, the PKF Worldwide Tax Update newsletter again brings together notable tax changes and amendments from around the world, with each followed by a PKF commentary which provides further insight and information on the matters discussed. PKF is a global network with 480 offices, operating in over 150 countries across our five regions, and its tax experts specialise in providing high quality tax advisory services to international and domestic organisations in all our markets.

In this issue featured articles include discussions on:

- (EU) VAT updates in France, Italy and the United Arab Emirates
- Case law with international implications in France and Ghana
- Significant personal and corporate income tax changes in Austria, Ecuador, Italy, Namibia, Papua New Guinea, Peru, Puerto Rico, Romania and South Korea
- International tax developments (CFC/thin cap, CbC Reporting, BEPS, MLI, double tax treaties, transfer pricing, etc.) in Chile, Germany, Hong Kong, Hungary, Switzerland, Taiwan, the United Kingdom and the United States.

We trust you find the PKF Worldwide Tax Update for the first quarter of 2023 both informative and interesting and please do contact the PKF tax expert directly (mentioned at the foot of the respective PKF commentary) should you wish to discuss any tax matter further or, alternatively, please contact any PKF firm (by country) at www.pkf.com/pkf-firms.

Austria

Changes to income tax and investment allowance

The year 2023 will bring a wealth of tax changes to Austria. Below you will find an overview of selected legal adjustments.

Corporate income tax

Corporate income tax will be reduced from the current 25% to 24% in calendar year 2023 and from 24% to 23% in calendar year 2024. For balance sheet dates during the year, the period can be proportioned into 12 equal parts; alternatively, interim financial statements can be prepared as of 31 December 2022.

Investment allowance

As a measure to promote the economy, an investment allowance for new assets acquired or manufactured after 31 December 2022 will be deductible as a business expense in addition to depreciation.

The investment allowance amounts to 10% of the acquisition or production costs. It increases to 15% for assets in the field of ecological investments.

The investment allowance can only be claimed for new (unused) tangible assets with a normal depreciation period of at least four years.

No investment allowance is available for assets with separately defined depreciation periods in the law. This mainly concerns buildings and motor vehicles with combustion engines ($CO_2 > 0$ g/km) as well as investments in connection with fossil fuels.

The assessment basis for the investment allowance is limited to EUR 1,000,000 per business year, so that up to EUR 100,000 or a maximum of EUR 150,000 in the case of ecological investments can be claimed as a tax reduction in addition to depreciation.

Income tax

Straight forward progression acted as a creeping tax increase and was abolished from 1 January 2023. The current inflation will increase the limits for the tax rates. In addition, some deductions will be valorised annually in future.

Until now, many employees found themselves in a situation where they had less money available despite wage or salary increases. A salary increase often led to a higher tax rate, so that real purchasing power still decreased.

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PKF Comment

If you believe the above measures may impact your business or require any advice with respect to Austrian taxation, please contact Stephan Rößlhuber at **stephan.roesslhuber@roesslhuber.at** or call **+43 662 84 22 90**.

Chile

International updates: Chile–India tax treaty, advance pricing agreements and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership

- The Chile–India double tax treaty entered into force on 19 October 2022. The treaty generally applies from 1 January 2023 with respect to Chile and from 1 April 2023 with respect to India. The withholding tax rate on dividends, interest, royalties and fees for technical services will be 10%.
- The tax administration has updated the requirements to apply for an APA (advanced pricing agreement) with its Resolution SII EX. No. 114, which was gazetted on 28 November 2022:
  - The APA needs to be lodged through the tax administration's platform;
  - A detailed description of operations between related parties must be provided, which must include market prices or values and the period for which the APA would apply;
  - Supporting documentation and the relevant transfer pricing analysis must be submitted along with the request.
- The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) was signed on 8 March 2018 and entered into force with respect to Chile on 20 February 2023. The CPTPP is a free trade agreement concluded between 11 countries (Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam).

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PKF Comment

If you believe the above measures may impact your business or personal situation or require any advice with respect to Chilean taxation, please contact Antonio Melys Alvarez at **amelys@pkfchile.cl** or call **+56 22650 4332**.

Croatia

Amendments to tax regulations in 2023

Extra Profits Tax Law

Following its adoption by the parliament, the Extra Profits Tax Law was gazetted on 22 December 2022 (No. 151/22) and came into force on 23 December 2022.

Additional corporation tax is levied and paid, in parallel and independently of the corporation tax liability, under the regulation on the taxation of profits and tonnage tax under the regulation governing maritime transport.

Liability to extra profits tax

The taxpayer subjected to the extra profit tax will be liable to corporate tax and tonnage tax if they generate revenues exceeding HRK 300,000,000 during the tax period when they are subject to the extra corporate tax liability (2022). For the purposes of the application of this act, the criterion relating to the level of revenue of HRK 300,000,000 for tax periods starting in 2022 and ending in 2023 shall be determined by applying the fixed conversion rate of the kuna into euro: EUR 1 = HRK 7.53450 (EUR 39,816,842.52).

Tax base

The extra profit tax shall be paid on a determined tax base, which represents the positive difference between the taxable profit of a tax period and the average taxable profit of previous tax periods plus 20%. Previous tax periods are the years 2018, 2019, 2020 and 2021.

The taxable profit of a tax period is determined in accordance with accounting rules as the difference in income and expenses before corporation tax is calculated, increased and reduced in accordance with the rules on the taxation of profits.

Tax rate

The extra corporate tax is paid on a determined tax base at a rate of 33%.

Act on administrative cooperation in the field of taxation

The European Union adopted Council Directive (EU) 2021/514 of 22 March 2021 amending Directive 2011/16/EU on administrative cooperation in the field of taxation (DAC7). The Directive extends the scope of automatic exchange of information to sellers carrying out certain activities through digital platforms.

The Tax Administrative Cooperation Act transposes the provisions of Council Directive (EU) 2021/514 (DAC7) into domestic law. Law No. 2338 was gazetted on 22 December 2022 and entered into force on 1 January 2023.

Platform operators are required to collect and report information to the tax administration on sellers carrying out the following activities for consideration:

1) sale of goods;
2) rental of any kind of transport;
3) personal services; and
4) rental of real estate.

Platform operators are obliged to submit information in only one of the EU Member States. If they fulfil the information requirements in more than one Member State, they can choose the Member State in which they fulfil their obligations. Foreign platform operators carrying out a commercial activity in the EU (not resident for tax purposes, established, not having a place of management or a permanent establishment in one of the Member States) need to register for data reporting purposes in one of the Member States.

VAT Act and ordinance

Solar panels and the application of the 0% rate

The Act stipulates that the supply and installation of solar panels on private dwellings, housing, public and other buildings used for activities in the public interest and the supply and installation of solar panels in the vicinity of such buildings, premises and buildings shall be subject to a 0% VAT rate.

A 0% VAT rate assessment can only be applied to the installation of solar panels after the entry into force of the VAT Act, regardless of when the service is contracted or paid.

Act on the introduction of the euro as the official currency

The Act on the introduction of the euro as the official currency entered into force on 1 January 2023 and with that the euro became legal tender in Croatia.

The amounts mentioned in kuna in legal instruments shall be regarded as amounts into euro subject to the application of the fixed conversion rate and in accordance with the rules for conversion and rounding set out in this Act.

The fixed conversion rate is an irrevocably fixed conversion rate between the euro and the kuna, which has five decimals (EUR 1 = HRK 7.53450).

This Act also introduced a dual reporting obligation (disclosure of the prices of goods, services and other financial statements of value by highlighting them simultaneously in kuna and euro using a fixed conversion rate) ending 12 months after the introduction of the euro, i.e. 31 December 2023.

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PKF Comment

If you believe the above measures may impact your business or require any advice with respect to Croatian taxation, please contact Diana Antičić at **diana.anticic@porezni-savjetnik.com** or call **+385 91 4000 333**.

Ecuador

Various updates on income tax, inheritance tax, VAT and deductibility limits on royalties and technical fees

Unified basic salary for the year 2023

Executive Decree No. 611 established that the monthly unified basic salary for the year 2023 will be USD 450.

Reduction of the tax rate on payments abroad

Executive Decree No. 643 introduced a progressive reduction of the tax rate on payments abroad, as set out in the following table:

Date	Rate
From 1 February 2023	3.75%
From 1 July 2023	3.5%
From 31 December 2023	2%

Reduction of the VAT rate from 12% to 8% on public holidays

Executive Decree No. 544 introduced a reduction in the VAT rate from 12% to 8%, on the provision of services related to tourism activities during the following dates:

Holiday	Dates
Carnival	18–21 February 2023 inclusive
Easter	7–9 April 2023 inclusive
Day of the Dead and Cuenca Independence Day	2–5 November 2023 inclusive

Ranges to determine income tax for individuals, undivided inheritances and on inheritances, legacies and donations for the year 2023

Ranges were established through Resolution No. NAC-DGERCGC22-00000058 to determine income tax, undivided inheritances and on inheritances, legacies and donations for the year 2023, in accordance with the following tables:

Personal and inheritance income tax

Year 2023			
Basic fraction (USD)	Excess up to (USD)	Basic fraction tax (USD)	Surplus fraction tax
0	11,722	-	0%
11,722	14,935	-	5%
14,935	18,666	161	10%
18,666	22,418	534	12%
22,418	32,783	984	15%
32,783	43,147	2,539	20%
43,147	53,512	4,612	25%
53,512	63,876	7,203	30%
63,876	103,644	10,312	35%
103,644	and upwards	24,231	37%

Income tax on income from inheritances, legacies, gifts

Year 2023			
Basic fraction (USD)	Excess up to (USD)	Basic fraction tax (USD)	Surplus fraction tax
0	75,402	-	0%
75,402	150,803	-	5%
150,803	301,607	3,770	10%
301,607	452,442	18,850	15%
452,442	603,266	41,476	20%
603,266	754,069	71,641	25%
754,069	904,852	109,341	30%
904,852	and upwards	154,576	35%

Deductibility limits for expenses related to royalties, technical, administrative and consulting services provided to related parties

Executive Decree No. 586 introduced a deductibility limit for royalties, technical, administrative and consulting services provided to related parties, equivalent to 5% of the total taxable income of the fiscal period, unless the following cases apply:

1) Taxpayers who are in the pre-operational business cycle: 10% of total assets.

2) Taxpayers who are not in a pre-operational cycle and whose sole activity is to provide technical services to independent parties: the deductibility limit will be determined based on the following calculation:

   - Operating sales will be multiplied by 7.5% and operating profit will be subtracted from the resulting amount; and

   - The deductibility limit shall be equal to the annual cumulative value of services and royalties incurred with related parties minus the value resulting from the previous step.

There will be no deductibility limit when the operating margin (operating profit/sales) is equal to or greater than 7.5%.

For cases 1) and 2), the tax administration may be requested to extend the deductibility limit by consulting the valuation of transactions with related parties.

No deductibility limit shall apply where:

1) The party that incurs the cost or expense has an effective tax rate equal to or less than that of its related party that performs the operation.

2) Within a fiscal period, the total number of operations with related parties for this concept does not exceed 20 times the 0% income tax bracket for individuals (USD 234,440 for the year 2023).

If the asset for which royalties are being paid to related parties has belonged to the resident company or permanent establishment in Ecuador for the last 20 years, the aggregate expense will not be deductible.

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PKF Comment

With these measures, the government hopes to improve the dynamics of the Ecuadorian economy, thanks to the increase in sectoral basic wages and the progressive reduction of the rates of certain taxes, either definitively or temporarily at certain stages of the year. Regulatory measures to avoid 'dumping' and tax evasion in operations between related parties aim to safeguard the interests of the country and seek competitiveness in the domestic market by complying with the principles of maximal competition.

If you believe the above may impact your business or require any advice with respect to Ecuadorian taxation, please contact Manuel García at **mgarcia@pkfecuador.com** or call **+593 4 236 7833**.

France

Indirect taxes updates and recent case law

Indirect taxes

Tax point for supplies of goods in case of advance payments

In its 2020 finance bill France aligned its VAT law with the provisions of the EU VAT Directive 2006/112/EC and updated its fiscal doctrine (art. 30, I-8° et III-B, LOI n° 2021-1900 du 30 décembre 2021 de finances pour 2022; BOFIP BOI-VAT-BASE-20-10, para. 65; art. 269, 2-a CGI) with regards to the tax point for supplies of goods in case of advance payments.

From 1 January 2023, VAT is payable and must be accounted for when taxable persons receive advanced payments from their customers prior to the delivery of goods.

Companies that purchase goods and receive advance payment invoices can deduct VAT immediately without waiting for the final invoice. Advance payment invoices must contain the same information as regular VAT invoices. The updated administrative doctrine emphasises that for VAT to become payable in such circumstances, all the relevant elements of the chargeable event, i.e. of the future delivery, must already be known at the time of the prepayment and, in particular, the goods or services must be precisely described. The new rule applies to all prepayments received from 1 January 2023, and consequently to all contracts in force at that date.

Implementation of an optional VAT group regime

Like many other EU Member States, France has transposed an optional VAT group regime into French law in its 2021 finance bill (art. 162, LOI n° 2020-1721 du 29 décembre 2020 de finances pour 2021; art. 256 C CGI). From 1 January 2023, taxable persons established in France and closely linked to each other financially, economically and organisationally may constitute a single taxable person (or VAT group). The objective of the new regime is to simplify the tax management of groups by considering intra-group economic transactions as outside the scope of VAT.

The VAT group receives its own VAT number and submits a single VAT return for the group. The option must be notified to the French tax administration before 31 October for an effective application from 1 January of the following year, for a renewable period of three years.

E-invoicing and e-reporting obligations

The French government has introduced e-invoicing and e-reporting obligations which will gradually enter into force, depending on the size of the company:

- from 1 July 2024, for large companies,
- from 1 January 2025, for companies of intermediary size, and
- from 1 January 2026, for small and medium-sized companies (Ordonnance n° 2021-1190 du 15 septembre 2021).

Electronic invoicing concerns all transactions for the purchase and sale of goods and/or services carried out between companies established in France which are subject to VAT when it comes to domestic transactions (B2B). Transactions with individual customers (B2C) or with foreign operators (companies or individuals) must be transmitted to the tax administration via the e-reporting of transaction data. Foreign companies not established in France may also be subject to the e-reporting obligation, if the transaction is carried out with non-taxable persons (individuals, associations or public persons) or with taxable persons not established in France and the operation is deemed to be located in France and subject to VAT (e.g. intra-community distance sales of goods, sale of goods stored in France, rental of means of transport, provision of services relating to a building in France, provision of certain other services).

One-stop shop for business formalities and the national business register

In accordance with the provisions of articles 1 and 2 of the PACTE law 2019-486 of 22 May 2019, the French government launched a one-stop shop portal for business formalities, https://formalites.entreprises.gouv.fr/.

From January 2023 it is mandatory to use the portal for all formalities in respect of the creation, modification and cessation of activity, as well as the filing of annual accounts (for companies required to do so). Once the company has been created on the portal, its references are recorded in a single register: the national register of companies ('RNE'). The creation of this portal aims to facilitate the administrative procedures of companies which have been complex until now. Foreign companies without an establishment in France must use this portal for their VAT registrations in France.

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PKF Comment

For further information or advice concerning French taxation, please contact Monika Bahm at **monika.bahm@pkf-arsilon.com** or call **+33 4 92 07 53 25**.

Case law

CE 9° et 10° ch. 20 May 2022, No. 444451 Sté Planet: application of the tax treaty applicable between the paying entity of the beneficial owner in the event of interposed companies

The French company Planet had initially signed a contract to distribute fitness programmes with a New Zealand company. It then changed the contractual circuit and signed a contract for distribution of the same programmes with a Belgian company and then with a Maltese company. The sums paid by the French company (which were ultimately described as royalties) thus benefited from an exemption from withholding tax, even though they would have been subject to a withholding tax of 10 % under the France–New Zealand double tax treaty.

The tax authorities questioned the beneficial ownership of the Belgian and Maltese companies and corrected Planet by automatically applying the France–New Zealand double tax treaty, considering that the New Zealand company was the actual recipient of the sums paid by Planet.

The French Supreme Court validates, in principle, the application of the tax treaty binding France to the state of the beneficial owner as long as it is clearly identified. This applies to both the tax administration and the taxpayer. This approach is even more valid for all tax treaties drawn up according to the OECD model and also applies to dividends and interest, since the concept of a beneficial owner is also relevant for the application of the provisions concerning such income.

CE 9°, 10°, ch. 25 April 2022, No. 439859 , Sté Rubis: 209 B anti-abuse rule and freedom of movement of capital

Article 209 B of the French Tax Code provides that, where a company established and liable for corporation tax in France directly or indirectly operates or holds more than 50% of an entity established in a state where it is subject to a preferential tax regime, the beneficiary results of this entity are subject to corporate tax in France.

There are, however, safe harbour clauses, the letter of which differs depending on whether or not the foreign entity is established in a Member State of the EU (artificial arrangement/absence of local activity).

The French Supreme Court considers that this rule is not incompatible with the freedom of movement of capital, but is intended to apply only to those holdings that can exercise a certain influence on the decisions of the subsidiary established outside France – particularly outside the EU – and to determine its activities, even if the French company did not hold a majority of the capital or voting rights.

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PKF Comment

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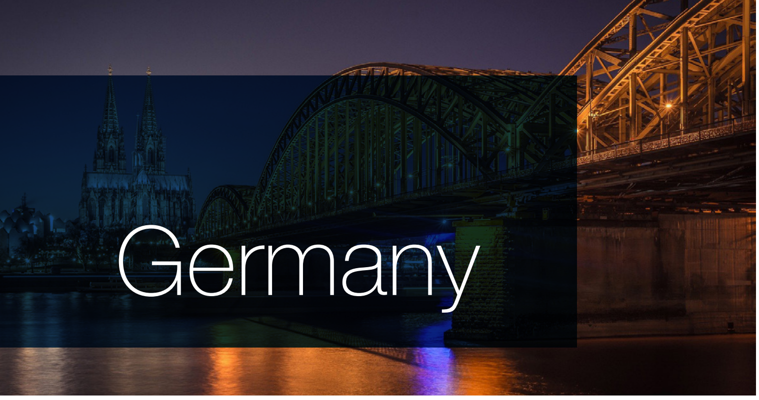

Germany

The global minimum tax from a German perspective

In response to the discussion about fairer taxation of global digital corporations, the OECD has set the goal of creating new tax rules worldwide. The aim of Pillar 1 is to redistribute taxation rights between domicile and market states for all large companies. Pillar 2, on the other hand, calls for minimum taxation for all large companies. The implementation of this Pillar 2 in Germany is discussed below.

1. Principles of CFC taxation vs minimum taxation

For many years, Germany has had specific taxation concerning a controlled foreign company (CFC). If the CFC has passive income and is taxed at a low rate, this foreign passive income of the CFC is subject to German tax at the level of the German parent company. Low taxation is deemed to exist if the effective tax burden of the foreign company under German tax law is less than 25%. By applying this CFC rule, the tax burden of foreign passive income is raised to the German tax burden of around 30%.

In contrast, the new minimum tax is an income inclusion rule (IIR). This rule is not aimed at the taxation of a single company but aims to ensure a minimum taxation of 15% across the board for all companies in a group. IIR applies if a German ultimate parent entity has generated consolidated group sales of at least EUR 750 million in at least two of the four preceding years.

2. Status of implementation of the minimum taxation

In December 2022, the EU Member States reached an agreement on the implementation of the Global Minimum Tax Directive until the end of 2023. It is therefore foreseeable that Germany will transpose the minimum taxation rules into national law with effect from 2024.

3. Application sequence

If there is both passive and active low-taxed income (< 15%) and the group's revenue exceeds EUR 750 million, both regulations generally apply. However, the already implemented national regulations for the taxation of foreign income according to the CFC rule have priority over the IIR regulations.

First, the passive low-taxed foreign income (< 25%) is brought up to the domestic tax level by means of an additional tax in Germany. In a second step, all low-taxed income (< 15%) is covered under the IIR.

4. Double taxation

It will be necessary to observe to what extent the additional taxation will be subject to adjustments, since according to the current implementation status of the IIR, cases will arise in which double taxation occurs due to the parallel application of both regulations.

5. Sanctions

To the extent that a multinational company fails to comply with the obligation to file a tax return on the additional tax in a timely manner or files a false tax return, a fine of 5% of its revenues in the relevant tax year should be imposed under the OECD proposal. Therefore, companies should start looking at the processes for calculating global taxation at an early stage.

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PKF Comment

If you believe any of the above measures may impact your business or require any advice with respect to German taxation, please contact Daniel Scheffbuch at **d.scheffbuch@pkf-wulf.de** or call **+49 711 69 767 238**.

New tax legislation and recent case law

New tax legislation

Three new acts have recently been introduced:

a) Electronic Transfer Levy (Amendment) Act 2022 (Act 1089)

b) Revenue Administration (Amendment) Act 2022 (Act 1086)

c) Value Added Tax (Amendment) (No.2) Act 2022 (Act 1087)

Electronic Transfer Levy (Amendment) Act 2022 (Act 1089)

Provisions made:

1) The levy has been reduced from 1.5% to 1%.

2) Levies collected should be remitted to the Ghana Revenue Authority (GRA) within 24 hours.

3) Returns must be filed. The Commissioner-General will determine the mode of filing.

4) Persons who qualify as agents to collect this levy must be registered with the GRA.

Revenue Administration (Amendment) Act 2022 (Act 1086)

Provisions made:

1) A person who realises an asset must file a separate return.

2) The Commissioner-General has been empowered to establish a monitoring mechanism to verify the actual revenue collected by a taxpayer in other to properly assess tax to be paid.

3) The above clause supersedes confidentiality clauses, privilege and public interest clauses provided for in any other enactment.

4) It imposes a 5% penalty of annual gross revenue on a person who refuses to permit the Commissioner-General or a tax officer physical access to the physical network node or infrastructure or system of that person. This penalty is in addition to any other punitive measures the tax laws provide for.

Value Added Tax (Amendment) (No.2) Act 2022 (Act 1087)

Provisions made:

1) The rate of VAT increased from 12.5% to 15%.

2) It permits the Commissioner-General to determine when a taxable person should use the certified invoicing system (E-VAT).

3) Additional and more punitive administrative penalties have been imposed for non-compliance.

4) Betting, gaming and other games of chance have been removed from the scope of VAT.

5) The exemption from VAT on imported textbooks, imported newspapers, architectural plans and similar plans, drawings, scientific and technical works, periodicals, magazines, trade catalogues, price lists, greeting cards, almanacs, calendars, diaries and stationery and other printed matter has been removed.

Case law: ruling decision

Richard Amo-Hene vs Ghana Revenue Authority, Attorney General Judicial Service

This is a ruling by the Supreme Court of Ghana dated 30 November 2022.

Section 42(5) (b) of the Revenue Administration Act, 2016, Act 915 requires that a person seeking a determination of objection by the Commissioner-General pays 30% of the assessment liability before the objection can be determined. Order 54 Rule 4(1) of the High Court (Civil Proceeding) Rule 2004, (CI 47) also requires that a person seeking to challenge a tax assessment in court must pay 25% of the assessment.

Among other relief the plaintiff sought a declaration of these provisions as inconsistent with the freedoms granted under the 1992 Constitution of Ghana. The apex court declined to grant these reliefs.

Export Finance Company Limited vs Ghana Revenue Authority, Attorney General Judicial Service

The issues for determination are similar to those in the case of Richard Amo-Hene. Here the apex upheld the provision of section 42(5) (b) of the Revenue Administration Act, 2016, Act 915 and Order 54 Rule 4(1) of the High Court (Civil Proceeding) Rule 2004, (CI 47) and declined to grant the relief sought by the plaintiff.

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PKF Comment

If you believe the above measures may impact your business or personal situation or require any advice with respect to Ghanaian taxation, please contact Aisha Gyasi at **aisha.gyasi@pkfghana.com** or call **+233 302 221 216**.

Hong Kong transfer pricing 2023: development trend and deadlines

Development trend

Form IR 1475

Since September 2020, the Hong Kong Inland Revenue Department (IRD) has started issuing Form IR 1475 (‘the Form’) to taxpayers to collect more information regarding transfer pricing documentation. The Form mainly collects the key information contained in the master file and local file in respect of a taxpayer’s related party transactions and transfer pricing policies to facilitate the IRD's preliminary review on the taxpayer’s transfer pricing matters. Upon receipt of further enquiries from the IRD, taxpayers are required to submit the above transfer pricing documentation within one month.

The IRD holds annual meetings with the Hong Kong Institute of Certified Public Accountants (‘the Institute’) to exchange views and discuss areas of concern for taxation matters. In the annual meeting held in 2022, the IRD stated that the Form serves as a tool for the IRD to collect more information to assess the compliance risk of taxpayers from a transfer pricing perspective. Nevertheless, the IRD further indicated that since they have received feedback from taxpayers that the information requested in the Form is too voluminous, the IRD will consider the feedback and may amend or refine the Form where appropriate.

OECD Transfer Pricing Guidelines

The OECD released the latest edition of the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations last year, which mainly reflects a series of revisions and reports released recently in relation to the BEPS (Base Erosion and Profit Shifting) project. In brief, the latest edition has incorporated the following changes and contains relevant amendments to certain other contents of the guidelines mentioned above:

- Changes to incorporate the supplementary guidance to the ‘Guidance on the Transactional Profit Split Method’: this provides a more theoretical basis and case references for the tax authorities and taxpayers when adopting the profit split method.
- Changes to incorporate the ‘Guidance for Tax Administrations on the Application of the Approach to Hard-to-Value Intangibles’: this states the basic principles that tax authorities should follow when assessing intangible assets that are hard to value, and provides case references as well as recommendations on relevant dispute handling and resolution.
- Changes to incorporate the ‘Transfer Pricing Guidance on Financial Transactions’: it was the first time that the OECD had issued such guidance on financial transactions and provided recommendations on relevant transfer pricing matters.

The IRD's approach

As the transfer pricing regulations have been implemented for many years in Hong Kong, it is anticipated that the IRD is going to conduct transfer pricing reviews and audits on taxpayers on a larger scale and on a more regular basis.

Further to the BEPS action plans introduced by the OECD, the IRD and the tax authorities in overseas jurisdictions have become more stringent in reviewing related party transactions and transfer pricing positions of multinational enterprises (MNEs). Even if a Hong Kong entity is exempt from preparing the above master file and local file, it is still required to maintain transfer pricing documents to justify that its inter-company transactions are in line with the arm's-length principle, and the IRD may still request relevant supporting documents and benchmarking results to assess the level of risk of the related party transactions.

Moreover, during the course of issuing enquiry letters to the taxpayers, apart from requesting the taxpayers to provide more information regarding their income or expenses, the IRD may also examine the calculation basis of the income or expenses in relation to related party transactions. Under certain circumstances, the taxpayers may also need to provide supporting documents to justify that the aforesaid calculation basis adheres to the arm's-length principle.

Deadline for transfer pricing documentation

Master file and local file

If your Hong Kong entity carries out a significant amount of cross-border related party transactions, it would be required to prepare the mandatory master file and local file in Hong Kong unless otherwise exempted under the business size test or the related party transaction size test. The deadlines for preparing the master file and local file are as follows:

Deadlines for master file and local file	
Financial year-end date	**Deadline**
Year ended 31 December 2022	30 September 2023
Year ended 31 March 2023	31 December 2023
Year ended 30 June 2023	31 March 2024

An MNE group entity which is carrying on a trade or business in Hong Kong and has engaged in related party transactions will be required to prepare the master file and local file, unless it is eligible for either of the two exemptions as follows:

Business size test	
Total revenue	Not exceeding HKD 400 million
Total assets	Not exceeding HKD 300 million
Number of employees (average)	Not exceeding 100
If an enterprise meets any two of the above conditions (i.e. any two of the 'total revenue', 'total assets' and 'number of employees' are below relevant thresholds) for an accounting period, the enterprise will be wholly exempt from preparing the master file and local file.	

Related party transaction size test (four categories of transactions)	
Transfer of tangible assets	Not exceeding HKD 220 million
Transactions of financial assets	Not exceeding HKD 110 million
Transfer of intangible assets	Not exceeding HKD 110 million
Any other transactions	Not exceeding HKD 44 million
If the total transaction amount under a category is below the relevant threshold for the accounting period, the enterprise will not be required to cover that category of transaction in the local file. If the total transaction amount under each of the categories is below the relevant threshold, the enterprise will be wholly exempt from preparing the master file and local file.	

Please note that the threshold for each type of related party transaction applies to the aggregate amount of the same type of transactions. A related party transaction can be a revenue item or an expense item. Each transaction should be considered separately without setting off each other (e.g. paying HKD 100 interest expense and receiving HKD 150 interest income will be counted as HKD 250). Furthermore, it is the arm's-length amount of the transaction which should be aggregated for determining whether the threshold is exceeded.

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Strategies for handling transfer pricing matters

Taxpayers may be subject to penalties imposed by the IRD if they fail to prepare the above mandatory transfer pricing documentation by the statutory deadlines, or if they (although not required to prepare mandatory transfer pricing documentation) fail to provide supporting documents to show that efforts have been made to review the transfer price of a related party transaction which was found to deviate from the arm's-length principle.

Our transfer pricing and advisory teams are well-positioned to assist you in preparing transfer pricing documentation, reviewing your current commercial relationships and transfer pricing policies and developing tax-efficient strategies for your MNE group.

A key step in transfer pricing analysis is to identify different value chains. Some MNE groups have their functions heavily centralised, and therefore detailed segregation of value chains as well as functions and risks should be performed before further evaluations. In fact, the contents of transfer pricing documentation (including the function and risk analysis, methodologies and rationales) for each relevant entity of the group should have a substantial level of consistency. We assist our clients in performing careful planning on a macroscopic level to properly formulate the function and risk profiles of each entity of the group based on its circumstances and contributions to the relevant value chain. During the course of work, we assist our clients in formulating transfer pricing defence strategies and designing specific transfer pricing documentation on a case-by-case basis. Instead of focusing on the Hong Kong transfer pricing risks only, we place emphasis on how to balance the transfer pricing defence strategy in one jurisdiction with that in the other jurisdiction where the counterparty is located. This would enable our clients to withstand challenges from different tax authorities and cope with the increasing disclosure or information exchange requirements on a global basis.

In addition, depending on specific needs, we can assist our clients in minimising the disclosure of information in the documentation or increase tax efficiency by reallocating the functions and risks to relevant group entities by appropriate arrangements and strategic approaches, while meeting the prevailing compliance requirements.

PKF Comment

Our advantages

Wide range of databases

Different types of databases can be adopted for benchmarking purposes depending on the nature of the transaction, the transfer pricing methodology and the search strategies. The IRD's view is that if the benchmarking studies are based on databases to which the Department has also subscribed, the data can be cross-checked and verified in an efficient manner. That being said, the determination of the database (e.g. Osiris, Orbis, Bloomberg, ktMine, ThomsonReuters, RoyaltyRange) should depend on the actual circumstances. We assist our clients in reviewing the surrounding facts on a case-by-case basis and select the appropriate databases to achieve effectiveness and reliability.

Internal transfer pricing team

We have set up an in-house team dedicated to handling transfer pricing matters to ensure that clients' transfer pricing projects are properly accomplished by our experts with high-quality service deliverables. As our client base covers a wide range of industries (including many listed companies and China state-owned enterprises), we have developed extensive experience in transfer pricing matters.

Cost efficiency

As we have set up an internal team dedicated to handling transfer pricing matters, we have achieved good cost efficiency. In terms of fee level, we can try to provide clients with specific service packages at more ideal prices, and also provide flexible solutions according to different needs. For example, if the MNE's transfer pricing exercise is mainly for internal needs, we will be able to provide a more streamlined transfer pricing summary report; if the MNE would like to merely update a certain part of the transfer pricing analysis, we will also be able to adopt a more result-oriented approach to control the cost.

Flexible service

Our flexible and client-oriented culture allows us to offer a wide range of transfer pricing services depending on our clients' needs. Our services include the following:

- Internal review
  - Review the current transfer pricing policies and perform benchmarking studies to identify the proper pricing or profit level
  - Compare the subject entity's financial data with that of the comparable companies
  - Identify transfer pricing risk and areas for improvement.
- Strategic planning
  - Forward-looking analysis to refine the allocation of functions and risks
  - Enhance tax efficiency based on proper arrangements
  - Design transfer pricing defence strategy on a global basis
  - Assist management to implement and monitor new operating structure and transfer pricing policies.
- Transfer pricing documentation
  - Review the contractual relationships, functions and risks, and underlying operational arrangements
  - Prepare transfer pricing documentation including comparability analysis to substantiate current or proposed transfer pricing strategy
  - Periodic review of transfer pricing policies with a view to keeping them in line with new transfer pricing regulations and industry changes.
- Transfer pricing defence
  - Handle queries raised by the tax authorities
  - Prepare defence file to withstand challenges from the tax authorities
  - Liaise and meet with the tax officers to settle the cases.

For further information concerning the above or any service request with respect to Hong Kong taxation, please contact Jeffrey Lau (Senior Tax Manager) at **jeffreylau@pkf-hk.com** and Henry Fung (Tax Partner) at **henryfung@pkf-hk.com** or call **+852 2806 3822**.

Refined foreign source income exemption (FSIE) regime passed in Hong Kong and now effective

Background

Further to the introduction of the Inland Revenue (Amendment) (Taxation on Specified Foreign-sourced Income) Bill 2022 ('the Bill') into the Legislative Council in October 2022, the Hong Kong SAR government ('HK government') subsequently proposed certain Committee Stage Amendments (CSA) to the Bill based on the comments given by the European Union (EU). The Bill together with the aforesaid amendments were passed by the Legislative Council on 14 December 2022 and the relevant laws came into effect on 1 January 2023.

For details of the FSIE regime, please refer to the tax articles previously published by PKF in Hong Kong and linked here: August 2022 article and November 2022 article.

Key amendments under the CSA

The main purposes of the CSA made to the Bill are to address the concerns raised by the EU and to ensure that Hong Kong is on a level playing field with other jurisdictions with reference to the relevant standard, as well as to avoid Hong Kong being blacklisted by the EU. The key amendments under the CSA are set out below:

- removal of the provision on carving out taxpayers who currently benefit from preferential tax regimes in Hong Kong from the refined FSIE regime;
- the foreign-sourced non-intellectual property (IP) income (i.e. interest, dividends and disposal gains) derived from or incidental to the carrying out of profit-producing activities of the taxpayers as required under the respective preferential tax regimes will fall outside the scope of 'specified foreign-sourced income'; and
- removal of the provision on carving out an 'excluded entity' from the definition of an 'MNE entity'.

The CSA essentially focus on what kind of exclusion will be granted under the refined FSIE regime. The CSA will basically switch the exclusion from an 'entity approach' (which excludes all entities benefiting from relevant preferential tax regimes from the scope of the refined FSIE regime) to an ‘income approach’ (which excludes relevant foreign-sourced interest, dividends or disposal gains derived by taxpayers benefiting from preferential tax regimes from the covered income under the refined FSIE regime). Such carve-out provisions are intended to minimise the compliance burden for taxpayers who are subject to substantial activities requirements under the preferential tax regimes in Hong Kong, which largely overlap with the economic substance requirement of the refined FSIE regime.

Key amendments to participation exemption (for dividends and disposal gains)

On 23 November 2022, after a vigorous exchange of views between the EU and the HK government and having regard to the precedents of other jurisdictions, the EU eventually agreed that the ‘headline rate’ approach (instead of the actual rate of 15%) proposed by the HK government could be adopted under the participation requirement in the refined FSIE regime.

Under the headline rate approach, the applicable rate for the purpose of the ‘subject to tax’ condition for invoking the participation exemption generally refers to the headline rate (i.e. the highest corporate tax rate) of the jurisdiction in which the specified foreign-sourced income, underlying profits or related downstream income is taxed. This headline rate need not be the actual tax rate imposed on the income or profits concerned.

However, if the income is taxable under special tax legislation at a lower rate than in the main legislation, and the lower rate is not a tax incentive for carrying out substantive activities, the headline rate should be the highest stipulated tax rate in the special legislation. If income or profits are subject to the foreign tax at more than one rate (e.g. progressive corporate tax rates), the applicable rate will be the highest corporate tax rate applied to that income.

The adoption of the headline rate approach (instead of the actual rate approach) in determining the applicable rate is generally beneficial to taxpayers. To illustrate, where a covered taxpayer receives foreign-sourced disposal gains in Hong Kong in relation to the sale of equities in a non-Hong Kong jurisdiction, even if such disposal gains have been taxed at a rate lower than the headline tax rate in that jurisdiction (e.g. 10% for direct disposal of equities in a mainland China entity), the ‘subject to tax’ condition may still be met if that jurisdiction has a headline tax rate of 15% or higher.

If an MNE entity satisfies the participation requirement but fails on the ‘subject to tax’ condition in respect of a foreign-sourced dividend or disposal gain received in Hong Kong, the tax relief available in relation to the income concerned will be switched over from full exemption to tax credit. In other words, the MNE entity will remain subject to profits tax in respect of the income concerned but with a deduction from the profits tax of foreign tax paid on the income concerned and underlying profits or income.

BACK

PKF Comment

Despite the amendments made to the Bill based on the EU’s comments, the Hong Kong entities of an MNE group which have no substantial economic activities conducted in Hong Kong and derive foreign-sourced passive income (i.e. interest income, dividends, disposal gains and IP income) are still the main targets of the refined FSIE regime. As the FSIE regime has come into effect from 1 January 2023, it is suggested that taxpayers in Hong Kong should evaluate the impact of the refined FSIE regime on their businesses and, if required, consider taking appropriate planning or restructuring exercises to mitigate the potential tax exposures arising from the refined FSIE regime in Hong Kong.

For further information concerning the above or any service request with respect to Hong Kong taxation, please contact Jeffrey Lau (Senior Tax Manager) at **jeffreylau@pkf-hk.com** and Henry Fung (Tax Partner) at **henryfung@pkf-hk.com** or call **+852 2806 3822.**

Hungary

Amendments to transfer pricing documentation requirements

The Hungarian Ministry of Finance has amended the transfer pricing administrative rules requiring taxpayers that are obliged to prepare transfer pricing documentation to align transfer pricing reporting with the submitting of the annual corporate income tax return.

The decree was published in Official Gazette No. 27/2022 (XII.28.) and the new rules will apply for the first time with respect to 2022 corporate income tax returns that must be submitted by 31 May 2023.

The amending decree lists in detail the information relevant to transfer pricing documentation that must be included in the corporate income tax return:

- the transaction and its sectoral classification;
- name, tax number and state of residence of the associated party;
- net transaction value per associated party;
- taxable base adjustment rate per associated party;
- the transfer pricing method used;
- the applied accounting standard;
- transaction-related indicators;
- the arm's-length price or price range; and
- the price applied in the transaction under consideration.

In addition, similar transactions cannot be aggregated as each transaction requires separate documentation.

Based on current regulations, companies were until now required to prepare transfer pricing documentation by the same deadline as the corporate income tax return, i.e. by 31 May of the year following the tax year. However, they did not have to upload the documentation, or the information contained therein, but only have it ready and available in case of a tax audit.

According to the new regulations, although the whole transfer pricing documentation does not have to be submitted along with the corporate income tax return, the information on almost all relevant elements of the documentation must be provided as an integral part of the tax return.

Furthermore, the transfer pricing documentation threshold has been increased from HUF 50 million to HUF 100 million, i.e. taxpayers must include in the transfer pricing documentation only transactions the arm's-length value of which reaches or exceeds the threshold of HUF 100 million.

BACK

PKF Comment

For further information or advice concerning the above or any advice with respect to Hungarian taxation, please contact Krisztián Vadkerti at **vadkerti.krisztian@pkf.hu** or call **+36 1 391 4220**.

Italy

2023 Budget Law

Italy has gazetted the Budget Law for 2023 enacting several important tax measures.

‘Black list’ cost deductibility regime

Deductibility limits are reintroduced for expenses from transactions with companies or professionals residing or located in countries or territories considered ‘non-cooperative’ for tax purposes.

Identification of ‘non-cooperative’ countries or territories

Non-cooperative countries or territories are considered those identified in the so-called ‘black list’ of the European Union, which currently includes American Samoa, Anguilla, the Bahamas, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, the Turks and Caicos Islands, the US Virgin Islands and Vanuatu.

Limits on the deductibility of costs

As a result of the changes:

- costs that do not exceed the normal value (i.e. which are in line with market amounts) are deductible tout court (without the need to demonstrate the effective economic interest of the operation);
- costs that exceed the normal value are deductible, for the excess, against proof of the effective economic interest of the operation.

Separate report in the tax return and penalty regime

The obligation to separately report costs in the tax return is reintroduced. In the event of omitted or incomplete reporting of the costs, an administrative penalty equal to 10% of the same is provided, with a maximum penalty of EUR 50,000.

Investment management exemption

The so-called ‘investment management exemption’ is introduced into the Italian legal system.

The purpose, common to that of the regulations in force in other legal systems, is to prevent subjects who manage investments in Italy on behalf of funds and other non-resident investors (asset managers) from assuming the status of Italian permanent establishment of such ‘vehicles’.

Tax credit for investments in capital goods

The ‘long’ deadline for making investments in so-called Industry 4.0 tangible assets booked by 31 December 2022 is extended from 30 June 2023 to 30 September 2023.

Communication obligations for sales via electronic interfaces

A specific communication obligation is introduced for VAT taxable subjects who facilitate, through the use of an electronic interface such as a virtual market, a platform, a portal or similar means, the sales of certain movable goods, existing in the territory of the country, towards transferees who are not taxable persons for VAT purposes.

Postponement of ‘plastic tax’ and ‘sugar tax’

A further deferral until 1 January 2024 of the provisions relating to:

- the tax on the consumption of manufactured goods with single use (so-called ‘plastic tax’);
- the tax on the consumption of sweetened soft drinks (so-called ‘sugar tax’).

Tax regime of crypto-assets

The tax regime for crypto-assets was formulated ex novo by the 2023 Budget Law.

A crypto-asset is defined as *‘a digital representation of value or rights that can be transferred or stored electronically, using distributed ledger technology or similar technology’*.

Non-entrepreneurs

The tax regime of crypto-assets for non-entrepreneurs can be found in the new art. 67 paragraph 1 letter c-sexies) of the TUIR (consolidated law on income tax) which includes among other income of a financial nature *‘capital gains and other income realised through repayment or sale for consideration, exchange or holding of crypto-assets, however named’*.

The new art. 67 paragraph 1 letter c-sexies) of the TUIR (consolidated law on income tax) also provides:

- that such income is not subject to taxation if it is less than a total amount of EUR 2,000 during the tax period;
- that in any case the exchange between crypto-assets having the same characteristics and functions does not constitute a fiscally relevant case.

According to the new paragraph 9-bis of art. 68 of the TUIR (consolidated law on income tax):

- capital gains pursuant to art. 67 paragraph 1 letter c-sexies) are calculated on the basis of the difference between the amount received, or the normal value of the assets exchanged, and the cost or purchase value of the same;
- the income from the holding of crypto-assets is calculated on the basis of what is received, without any deductions.

Furthermore, the purchase cost or value, to be documented by the taxpayer, is based on 'certain and specific elements'. In their absence, the cost is zero.

The capital gains and other income referred to in art. 67 paragraph 1 letter c-sexies) of the TUIR (consolidated law on income tax) are subject to the substitute tax of 26% pursuant to art. 5 paragraph 2 of Legislative Decree 461/97.

Option for administered savings and managed savings

For such income, the options for the administered savings and managed savings regimes are expressly permitted.

Entrepreneurs

The 2023 Budget Law included in art. 110 of the TUIR (consolidated law on income tax) a new paragraph 3-bis, pursuant to which, as an exception to the evaluation criteria generally envisaged by the same art. 110, the positive and negative components that result from the valuation of crypto-assets at the end of the tax period do not contribute to create income, regardless of the allocation to the income statement.

The tax irrelevance criterion of crypto-asset valuations also extends to IRAP tax.

Tax monitoring of crypto-assets

With respect to the RW framework, through an amendment to art. 4 paragraph 1 of Legislative Decree 167/90, crypto-assets have been expressly included among the activities subject to reporting.

Reassessment of the value of crypto-assets

For the purposes of calculating the capital gains and losses on crypto-assets referred to in letter c-sexies) of paragraph 1 of art. 67 of the TUIR (consolidated law on income tax) held as at 1 January 2023, the value at that date should be calculated pursuant to art. 9 of the TUIR (consolidated law on income tax), provided that the aforementioned value is subject to a substitute tax of 14% of income taxes.

Objective scope

The optional regime may concern 'each crypto-asset' held and the taxable base of the substitute tax for the recalculation of the value of the crypto-assets is represented by their normal value, determined under the criteria set forth in art. 9 of the TUIR (consolidated law on income tax), as at 1 January 2023.

Payment of the substitute tax

The substitute tax of 14% must be paid, alternatively:

- in a single payment, by 30 June 2023;
- in instalments (i.e. in a maximum of three annual instalments of the same amount, with interest of 3% per annum on the instalments following the initial instalment).

The tax is paid in the manner set forth in chapter III of Legislative Decree 241/97, for which, for example, offsetting with credit amounts is permitted in the F24 form.

Raising the limit for cash transfers

As from 1 January 2023, the limit for the transfer of cash between different parties will no longer be restricted to EUR 1,999.99 (threshold of EUR 2,000), but will increase to EUR 4,999.99 (threshold of EUR 5,000).

BACK

PKF Comment

If you believe any of the above measures may impact your business or personal situation or if you require any advice with respect to Italian taxation, please contact Federica Godoli at **fgodoli@studiogodoli.it** or call **+39 051 232450**.

5% withholding tax on dividends paid out by a UK subsidiary

Post-Brexit a conventional 5% withholding tax applies on dividends paid out to a UK parent company. This is stated in the reply to tax ruling No. 117, dated 20 January 2022, provided by the Revenue Agency on the aforementioned dividends for which the 1.2% withholding tax does not apply.

In the case of distribution of dividends by an Italian company to a company resident in an EU Member State or in a state adhering to the Agreement on the European Economic Area, the reduced 1.2% withholding tax is applied, pursuant to article 27, para. 3b of Presidential Decree No. 600 of 29 September 1973.

However, post-Brexit, this reduced tax does not apply to dividends paid out to a UK parent company, in which case the conventional 5% withholding tax applies.

However, it is clear that the EEA agreement is subject to fulfilment of the other conditions stipulated therein, i.e. that the UK parent company qualifies as a resident person for conventional purposes and is the beneficial owner of the dividends.

BACK

PKF Comment

If you believe the above measure may impact your clients' personal position and need further clarifications or support on this subject, PKF TCL Group's team will be available to provide any additional information you or your clients might need.

You can contact PKF TCL Group Tax Consulting Legal (Stefano Quaglia) at **s.quaglia@pkf-tclsquare.it** or call **+39 02 9285 4246** (Milan office).

VAT treatment in Italy for e-gaming web platforms

In response to a tax ruling submitted by a company holding a virtual platform, a sort of e-gaming arena that we call Beta, in December 2022 the Italian Tax Agency clarified their position about the VAT treatment of this activity.

The platform in question is accessible to anyone interested in e-gaming competitions; users can register and compete for a specific game after paying a single entry fee in Betacoins.

The platform does not release video games to end users but simply helps organise and manage the various challenges through virtual meeting rooms where users can compete to win a jackpot paid in Betacoins.

Based on the tax ruling, the company is not involved in financial and credit activities nor is there a financial investment by the users and the Betacoins do not qualify as a cryptocurrency or crypto-asset, i.e. they are not crypto-coins.

The users are exclusively private individuals located in Italy and abroad (B2C business), they can log in after registration on a free app and are identified by a personal profile. The entry fee in Betacoins is obtained by paying the company in euro at a one-to-one exchange rate. Each user has a personal wallet and the jackpot is paid in Betacoin that can only be reused on the platform to join other competitions or be refunded through the platform.

The game playing service offered by the company is paid by the registration fee paid for each competition and the service for transferring Betacoins or money is free of charge.

The company asked the Tax Agency about the VAT treatment to be applied for the services provided but the reply regarding the remuneration was somewhat ambiguous:

- The currency exchange service is free of charge therefore there is no VAT relevance;
- Regarding the remuneration for the game playing services (the registration fee paid to join each competition), it is not completely clear for the Agency how this activity is carried out.

The Agency also took the opportunity to clarify the VAT treatment of different scenarios pursuant to Article 7 of EU Regulation No. 282 of 2011:

1) The service is provided by the internet or another e-network and is essentially automated, involving minimal human action and cannot be provided in the absence of the information technology;
2) The service, although carried out by electronic devices, requires more than minimal human action.

In the first case it would be an electronic service and according to Article 7-octies of the Italian VAT Law it is possible for the company to pay VAT applying the one-stop shop (OSS) scheme and therefore in relation to the relevance in Italy:

- Payments received by domestic end users, subject to 22% VAT rate; it is mandatory for the company to obtain the end users' tax code and issue the invoice;
- Payments received by EU end users, subject to VAT in accordance with the rules laid down by the country of the end users through the OSS scheme; the company has no obligation to issue an invoice or a receipt;
- Payment received by non-EU end users, no VAT relevance; the company has no obligation to issue an invoice or a receipt.

In the second case the game playing service would be a generic service provision, territorially relevant in Italy according to article 7-ter of the Italian VAT Law: in this case the OSS scheme is not applicable and the company will have to apply the standard Italian 22% VAT rate in addition to the obligation of issuing an invoice that contains the client's tax code.

BACK

PKF Comment

If you believe any of your clients may be interested in the above or should you need further information on the subject, please contact Barbara Pollicina at **b.pollicina@pkf-tclsquare.it** or call **+39 010 81 83 250** (Genoa office).

Mexico tax updates: 2023 economic package, social security law reform and transfer pricing

Economic package 2023

The economic package that was released at the end of 2022 and entered into force in 2023 provides for the following salient features:

- The creation of new taxes is not proposed, nor is the rate increased for existing ones.
- The benefit by tax stimulus in force during 2022 remains in 2023, the accumulation of benefit is maintained when it is applied against income tax.
- Surcharge rate is maintained.
- Increase in the withholding income tax rate applicable to interest payments made by financial institutions. Effective from 1 January 2023, the withholding tax rate charged by financial institutions will increase from 0.08% (rate applicable in 2022) to 0.15%.

Social Security Law reform in force

Entry into force from 1 January 2023 of the reforms approved by the Social Security Law and Savings Systems Law on 16 December 2020.

The reform 'to the pension system' aims at increasing employer contributions for retirement, reducing the number of weeks contributed as a requirement to obtain the guaranteed pension, increasing the value of the minimum guaranteed pension, reducing the commissions charged by the AFORES, among other things.

This reform provides that the increase in employer contributions to the Retirement, Unemployment in Advanced Age and Old Age branch of insurance will rise from the current 3.15% until reaching 11.875% in 2030 based on the employee's salary. It will, however, be implemented gradually starting from 1 January 2023.

Changes in transfer pricing FY2022

As a result of the modifications to the Mexican Income Tax Law and the Mexican Federal Fiscal Code, new transfer pricing obligations are considered in Mexico for the 2022 tax year, which include significant technical changes and modifications to procedures that taxpayers and tax authorities should be aware of:

- **Informative report (Annex 9 of the 'DIM' multiple informative return)**

Increased administrative burden for taxpayers as transactions carried out during the fiscal year 2022 must be reported to the tax authority (*Servicio de Administración Tributaria* (SAT)) through Annex 9 of the DIM, which must include information on all transactions with related parties, now including both local and foreign related parties (articles 179 and 76 section IX). If the information is not reported, is incomplete or contains errors, the taxpayer may be subject to penalties ranging from MXN 86,050 to MXN 172,100.

- **Financial information of comparable operations**

Comparable companies in a transaction must be associated with the fiscal year under analysis. In other words, for the transfer pricing study of 2022, only the financial information of the fiscal year under analysis should be considered; in this case, the fiscal year 2022 for all the companies selected as comparable. This does not apply in cases where taxpayers demonstrate that the commercial market cycle of a product is considered to be more than one year.

- **Interquartile range**

Article 180 of the Income Tax Law in effect for tax year 2022 allowed the use of statistical methods, such as the range of maximum and minimum values. As a result of the modifications made, only the interquartile range can now be used for determining a range of market values.

- **Manufacturing companies**

It is no longer possible for manufacturing companies to request an advance transfer pricing agreement ('APA'). This means that the only option for manufacturing entities to demonstrate their compliance with transfer pricing rules is to apply the safe harbour calculation (article 182 of the Income Tax Law).

BACK

PKF Comment

If you believe any of the above measures may impact your business or personal situation or require any advice with respect to Mexican taxation, please contact Antonio Garcia at **antonio.garcia@pkf.com.mx** or call **+52 (81) 8363 8311** and Jimy Cruz at **jimy.cruz@pkf.com.mx** or call **+52 (33) 3122 2081**.

Amendments to the Income Tax Act

On 29 December 2022, the Namibian Minister of Finance approved and gazetted the Income Tax Amendment Act, which was tabled on 1 November 2022 in the National Assembly and entered into effect on 1 January 2023.

Section	Topic	Amendment (underlined and bold)	Comment
S 15 (9)	Deemed source of income	Section 15 of the Income Tax Act, 1981 (act 24 of 1981) (hereafter referred to as the 'principal Act') is amended by the substitution for introductory sentence of subsection (9) of the following sentence: '(9) Any amount referred to in paragraphs (o) and (q) of the definition of "gross income" is deemed to have been received or accrued from a source within Namibia irrespective of –'	The inclusion of subparagraph (q) into the deemed source section results in the taxation of income received on disposal of a petroleum licence or the right to mine petroleum in Namibia irrespective of: • whether the transaction was concluded in or outside Namibia; • the place where payment was made; or • the place where the funds from which payment was made are held. Paragraph (o), relating to mineral rights and mineral mining, was included as a subsection of the 'gross income' definition and the source of the income was deemed to be from a source in Namibia in terms of the inclusion of paragraph 9 of section 15 with the Amendment Act, Act 15 in 2011. Subparagraph (q) and the inclusion thereof in paragraph (9) of section 15 effectively means that the source of the sale of a petroleum licence or the right to mine petroleum in Namibia will be deemed to be Namibia.
S 17(2)	General deductions allowed in determination of taxable income	Section 17 of the principal Act is amended by: (a) the deletion of subparagraph (i)(w); and (b) the substitution for subsection (2) of the following subsection: '(2) The aggregate of the amounts that may be deducted in terms of paragraphs (n), (q), (qA) and (w) of subsection (1) shall not be, as from the year of assessment commencing on or after [2011] 2022 in any year of assessment exceed the sum of [N$40 000] N$ 150 000'	The substitution of S 2 increases the allowable deductions of contributions made to Namibian registered pension, provident and retirement annuity funds and education policies from the current NAD 40,000 to NAD 150,000. The deletion of S (1)(w)(i) means that the keyman policy contributions made by an employer, in future, need not be included in the taxable income of the employee for it to be deductible by the employer. The amount deductible in respect of keyman policies is also increased to NAD 150,000. The amendment is effective from 1 March 2022 therefore individuals can still utilise the increased deduction in the year of assessment ending 28 February 2023.
S 56	Taxpayer responsible to furnish a return of income and computation of tax payable, and to pay the tax so payable, and the manner of furnishing returns and interim returns	Section 56 of the principal Act is amended by the insertion after subsection (2) of the following subsections: **'(2A) Notwithstanding subsections (1) and (2), a person liable to furnish a return of income pursuant to paragraph (a) of subsection (1) may furnish such return in electronic format and in that case subparagraph (i) of paragraph (a) of subsection (1) shall not apply to that person'**	The insertion allows for filing of tax returns electronically i.e. via ITAS (integrated tax administration system).
S 67	Examination of returns and assessments	S 67 of the principal Act is amended by the substitution for subsection (2) of the following subsection: '2) Upon examination of a taxpayer's return and computation of liability for tax the Minister shall issue to the taxpayer a notice of assessment, **in writing or electronic format**, stating-'	The amendment allows for issuing of assessments electronically i.e. via ITAS (integrated tax administration system) or in writing.
S 81	Accounts and recovery proceedings in respect of certain taxes	Section 81 of the principal Act is amended by the substitution for subsection (4) of the following subsection: '(4) Where, in addition to any amount of tax which is due and payable by any person under this Act, any amount of interest or penalty is payable, any payment made by that person in respect of such tax, interest or penalty which is less than the total amount due shall be dealt with as made – (a) in respect of such tax; (b) to the extent that such payment exceeds the amount of such tax, in respect of such **[penalty] interest**; and (c) to the extent that such payment exceeds the sum of such tax and **[penalty] interest**, in respect of such **[interest] penalty**.'	Based on the 2015 amendment, the application of payment was tax, penalty and interest. The 2022 amendment makes provision for the payment to be applied to payment of tax, then interest and lastly penalties. This amendment will lessen the administrative burden of reallocation of payments where taxpayers submit a request for waiver of penalties. The application of payment will also apply in respect of VAT payments.

S 95A	Determination of taxable income of certain persons in respect of international transactions	Section 95A of the principal Act is amended by the insertion after subsection (3) of the following subsection: '(4) Notwithstanding the provisions of this Act, where a resident company in which any non-resident company or person has an interest of not less than 25 percent of the dividends, profits or capital of the recipient of the financial assistance contemplated in paragraph (c) of the definition of "services" under subsection (1), either alone or together with an associate, and the aggregate of all such financial assistance exceeds the ratio of three-to-one in relation to the fixed capital of the resident company at any time during a year of assessment, a deduction will be disallowed for – (a) any interest paid to the non-resident investor in respect of the financial assistance granted; and (b) any realised currency exchange loss incurred by the resident company during that period on that part of the financial assistance which exceeds the three-to-one ratio. (5) The resident company referred to in subsection (4) may approach the Minister for permission to exceed the ratio stated in subsection (4), and the Minister must consider the circumstances and risks associated with the business of the taxpayer that warrant such a request being acceded to by the Minister.'	This amendment is applicable to interest-bearing inter- company loans and limits the interest deductible by the Namibian subsidiary to the non-resident holding company by quantifying the concept of 'excessive' referred in subsection 3(a). The amendment now determines that if the debt to equity ratio is above 3:1 then the interest paid by a subsidiary to a holding entity whose shareholding or profit share is at least 25% will be limited to a 3:1 ratio and the interest paid on that part of the loan above the 3:1 ratio will not be tax deductible. This amendment is a further attempt to prevent base erosion and profits shifting (BEPS) and thin capitalisation. Provision is made for mitigating circumstances but there is no indication of what the Minister will take into account when considering the application by a taxpayer for a higher ratio.

BACK

PKF Comment

If you believe any of the above measures may impact your business or personal situation or require any advice with respect to Namibian taxation, please contact Lynette Rautenbach at **lr@fcsnam.com** or call **+264 64 215 100**.

Papua New Guinea

Various tax updates – corporate and personal income tax, temporary GST exemption on fuel

Corporate tax

Market concentration levy

A sunset clause has been included for the market concentration levy ('additional company tax') to cease to apply as of 1 January 2023. The transitional provisions have been included to save and preserve any existing action, arbitration or court proceeding challenging the validity of the additional company tax.

The market concentration levy was introduced in 2022 and was imposed on licensed financial institutions and telecommunications companies that dominated more than 40% market share. Flat rates of PGK 190 million and PGK 95 million applied to financial institutions and telecommunications companies respectively for each financial year commencing in 2022 provided they were in a taxable position.

Increase in corporate income tax rate from 30% to 45% on commercial licensed banks

A company that is a financial institution licensed to operate as a commercial bank under the Banks and Financial Institutions Act 2000 will have a new corporate income tax rate increase from 30% to 45% from 1 January 2023.

From 1 January 2023 to 30 June 2023, the banking industry will be consulted by the government to consider whether a different type of tax, such as an additional profits tax, should be applied from 2024 onwards.

Personal income tax

Increase in personal income tax-free threshold from PGK 17,500 to PGK 20,000

The Treasurer announced the increase in the personal income tax-free threshold from PGK 17,500 per annum to PGK 20,000 per annum.

Current income tax-free threshold
From 1 June 2022 to 31 December 2022, the income tax-free threshold was increased from PGK 12,500 per annum to PGK 17,500 per annum. Resident rates from 1 June 2022 to 31 December 2022 are as follows:

Taxable income (PGK)	Tax thereon (PGK)	Rate of tax on excess
17,500	nil	22%
20,000	550	30%
33,000	4,450	35%
70,000	17,400	40%
250,000	89,400	42%

The non-residents tax-free threshold remains unchanged as follows:

Taxable income (PGK)	Tax thereon (PGK)	Rate of tax on excess
nil	nil	22%
20,000	4,400	30%
33,000	8,300	35%
70,000	21,250	40%
250,000	93,250	42%

New income tax-free threshold from 1 January 2023
From 1 January 2023, the income tax-free threshold will be increased to PGK 20,000 per annum to further alleviate the inflationary pressure on the domestic economy caused by global economic shock and its impact on the current rise in domestic prices. Workers earning more than PGK 20,000 per annum will have tax savings of PGK 21.15 per fortnight.

In other words, workers earning up to PGK 20,000 per annum will no longer be subject to tax. Resident rates from 1 January 2023 are as follows:

Taxable income (PGK)	Tax thereon (PGK)	Rate of tax on excess
20,000	nil	30%
33,000	3,900	35%
70,000	16,850	40%
250,000	88,850	42%

The non-residents tax-free threshold remains unchanged as follows:

Taxable income (PGK)	Tax thereon (PGK)	Rate of tax on excess
nil	nil	22%
20,000	4,400	30%
33,000	8,300	35%
70,000	21,250	40%
250,000	93,250	42%

Continuation of excise duty exemption on fuel products for a further six months
In April 2022, a temporary exemption of excise duties on diesel, petrol and zoom products purchased by the public was introduced. This reform came into effect for the period from 1 May 2022 to 31 October 2022; the exemption relief was extended from 1 November 2022 to 31 December 2022.

Further, this measure will be extended for six months in 2023, from 1 January 2023 to 30 June 2023. This means retail prices for diesel, petrol and zoom products will be reduced as follows:

- petrol by 61 toea per litre,
- diesel by 23 toea per litre, and
- zoom by 2 toea per litre.

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PKF Comment

If you believe the above measures may impact your business or require any advice with respect to Papua New Guinean taxation, please contact Thomas Taberia at **thomas.taberia@ktk.com.pg** or call **+675 321 6070**.

Peru

Recent tax developments: R&D tax incentives, tax benefits for real estate investment funds and 2023 tax unit value

- The value of the tax unit for 2023 has been set at PEN 4,950 (Supreme Decree 309-2022-EF, gazetted on 24 December 2022). The tax unit is a reference value used to determine, among others, deductions and the amount of fines in cash and its value is adjusted annually. The value of the tax unit for 2022 was PEN 4,600.
- Tax benefits for real estate investment funds (REIFs) have been extended until 31 December 2026 (entry into force on 1 January 2023). These tax benefits include:
  - deferral of income tax on the sale of real estate held by the REIF;
  - 5% withholding tax rate applicable for income derived from leasing or any other type of transfer of the use of the property; and
  - deferral of real estate transfer tax on the sale of real estate held by the REIF.
- The validity of temporary tax incentives for expenses on scientific research, technological development and technological innovation (R&D expenses) has been extended until 31 December 2025 (entry into force on 1 January 2023).

  In addition, higher deduction rates for R&D expenses were introduced. The deductible amount depends on whether the taxpayer's net income does or does not exceed 2,300 tax units.

  Where an R&D project ends after 31 December 2025, the higher deduction rates for R&D expenses may be extended until 31 December 2027.

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PKF Comment

If you believe the above measures may impact your business or require any advice with respect to Peruvian taxation, please contact Renato Vila at rvila@pkfperu.com or call **+51 142 16 250**.

Poland

Draft act amending the Code of Commercial Companies

Another amendment to the Code of Commercial Companies

On the website of the Government Legislation Centre on 30 November 2022, another version of the draft act ('Draft' or 'Amendment') amending the Code of Commercial Companies and certain other acts was published. As an introduction, it should be noted that the Amendment focuses primarily on the processes of mergers, transformations and divisions of companies and is the next stage of the implementation of the so-called company law package, which includes Directive 2019/2121 of the European Parliament and of the Council of 27 November 2019 amending Directive (EU) 2017/1132 regarding cross-border conversions, mergers and divisions (OJ L 321 of 12 December 2019) ('Directive 2019/2121').

Pursuant to Directive 2019/2121, Poland should adopt the analysed provisions by 31 January 2023, but it should be emphasised that the Draft, as at 30 January 2023, has not yet been adopted by the Council of Ministers, so it should be assumed that this deadline will not be met.

Changes in cross-border processes

Among the changes, the Amendment includes introducing regulations into the Polish legal system that will enable companies to participate in two new cross-border processes: a cross-border division and a cross-border transformation (under the current regulations, only a cross-border merger is possible). The planned changes will contribute significantly to facilitating the expansion of companies outside the domestic market.

The Draft provides that a cross-border division may be carried out by transferring the assets of the divided company to the newly formed company or companies (proposed art. 5505 of the Code of Commercial Companies). A certificate of compliance of the cross-border division with national law will be required. What is important here is that until such a certificate has been received, the cross-border division will be subject to the law of the country of the company being divided, and after the certificate has been received, it will be subject to the law of the country of its registered office for each of the newly formed companies. Directive 2019/2121 imposed the obligation to implement this type of procedure on all members of the European Union. According to the Amendment, a new type of connection will also be introduced – connection by separation, which will be discussed hereafter.

The proposed changes also provide for the possibility of transforming a capital company and a limited joint-stock partnership into a foreign company listed in Annex II to Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017, subject to the law of an EU Member State or a state party to the EEA Agreement and having its registered office, central administration or main establishment in the EU or a country party to the EEA Agreement, with the simultaneous transfer of at least the registered office to that country. It is worth highlighting that according to the proposed changes, a cross-border transformation will not require liquidation proceedings.

Reorganisations of companies

The Draft provides that the provisions of the Code of Commercial Companies will also introduce other changes regarding the reorganisation of companies including, above all, two new reorganisation processes, i.e. simplified mergers of companies and a new type of division of companies – division by spin-off.

As noted above, a new type of simplified merger of companies is due to be introduced into national regulations. Directive 2019/2121 obliges Member States to introduce a new type of cross-border merger (the new type of company merger will also apply to domestic processes), whereby one or more companies transfer all their assets and liabilities upon dissolution without going into liquidation to another existing company – the acquiring company – without the need to issue new shares or establish new shares by the acquiring company, provided that:

- one person holds, directly or indirectly, all the shares or stocks of the merging companies; or
- shareholders of the merging companies hold their securities and shares in the same proportion in all merging companies.

The proposed new type of merger achieves simplification as there would be no requirement to issue new shares, due to the identity of the shareholder or shareholders in the merging companies and the same proportion of capital involvement in the merging companies. The absence of an issue of shares on such mergers is justified by the fact that, as a result of this type of merger, the shareholding relationships remain unchanged.

One of the biggest changes to be introduced to the Code of Commercial Companies is also the addition to the Polish legal system of a new concept of division of companies, i.e. division by separation. The new type of breakdown will apply to both cross-border and domestic operations.

Currently, under Polish law, there exists a partial division of a company (the so-called division by spin-off), which involves transferring part of the assets of the divided company to an existing company or to a newly established company, but in this case the shares or stocks are taken over by the shareholders of the divided company, and the new type of division provides for them being taken over by the divided company. In a division by spin-off, the shareholders of the divided company do not automatically become shareholders of the acquiring company, as the shares will be acquired by the divided company, and not by its shareholders.

The definition of the new possibility of dividing the company is to be included in the draft art. 529 § 1 item 5 of the Commercial Companies Code, which states that the division of the company may be carried out ‘by transferring part of the assets of the divided company to an existing or newly formed company or companies for shares in the company or companies taking over or newly formed, which include the divided company (division by separation)’.

Limited joint-stock partnership in reorganisation processes

Referring to a limited joint-stock partnership, in the context of cross-border mergers regulated so far, art. 491 § 11 of the Code of Commercial Companies and art. 528 § 2 of the Code of Commercial Companies provide for restrictions that this company cannot be the acquiring company or a newly established company in the process of merging companies, and that a partnership cannot be subject to division.

The Amendment is to grant a limited joint-stock partnership full merging and division capacity by specifying that a limited joint-stock partnership will be able to be the acquiring company or a newly established company both in the process of domestic and cross-border mergers of companies (proposed art. 491 of the Commercial Companies Code) and by specifying that ‘a partnership other than a limited joint-stock partnership is not subject to division’ (proposed art. 528 § 2 of the Code of Commercial Companies).

Creditor protection

The Amendment aims to introduce measures to facilitate the protection of creditors of companies participating in reorganisation processes. The main method of protecting creditors of a domestic company is to be able to submit a request, within one month from the date of disclosure or access to the cross-border merger plan, to secure their claims that have not become due at the time of disclosure or access to this plan. Creditors should demonstrate that the satisfaction of their claims is jeopardised by the merger. In the event of a dispute, the court competent for the registered office of the merging, divided or transformed company is to decide on securing the creditor's claims. It should be emphasised, however, that obtaining collateral will depend on the effectiveness of a given cross-border operation.

Partner protection

The main instrument specified in Directive 2019/2121 to protect shareholders voting against a given cross-border operation is the right to exit the company and receive remuneration for their shares with a value equal to the market value of their shares, as estimated by an independent expert. Similar provisions are already in force in the Polish legal system. The Amendment provides only for the extension of the protective provisions to shareholders of non-voting shares and shareholders unreasonably prevented from participating in the shareholders' meeting or the general meeting in the matter of adopting a resolution on a cross-border merger.

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Checking the legality of a given cross-border operation

As part of the Amendment, ensuring the legality of cross-border operations is to undergo a significant change, with the new practice of issuing a certificate of compliance of such an operation with Polish law, which has so far been in force on the basis of cross-border mergers. The scope of the examination aimed at issuing a certificate of legality of a given cross-border operation will be extended to include issues related to the assessment of whether a given cross-border operation is carried out for the purpose of committing abuse or fraud resulting in or intended to evade or circumvent EU or national law or for other criminal purposes.

In addition, as indicated in the explanatory memorandum to the Draft, it is specified that 'the competent authority may consider the fact that the cross-border operation would lead to the company's place of actual management or business activity being in the Member State where the company or companies are to be registered after the cross-border operation, as indicating the absence of circumstances leading to abuse or fraud'. This is a significant facilitation for companies wishing to participate in reorganisation processes with companies from European Union countries.

Under the current legal status, the registry court was the authority competent to issue a certificate of legality of a given cross-border operation. However, due to the extension of the scope of the examination of the compliance of a given cross-border operation related to the abuse clause, this inspection is to be of an interdisciplinary nature (registration, tax, employee, criminal matters), which 'encourages involvement in the procedure of issuing a certificate of compliance with the cross-border operations law also of other specialised bodies' (for example, the opinion of the Head of the National Revenue Administration including assessment of the tax consequences of the cross-border merger from the perspective of the provisions regulating the anti-tax avoidance clause).

PKF Comment

The analysed Amendment serves not only to implement EU regulations on cross-border divisions and transformations, but also provides for significant changes in national regulations. The changes should be assessed as revolutionary for both the Polish and international markets. Adoption of the provisions of the Draft, on the one hand, will prolong the procedure of cross-border reorganisations, for example due to the need to obtain the opinion of the Head of the National Revenue Administration, which will be tantamount to assigning a greater role to the justification prepared by the company regarding the reorganisation and the analyses carried out in terms of transfer pricing, but at the same time it will increase the protection of interested entities and legal stability in this area. Despite the delay in the adoption of the Amendment, the entry into force of the Amendment is certain, as it is an obligation imposed on the Member States of the European Union.

If you believe the above measures may impact your business or require any advice with respect to Polish taxation, please contact Agnieszka Chamera at **agnieszka.chamera@pkfpolska.pl** or call **+48 609 331 330**.

Puerto Rico

Key amendments to the Puerto Rico Internal Revenue Code under the Puerto Rico Public Finance Stabilisation Act

On 30 June 2022, Act No. 52-2022, known as the Puerto Rico Public Finance Stabilisation Act, was enacted with various new provisions and amendments to Puerto Rico's local tax and incentives laws. These new provisions and amendments were effective upon enactment, unless otherwise indicated.

We hereby highlight some of the provisions enacted in Act No. 52-2022 affecting the Puerto Rico Internal Revenue Code ('PR Code') for income taxes.

Remote worker provisions

In response to the post-pandemic work environment, Act No. 52-2022 adopted the following tax rules for 'remote employees' residing in Puerto Rico and their foreign employers:

- The 'engaged in trade or business' definition in section 1010.01(a)(40) of the PR Code was amended for taxable years beginning after 31 December 2021, to exclude foreign employers that have 'remote workers' in Puerto Rico, if the foreign employer: (i) at no time during the taxable year has an office or other fixed place of business in Puerto Rico; (ii) at no time has an economic nexus with Puerto Rico (a foreign employer will not be considered to have an economic nexus with Puerto Rico even if the remote worker's home office is necessary for or a condition of employment); (iii) is not considered a merchant, pursuant to section 4010.01 of the PR Code; (iv) the remote worker is not an officer, director or majority shareholder of the foreign employer; and (v) the foreign employer reports the income paid to the remote worker on Federal Form W-2 or on Form 499R-2/W-2PR.
- Remote employees will be required to make estimated tax payments on salary payments received from their foreign employers.
- The 'foreign tax credit' rules were amended to allow 'remote workers' residing in Puerto Rico to credit in Puerto Rico the contributions paid to the US or to another state, in those cases where a state's sourcing rules impose tax on this income.
- Foreign employers are not required to withhold Puerto Rican income tax on payments to remote workers residing in Puerto Rico.

Disregarded entities

Act No. 52-2022 added section 1010.01(a)(41) to the PR Code to introduce into our tax system the concept of 'disregarded entities', already used in other countries. Under this new section, a 'disregarded entity' will be ignored as a separate entity from its owner for the purposes of computing the income tax provided for in subtitle A of the PR Code.

Accordingly, the owner of a disregarded entity will recognise the disregarded entity's income in their personal income tax return as if the disregarded entity did not exist.

On 21 November 2022, the Puerto Rico Department of Treasury issued Administrative Determination 22-10 ('AD 22-10'), in which it clarified that disregarded entities will need to comply with the following provisions (under the disregarded entity's employer identification number): (i) filing of withholding vouchers in accordance with the provisions of section 1062.01 of the PR Code; (ii) filing informative returns in accordance with the provisions of section 1063.01 of the PR Code; (iii) registration in the Merchant's Registry pursuant to section 4060.01 of the PR Code; and (iv) the collection and remission of the sales and use tax, in accordance with Subtitles D and DDD of the PR Code, among others.

Pass-through entities

Among the new provisions enacted by Act No. 52-2022, section 1010.01(a)(43) was added to the PR Code to define the new 'pass-through entity' tax election, which incorporates in its definition 'corporations'.

Under the new definition, a 'pass-through entity' is an entity organised under the Puerto Rico General Corporations Act, the laws of the US or of a foreign country whose income and expenses is attributed to its owners for income tax purposes. Any corporation, partnership or limited liability company may choose to pay taxes as a pass-through entity even if they only have one owner.

A new subchapter H was added to chapter 7 of subtitle A of the PR Code, which, in general terms, subjects 'pass-through entities' to the taxation regime for partnerships under the PR Code.

An existing corporation wishing to elect for 'pass-through entity' status will be deemed to have transferred its assets and liabilities to its owners in a corporate liquidation under the PR Code, and immediately thereafter, the owners will be deemed to have contributed these assets to the 'new' pass-through entity.

On 21 November 2022, the Puerto Rico Department of Treasury issued AD 22-10 with the purpose of: (i) clarifying the default tax treatment of legal entities in Puerto Rico; (ii) establishing the tax treatment of entities that for taxable year 2021 were taxed as partnerships, special partnerships or corporations of individuals; (iii) establishing the rules for electing to be taxed as a pass-through entity or disregarded entity and the tax effect of such conversions; and (iv) determining the taxable year of pass-through entities, among other matters.

Foreign limited liability companies

Act No. 52-2022, amended section 1010.01(a)(3) of the PR Code to clarify that for tax years beginning 31 December 2022, if a foreign limited liability company, for reasons of an election or provision of law or regulation under the US Internal Revenue Code, or analogous provision of a foreign country, is treated as a partnership, disregarded entity or entity whose income and expenses are attributed to its members for reporting US or foreign country income taxes, the foreign limited liability company will be treated as a pass-through entity subject to subchapter H of chapter 7 of subtitle A of the PR Code, or as a disregarded entity if it only has one member, and will not be eligible to be taxed as a corporation.

Capital gain sourcing

Act No. 52-2022, amended section 1035.03 of the PR Code to clarify that in the case of a sale of capital assets acquired by an individual before becoming a resident of Puerto Rico, the portion of the capital gain (but not loss) that is related to the appreciation of such assets while the individual lived outside of Puerto Rico and up to the date of becoming a resident of Puerto Rico, will be considered income from sources outside of Puerto Rico.

Foreign financial bank accounts

Among the new provisions enacted by Act No. 52-2022, section 1061.25 was added to the PR Code, to require every individual resident of Puerto Rico under penalty of perjury, to file alongside their individual income tax return a new declaration for financial accounts whose value exceeds USD 10,000 maintained outside of Puerto Rico or the US in which the taxpayer maintains a financial interest.

A taxpayer will have a 'financial interest' in a financial account if: (i) the taxpayer is the record owner of the account; (ii) the record owner is an agent, attorney or any other person acting on the taxpayer's behalf; (iii) the owner of record is a legal entity in which the individual has, directly or indirectly, at least 50% of the total shares or participation by vote or value; (iv) the record owner is a trust for the benefit of the grantor ('grantor trust') and the grantor is the taxpayer; or (v) the taxpayer has authority (individually or with others) to control the disposition of assets held in such an account.

For these purposes 'financial accounts' include: (i) bank accounts, such as savings accounts, checking accounts and term deposit accounts; (ii) securities accounts, such as managed and derivative accounts or other financial instrument accounts; (iii) options or futures contract accounts; and (iv) active crypto accounts.

This new declaration will require disclosure of the following information: (i) name of the institution where the financial account is maintained; (ii) maximum value in the account during the year; (iii) account number; and (iv) any other information that the Secretary determines through regulations. Taxpayers could comply if they submit to the Puerto Rico Department of Treasury their FinCEN Form 114, Report of Foreign Bank and Financial Accounts

(FBAR) filed to the US Internal Revenue Service for the relevant taxable year.

A new USD 10,000 penalty was added to section 6030.11 of the PR Code for taxpayers who do not comply with this new filing requirement.

Sale of partnership interest

Act No. 52-2022 amended section 1035.08 of the PR Code to state that for taxable years after 30 June 2022, any gain derived by a foreign corporation or non-resident foreign individual from the sale, directly or indirectly, of an interest in a company that is dedicated to an industry or business in Puerto Rico, will effectively constitute connected income related to the exploitation of trade or business in Puerto Rico.

The gain will be an amount equal to the foreign corporation's or non-resident alien individual's distributable share on the gain that the partnership would have generated if the partnership had sold all of its assets at their market value on the date of sale of the interest in the partnership by the foreign corporation or non-resident foreign individual.

The buyer will be required to withhold at source 15% on this gain.

BACK

PKF Comment

If you believe the above measures may impact your business or require any advice with respect to Puerto Rican taxation, please contact Edwin Torres at **etorres@pkfpuertorico.com** or call **+1-787-400-9548**.

Romania

Various tax updates

1. Changes regarding micro-enterprise income tax

The condition regarding the revenue threshold (EUR 500,000 instead of EUR 1,000,000) becomes effective starting with the income of 2023.

In the event that, during a fiscal year, a micro-enterprise achieves revenues greater than EUR 500,000 or the share of income from consulting and/or management, with the exception of revenues from fiscal consulting, corresponding to CAEN code: 6920 ('Accounting, bookkeeping and auditing activities; tax consultancy'), if the total income is over 20% inclusive, it becomes liable for profit tax starting with the quarter in which any of these limits was exceeded.

Starting from 1 January 2023, companies that make more than 20% of their income from consulting and management activities, with the exception of income from tax consulting, corresponding to CAEN code: 6920 ('Accounting, bookkeeping and auditing activities; tax consultancy'), are removed from the category of micro-enterprises.

2. Changes regarding income tax

If dividends are distributed based on the interim financial statements prepared during the financial year 2022, the dividend tax rate is 5%, without the recalculation of the tax on the respective dividends after their regularisation based on the annual financial statements for the financial year 2022.

In order to grant tax facilities to the construction industry, the share of the turnover achieved as a result of construction activities in the total turnover needs to be taken into account. Income resulting from construction activities performed outside Romania will no longer be taken into account.

For financial year 2023, the annual tax due by taxpayers who realise income from the grant of the use of goods (other than those for which the annual net income is determined under the real system), leasing and from rental for tourist purposes of rooms located in their properties, such as by those who earn income from intellectual property rights for which the annual net income is determined according to the provisions of art. 72.1, is established by applying a 10% rate to the taxable income or taxable annual net income, as applicable.

3. Changes regarding profit tax

As a supplementary deduction for CIT purposes, companies can benefit from an additional deduction of 50% of the eligible expenses for their research and development and/or experimental development activities (not technological).

4. Changes regarding the introduction of modern payment systems

Merchants who register cash receipts with a value greater than RON 50,000 annually have to accept payments with debit/credit or prepaid cards, through a point of sale (POS) terminal and/or other modern acceptance solutions, including applications that facilitate the acceptance of electronic payments.

It is also regulated that any operation that does not constitute a delivery of goods is included in the category of services for which the obligation to provide POS applies (in case of exceeding the threshold on cash payments).

5. Changes regarding salaries

Starting from 1 January 2023, the minimum gross wage has been increased from RON 2,550 to RON 3,000 per month, and the level of the average gross salary used to establish the social insurance budget was increased to RON 6,789.

In the period from 1 January 2023 to 31 December 2028, in the construction industry, the minimum gross basic salary guaranteed in payment will be at least RON 4,000 per month.

From 1 January 2023 to 31 December 2023, an amount of RON 200 per month is treated as non-taxable for employees with a full-time employment contract and monthly income below RON 4,000.

BACK

PKF Comment

If you believe the above measures may impact your business or personal situation, or require any advice with respect to Romanian taxation, please contact Carmen Mataragiu at **carmen.mataragiu@pkf.ro** or call **+40 744 534 721** or **+40 741 228 003**.

South Korea

Amendments to the Corporate Tax Act

The following amendments to the Corporate Tax Act have been made in order to enhance economic vitality: the corporate tax rate is adjusted, the maximum deductible amount for losses carried forward for corporations other than small and medium enterprises is raised and the exemption from the interim tax prepayment obligations is expanded. These amendments have become effective from 1 January 2023.

Adjustment of corporate tax rates (Corporate Tax Act article 55)

The tax rate applied to the corporate tax base section shall be reduced by 1% for each income bracket. The reason is to enhance economic vitality through reducing the corporate tax burden with the adjustment of the corporate tax rate.

With the reduction, the highest rate will come down from 25% to 24%.

Tax base (KRW million)	Previous CIT rates	CIT rates effective from 2023
up to 200	10%	9%
200 to 20,000	20%	19%
20,000 to 300,000	22%	21%
over 300,000	25%	24%

Expansion of the maximum deductible amount for losses carried forward (Corporate Tax Act article 13, article 45, article 46 - 4, article 76 - 13, article 91)

With a view to equity with small and medium enterprises that can deduct losses carried forward up to 100% of their business year's income, the maximum deductible amount for losses carried forward for general corporations, consolidated corporations, merging corporations, divided corporations and foreign corporations other than small and medium enterprises shall be raised from 60% of the income for each business year to 80% of the income for each business year.

Expansion of the exemption from the interim tax prepayment obligations (Corporate Tax Act article 63)

The standard tax amount for corporations exempted from the obligation to pay corporate tax for the interim prepayment period will be raised from KRW 300,000 to KRW 500,000. It promotes the convenience of tax payments for small and medium enterprises by expanding the scope of exemption from the obligation of interim prepayments.

BACK

PKF Comment

If you believe the above measures may impact your business or personal situation or require any advice with respect to South Korean taxation, please contact Jooil Park at **jooil.park@shcgr.kr** or call **+82 2 3011 1173**.

Spain

New tax on non-reusable plastic packaging

On 1 January 2023, the new excise duty on non-reusable plastic packaging regulated in Chapter I of Title VII of Law 7/2022 on Waste and Contaminated Soils for a Circular Economy entered into force.

This new indirect tax is levied on the use on Spanish territory of non-reusable packaging containing plastic, whether it is empty or whether it is presented containing, protecting, handling, distributing or presenting goods. Deliveries of non-reusable plastic packaging by domestic manufacturers will be subject to the tax, as well as foreign acquisitions of goods containing such packaging (i.e. imports, EU intra-community acquisitions and transfers).

Briefly summarised, these would be the salient features and obligations regarding the tax to be taken into consideration.

Subject of this tax:

- The manufacture or production, importation or intra-community acquisition of non-reusable packaging containing plastic.

Who is required to register in the tax census:

- Manufacturers and intra-community acquirers. Importers do not have to register.

Taxable base and tax rate:

- Taxable base: kilograms of non-recycled plastic contained in non-reusable packaging.
- Exemption up to 5 kg per month for imports and intra-community acquisitions (separately).
- Rate: 0.45 EUR/kg of non-recycled plastic.

Payment and tax refund:

- Intra-community manufacturers and purchasers: self-assessment using form 592. The filing deadline is the same as that for VAT: quarterly/monthly.
- Importers: payment is managed at the customs office.
- Importers and acquirers considered non-taxpayers: application for refund form A22, to be filed quarterly.

Formal obligations:

- For manufacturers: accounting of the products subject to the tax, to be provided to the tax administration in the month following the settlement period.
- For intra-community acquirers: stock record book of the products subject to the tax, to be provided in the month following the settlement period.
- Obligations for deliveries of the products subject to the tax:
  - For the first deliveries by the manufacturer, mention on the invoice: (i) amount of tax charged and (ii) quantity of non-recycled plastic (kg).
  - For other deliveries, at the purchaser's request, mention on the invoice or a separate certificate: (i) amount of tax paid for the packaging and (ii) quantity of non-recycled plastic (kg).

Means of proof for the amount of recycled plastic:

- Certificate by accredited entity according to UNE -EN 15343:2008 standard.
- As an exception, during 2023 a responsible statement of the manufacturer would suffice as evidence.

BACK

PKF Comment

The new tax on non-reusable plastic packaging already has a wide impact, as it keeps a transverse approach to the entire commercial and productive chain of goods. Moreover, it entails a very significant administrative workload for the taxpayers involved.

Undoubtedly, it clearly impacts numerous companies with supply and/or acquisition of goods involving non-reusable plastic packaging within Spain. In fact, foreign companies could become subject to relevant obligations if they introduce in Spain on their behalf goods subject to the tax (imports, EU intra-community acquisitions, transfers, etc.).

It is important to note that failure to comply with these tax obligations could lead to significant penalties, but also result in delays in the importation of goods by customs, or reputational damage.

If you believe the above measures may impact your business or personal situation or require any advice with respect to Spanish taxation, please contact Alberto Rodriguez at **arodriguez@pkf-attest.es** or call **+34 945 137 426**.

Switzerland

Implementation of BEPS in three double tax treaties

Switzerland has updated the double tax treaties with the United Arab Emirates, Japan and Tadzhikistan regarding the implementation of the BEPS minimum standards (among other changes).

BACK

PKF Comment

Switzerland will continue to update double tax treaties which do not yet contain such clauses – BEPS cannot be neglected anymore and needs to be considered in any cross-border structuring.

Consultation on individual taxation opened

Currently, married couples tax resident in Switzerland file a joint tax return. This leads in certain cases to a higher tax liability compared to having filed single tax returns – which is in Switzerland known as the marriage penalty. Individual taxation pursues the goal of setting the highest possible work incentives for second earners and promoting gender equality. The consultation period ends on 16 March 2023.

BACK

PKF Comment

In order to foster the attractiveness in Switzerland and in particular the incentives for second earners towards an equal workforce, this is a step in the right direction for the elimination of the marriage penalty.

Update on agreements regarding home office in connection with COVID-19 with Italy and France

The competent authorities of Italy and Switzerland have determined that there are no longer any restrictions on the free movement of persons in either country due to the COVID-19 health emergency. It was agreed that the Memorandum of Understanding of 18/19 June 2020, which includes, among other things, exceptional and provisional special arrangements for home office taxation, will remain in force until 31 January 2023. Due to the current health situation, no extension is planned from 1 February 2023.

The competent authorities of Switzerland and France have agreed that home office work of up to 40% of the annual working time in the cross-border worker's country of residence for an employer in the other contracting state does not call into question the cross-border worker’s status within the meaning of this agreement, which applies from 1 January 2023. It applies irrespective of overnight stays in the state of the usual place of work, i.e. 45 overnight stays are possible without calling into question the status of the cross-border worker.

For the sake of completeness, the agreement with Germany in connection with COVID-19 was already terminated with effect from the end of June 2022.

BACK

PKF Comment

The agreement with France shows that home office is becoming state of the art and could guide the way to future considerations in this regard.

For further information or advice concerning Swiss unilateral and international taxation, please contact Dominique Kipfer at **dominique.kipfer@pkf.ch** or Rilana Wolf-Bayard at **rilana.wolf@pkf.ch** or call **+41 44 285 75 00**.

Taiwan

Amendment to R&D incentives and CFC legislation comes into effect

R&D incentives

An amendment to the Statute for Industries Innovation was passed on 7 January 2023 to provide tax incentives in the form of tax credits for investment in R&D (research and development) and equipment to encourage technological innovation. The effective period for these incentives is from 1 January 2023 until 31 December 2029 and can be summarised as follows:

- pioneer innovation R&D investment credit: 25% of R&D expenditure incurred during a fiscal year; and
- advanced manufacturing equipment investment credit: 5% of equipment purchase price exceeding a certain amount in a fiscal year but no upper limit.

The total tax credit amount for these incentives is capped at 50% of income tax payable in a fiscal year.

To qualify for the tax credit, the following conditions must be met:

- the R&D expenditure and the ratio of R&D expenses to operating net revenue must exceed a certain scale during a fiscal year;
- the applicable alternative minimum tax rate is 12% in 2023 and may be raised to 15% in 2024 depending on the legislative progress of the OECD Global Minimum Tax System (Pillar 2); and
- there has been no violation of environmental protection, labour or food safety and public sanitation laws over the past three fiscal years.

CFC legislation

The controlled foreign company (CFC) rules will become effective from 1 January 2023.

If a foreign subsidiary meets the following two conditions, its non-distributed profits are attributed to its domestic parent company:

- more than 50% of the shares or capital in the foreign subsidiary are owned (directly or indirectly) or significantly controlled by domestic profit-seeking enterprises or their related parties; and
- the foreign subsidiary is established in a low tax jurisdiction, i.e. a jurisdiction where: (i) the corporate income tax rate is lower than 70% of the domestic statutory corporate income tax rate of 20% (i.e. lower than 14%); or (ii) the taxes are levied only on domestic-source income or only on a remittance basis. If a jurisdiction adopts a special tax rate or regime for special regions or industries, the calculation of the tax rate must be made on the basis of that special rate or regime.

Twenty-nine jurisdictions are currently listed for not having a tax rate exceeding 70% of the Taiwan rate, being: Andorra, Anguilla, Bahamas, Bahrain, Barbados, Bermuda, BES Islands, Bosnia and Herzegovina, British Virgin Islands, Bulgaria, Cayman Islands, Cyprus, Guernsey, Hungary, Isle of Man, Jersey, Kosovo, Kyrgyzstan, Liechtenstein, Macao, Marshall Islands, Moldova, North Macedonia, Palau, Paraguay, Qatar, Timor-Leste, Turks and Caicos Islands and Vanuatu.

Fifty jurisdictions are listed for only taxing on a territorial basis or only taxing overseas source income when remitted, being: Belize, Bolivia, Botswana, Brunei, Chad, Costa Rica, Curacao, Democratic Republic of the Congo, Djibouti, El Salvador, Eritrea, Eswatini, France, French Guiana, French Polynesia, French Southern Territories, Georgia, Gibraltar, Guadeloupe, Guatemala, Guinea-Bissau, Honduras, Hong Kong, Kenya, Kuwait, Libya, Malawi, Malaysia, Martinique, Mayotte, Micronesia, Monaco, Namibia, Nauru, New Caledonia, Nicaragua, Niger, Palestine, Panama, Reunion, Saint Barthelemy, Saint Martin (French Part), Saint Pierre and Miquelon, Seychelles, Singapore, Syria, Tuvalu, United Arab Emirates, Uruguay, and Wallis and Futuna.

It is further noted that foreign companies in Ireland, Mauritius, Samoa and other jurisdictions with special rates for certain regions/industries will be evaluated individually based on the facts of each case. Lastly, it is noted that the lists are for reference only and that the determination of a foreign company as a CFC will be based on the actual situation.

BACK

PKF Comment

If you believe the above measures may impact your business or personal situation or require any advice with respect to Taiwanese taxation, please contact Ronnie Chang at **rc@pkf.com.tw** or call **+886 2 8792 2628**.

United Arab Emirates

UAE tax updates

Corporate tax

The Federal Tax Authority (FTA) of the United Arab Emirates (UAE) released the Corporate Tax Decree-Law, i.e. ‘Federal Decree-Law No. 47 of 2022 – Taxation of Corporations and Businesses’ (‘Corporate Tax Decree-Law’/‘CT Decree-Law’) on 9 December 2022.

The CT Decree-Law is broadly in line with internationally accepted taxation principles. It provides a broad framework of corporate tax (CT), and cabinet decisions/further guidance with respect to certain provisions are still awaited.

The key features of the CT Decree-Law are provided as follows:

- CT is effective for financial years starting on or after 1 June 2023.
- The CT rates on taxable income of taxable persons are as follows:

Taxable income (AED)	Corporate tax rate (for taxable person/non-qualifying free zone person)
0 to 375,000*	0%
Above 375,000*	9%
Taxable income	**Qualifying free zone person**
Qualifying income	0%
Income other than qualifying income	9%

* This is per the recently released cabinet decision wherein the threshold of taxable income up to which a 0% CT rate applies (i.e. AED 375,000) is specified.

- A taxable person shall be either a resident person (juridical persons and natural persons who conduct a specified business/business activity in the UAE) or a non-resident person having a permanent establishment, state-sourced income or a nexus in the UAE.
- Certain entities shall be exempt from CT such as government entities, certain persons engaged in certain extractive/non-extractive business, qualifying public benefit entities, qualifying investment funds, public pension or social security funds.
- Unincorporated partnerships shall not be considered taxable persons in their own right; persons conducting a business as an unincorporated partnership shall be treated as individual taxable persons, subject to certain conditions.
- 'Qualifying free zone' is defined as a free zone that meets all the prescribed conditions, i.e. maintaining adequate substance, derives qualifying income (definition to be prescribed in the cabinet decision), has not elected for normal corporate tax provisions, complies with transfer pricing provisions prescribed and meets any other condition which may be prescribed.
- Computation of taxable income shall be on the basis of the stand-alone financial statements prepared in accordance with accepted accounting principles.
- A resident person may elect for small business relief (conditions to be prescribed).
- Income such as certain dividends and other profit distributions, income of a foreign permanent establishment and income derived by a non-resident from operating aircraft or ships in international transportation, subject to prescribed conditions, shall be considered as exempt income. Income from a participating interest (i.e. 5% or greater ownership interest in the shares or capital) shall be exempt, subject to fulfilment of all the prescribed conditions.
- Certain group reliefs (such as the transfer of assets or liabilities between two taxable persons that are members of the same qualifying group, business restructuring reliefs as prescribed) shall be available, subject to prescribed conditions.
- The following shall be allowed as deductible expenditure when computing taxable income:
  - expenditure incurred wholly and exclusively for the purposes of the business
  - expenditure which is not capital in nature
  - expenditure incurred during the tax period.

Certain specific deductions are provided such as:

- Net interest expenditure up to 30% of earnings before the deduction of interest, tax, depreciation and amortisation (EBITDA) shall be allowed, subject to certain conditions.

  However, a specific interest deduction limitation rule is also provided wherein no deduction shall be allowed for interest expenditure incurred on a loan obtained, directly or indirectly, from a related party for profit distribution to a related party, redemption, repurchase, reduction or return of share capital to a related party, capital contribution to a related party, acquisition of an ownership interest in a person who is or becomes a related party following the acquisition.
- 50% of any entertainment, amusement or recreation expenditure incurred during a tax period shall be allowed as a deduction, subject to certain conditions.

No deduction shall be allowed for the following:

- Expenditure not incurred for the purposes of the taxable person's business;
- Expenditure incurred in deriving exempt income;
- Losses not connected with or arising out of the taxable person's business;
- Such other expenditure as may be specified in a cabinet decision.

Certain specific non-deductible expenditure is provided, such as:

- Donations, grants or gifts made to a non-qualifying public benefit entity;
- Fines and penalties, other than amounts awarded as compensation for damages or breach of contract;
- Bribes or other illicit payments;
- Dividends, profit distributions or benefits of a similar nature paid to an owner of the taxable person;
- Amounts withdrawn from the business by a natural person (subject to conditions);
- Corporate tax imposed on a taxable person;
- Input VAT incurred by a taxable person that is recoverable;
- Tax on income imposed on the taxable person outside the state;
- Such other expenditure as specified in a cabinet decision.

- CT Decree-Law also includes transfer pricing provisions which are applicable for prescribed taxpayers having transactions with related parties/ connected persons. It has also stated that the opening balance sheet for the first tax period for UAE CT purposes shall be required to be prepared taking into consideration the arm's-length principle. Further guidance is awaited on the applicability of transfer pricing disclosure forms, master file and local file. The CT Decree-Law also contains a provision for advance pricing agreements (APA), wherein persons who are required to comply with the transfer pricing provisions can apply for an APA with the FTA, before entering into such transactions/arrangements.
- The setting off of tax losses and the transfer of tax losses between entities having direct/indirect ownership is allowed subject to prescribed conditions.
- Formation of a CT group can be applied for, subject to prescribed conditions.
- Withholding tax credit, foreign tax credit, other specified credits/reliefs as per the cabinet decision shall be available.

General anti-abuse rule (GAAR)

The CT Decree-Law includes a GAAR, which shall apply to a transaction or an arrangement if, having regard to all relevant circumstances, it can be reasonably concluded that:

- the entering into or carrying out of the transaction or arrangement, or any part of it, is not for a valid commercial or other non-fiscal reason which reflects economic reality; and
- the main purpose or one of the main purposes of the transaction or arrangement, or any part of it, is to obtain a corporate tax advantage that is not consistent with the intention or purpose of this Decree-Law.

Where the provisions of the GAAR apply to a transaction or arrangement, the FTA may make a determination that one or more specified corporate tax advantages obtained as a result of the transaction or arrangement are to be counteracted or adjusted.

It has also been stated that the GAAR will be applicable for transactions or arrangements entered into on or after the date the CT Decree-Law is published in the Official Gazette.

Registration and compliance

Registration is mandatory for all taxable persons. Corporate tax return filing is required to be done within nine months from the end of the tax period.

The registration process has recently been initiated on the EmaraTax portal. However, the registration is carried out in a phased manner and currently certain businesses have received a personal invitation from the FTA for registration.

Further, a person may make an application to the FTA for a clarification regarding the application of the CT Decree-Law or the conclusion of an APA with respect to a transaction or an arrangement proposed or entered into by the person in the prescribed form and manner.

CT Decree-Law provides that to the extent the terms of an international agreement that is in force in the UAE are inconsistent with the provisions of the CT Decree-Law, the terms of the international agreement will prevail.

Economic Substance Regulations

The government of the UAE introduced the Economic Substance Regulations ('the Regulations'/'ESR') on 30 April 2019 vide Cabinet Resolution No. 31 of 2019. These Regulations were amended retrospectively vide Cabinet Resolution No. 57 of 2020.

The Regulations (as amended), inter alia, prescribe two types of annual compliances:

i) Submission of the 'Information Notification' within six months from the end of the accounting year; and

ii) Submission of the 'Substance Report' within 12 months from the end of the accounting year.

Accordingly, licensees with a financial year ending 31 March 2022 are required to file their Economic Substance Report on or before 31 March 2023. Similarly, licensees with a financial year ending 31 December 2022 are required to file their Economic Substance Notification on or before 30 June 2023.

VAT and excise tax update

With respect to VAT and excise tax, the UAE FTA has recently released certain amendments/updates which are given below:

Date	Tax	Type of update	Particulars of update
October 2022	VAT	Cabinet decision and public clarification	Executive Regulation of the Federal Decree-Law No. 8 of 2017 on Value Added Tax (Cabinet Decision No. 99 of 2022)
September 2022	VAT	Federal decree-law	Federal Decree-Law No. 28 of 2022 – Tax Procedures Law

A summary of the updates is as follows:

- **Executive Regulation of the Federal Decree-Law No. 8 of 2017 on Value Added Tax (Cabinet Decision No. 52 of 2017 and its amendments)**

The FTA has recently amended the Executive Regulation to the Federal Decree-Law No. 8 of 2017 on Value Added Tax (ER) vide Cabinet Decision No. 99 of 2022 issued on 21 Oct 2022 (with effect from 1 January 2023). The new provisions are summarised below:

Sr#	Explanation
1.	**Services provided by a board member as natural person not to be considered as 'supply of services'** The FTA has amended and provided the clarifications vide amending the Executive Regulation and issuing a public clarification on the functions/services provided by a natural person in the capacity of serving as a member of a board of directors. • **Eligibility criteria and services/functions not to be considered as 'supply of services'**

Criteria	Explanation
Persons eligible	A natural person performing the functions of a director on a board of directors of any government entity or private sector.
Persons not eligible	Legal person who may delegate a natural person to act as director on their behalf.
Functions/ services eligible	Only the services performed in the formal capacity as a director.
Functions/ services not eligible	Any freelance services rendered by a third-party natural person who is not a director during the meetings of a board of directors.

- **Transitional rules**

Situation	Date of supply
Performance of service: Calendar year 2022 Tax invoice issued: No Board fees determined and known w.e.f. 1 January 2022	Date of actual completion of the services (article 25 of Decree-Law) Conclusion: Within the scope of UAE VAT
Performance of service: Calendar year 2022 Fees determination: Conclusion of the AGM to be held on 31 January 2023	Date on which the provision of the director's services was completed (i.e. after 31 January 2023) Conclusion: Outside the scope of UAE VAT
Contract period: two consecutive years (i.e. 2022 and 2023) Date of payment: First business day after end of each calendar quarter Tax invoice: To be issued after receipt of payment	Date of receipt of payment (article 26 of Decree-Law) Payments received on 1 April 2022, 1 July 2022, 3 October **2022** Conclusion: Within scope of UAE VAT Payments received on or after 1 January **2023** Conclusion: Outside the scope of UAE VAT

- **Deregistration**
  - A natural person already registered under UAE VAT not meeting the requirements for mandatory registration after this amendment must deregister themselves.
  - However, only the value of services supplied as part of performance of functions as board of directors as specified above would be excluded from the calculation of threshold limit for registration.

2. Changes in emirate-wide record-keeping if taxable person does not have a fixed establishment in the state

The FTA has amended record-keeping provisions of the supplies as follows:

Situation	Provision
Taxable person does not have a ***fixed establishment*** in the state	Record to be kept proving the emirate where place of establishment is located.
Taxable person does not also have a ***place of establishment*** in the state	Record to be kept proving the emirate where the supply is received.

3. Relief to e-commerce operators for record-keeping of the supplies made

The FTA has included clauses pertaining to the record-keeping requirements in respect of the supplies through e-commerce operators as follows:

- **Turnover limitation**
  Emirate-wide recording of transactions to prove the emirate where the supply is received must be kept only if taxable supplies exceed AED 100 million during the calendar year.
- **Time limit for record-keeping**
  Taxable persons exceeding the above threshold limit are required to keep the following records:

Calendar year end in which taxable supplies exceed AED 100 million turnover threshold	Period for which records to be kept	Time period for keeping records
31 December 2022	From first tax period beginning on or after 1 July 2023	For 18 months
31 December 2023 and onwards	From first tax period of the calendar year following the calendar year during which taxable supplies exceed AED 100 million threshold limit	For 2 years

- **Federal Decree-Law No. 28 of 2022 – Tax Procedures Law**
  Key Highlights:

1) Tax Procedures Law has introduced a few new definitions such as 'business day', 'tax residency certificate', 'tax resident' and 'executive regulations' and has amended some of the existing definitions such as 'tax law', 'business', 'legal representative' and 'tax auditor'.

2) The Amended Tax Procedures Law has widened the scope of the law to 'administrative penalties' imposed by the FTA in addition to a few existing scopes.

3) A new clause (5) has been added which states that if the taxpayer discovers that there is an error or omission in the tax return submitted to the FTA, without there being a difference in the amount of tax due, they must correct this declaration by submitting a voluntary disclosure (VD).

4) The Amended Tax Procedures Law has increased the timeline to notify the taxpayer from five to ten business days before conducting a tax audit by the FTA.

5) The Amended Tax Procedures Law has increased the timeline to issue a tax assessment and to determine the value of the payable or refundable tax or any other matters specified in the tax law or the executive regulations from five to ten business days.

6) The FTA has removed the minimum penalty amount of AED 500 for any violation and maximum penalty cap of 300% of the amount of tax in respect of which the administrative penalty was levied. The new clause (4) has been added which states the amount of any administrative penalty shall not exceed 200% of the amount of the tax for which the administrative penalty assessment was issued.

7) Tax crimes and its penalties (previously: tax evasion cases):

   - The FTA has given a relief measure by reducing the quantum of fine in clause (2) from five times to three times the amount of evaded tax. No changes have been made to the associated prison sentence. A new clause (3) has been added which states that any person who deliberately does not settle a due administrative penalty will be liable to the punishment as stated above.

   - A new clause (4) has been added which imposes punishment of imprisonment and a penalty not exceeding AED 1,000,000, or one of these two penalties, on a person who commits the acts below:

     - deliberately providing false information;
     - concealing or destroying documents or other material;
     - stealing, misusing or causing the destruction of documents; or
     - preventing or hindering the FTA's employees from performing their duties.

   - A new clause (8) has been added which states that if a person is found guilty and is convicted of any one of the crimes and then commits another of those crimes within five years from the date of the previous judgment, it would be considered an aggravating circumstance and they would be classed as a reoffender.

8) A new article provides any person the right to submit a request to the FTA for review of any tax assessment or part thereof and any related administrative penalties.

9) Procedure for an application for reconsideration: the time limit of 20 business days has been increased to 40 business days to submit any objection request against a reconsideration request to the FTA in respect of any decision issued by the FTA.

10) Extension of timeframes: a new article has been inserted which states that for any reasons specified in the Executive Regulations or at the request of a person the FTA may extend any of the periods for submission and review of reconsideration and objection requests for a period specified by the Executive Regulations. The FTA's decision of refusing a request for extension of the time period made by a person shall be final and not subject to any objection or appeal.

11) Tax refund procedures: as per the amendment, the FTA shall offset the amount of refund requested with any undisputed payable tax or administrative penalties before refunding any amount related to a specific tax.

Source: https://www.tax.gov.ae/en

Customs

Customs Notice No. 11/2022 on Procedure and Fees for Electronic Attestation for Import Commercial Invoices

The Ministry of Foreign Affairs and International Cooperation (MOFAIC) has put in place a new system for the attestation of commercial invoices relating to the import of goods into the UAE which is effective from 1 February 2023.

Key highlights of the new system:

- The commercial invoices for the import of goods with a value of AED 10,000 or more will be subject to this new electronic attestation.
- The MOFAIC would collect AED 150 per commercial invoice for the import of goods for electronic attestation services. The fees would be collected by MOFAIC through its own portal – eDAS (Link: https://www.mofaic.gov.ae/en/Services/EDAS-Attestation).
- The declarant may finalise the payment of attestation fees within a maximum of 14 days from the date of filing the customs declaration.
- In the event of failure of attestation of the commercial invoice for imported goods within the stated period of 14 days, the MOFAIC may impose an administrative penalty of AED 500.
- The MOFAIC has given an exemption from the subject attestation requirement to certain categories of import transactions as listed below:
  - goods with a value of less than AED 10,000
  - goods imported into free zones
  - personal imports
  - B2C e-commerce movements
  - goods imported by diplomatic service, police and military, charitable societies and international organisations
  - transit goods imports
  - goods imported from Gulf Cooperation Council (GCC) countries.

Other developments

UAE FTA launched new integrated platform 'EmaraTax'

The FTA launched a new integrated platform, 'EmaraTax' on 5 December 2022 for all existing 'e-services' related to VAT and excise which aims to enhance the user experience and improve the online tax administration process. The existing 'e-services' web address (https://eservices.tax.gov.ae/) continues to be the same, while the user interface has changed as per the new 'EmaraTax' platform design. Another interesting aspect is that 'EmaraTax' will soon be available as a mobile application.

'EmaraTax' integrates with important government agencies such as the UAE Central Bank, Land Department, Federal Authority for Identity and Citizenship and national technology-based programs including UAE PASS to streamline the user experience.

The FTA has briefly stated the procedures on the aspects below:

- **Migration from existing to new platform**

  Migration to the new platform commenced from 30 November 2022. Tax registrants will keep their login credentials updated on the existing FTA portal in order to successfully migrate themselves to the new portal.

- **Payments under new 'EmaraTax' platform**

  Alternative 1:

  'EmaraTax' generates a unique payment reference number. The taxpayer should always include the unique reference number when making payments using GIBAN. This unique number is used to ensure that payments are accurately allocated against selected liabilities.

  Alternative 2:

  The FTA will no longer accept eDirham as a payment method. 'Magnati Pay' is the new payment gateway. It accepts payments made using any Visa or Mastercard prepaid, debit or credit card. The FTA has reduced payment handling charges from 2% to 0.714%. Taxpayers are advised to contact their issuing bank to redeem any remaining eDirham balances.

The FTA has also released the User Manual on Payments through GIBAN and Magnati Pay including steps and instructions for making payments.

- **Refunds under new 'EmaraTax' platform**

  Taxpayers are now able to submit one consolidated refund request for all eligible credit balances for each tax type for multiple tax periods. All evidence supporting a refund request can also be submitted online together with the claim. The process will be in real time and taxpayers can follow the progress of the refund online.

BACK

PKF Comment

The CT Decree-Law released is broadly in line with internationally accepted principles. Cabinet decisions/further guidance with regard to certain provisions are still awaited and can be expected soon.

Considering the applicability of the CT law is for financial years starting on or from 1 June 2023, businesses would be required to proactively carry out a CT and transfer pricing impact assessment on their current/proposed businesses and be UAE CT compliant from the outset.

Businesses in the UAE which have identified themselves as in-scope for the purposes of UAE ESR are required to continue to comply with the prescribed filing requirements within the timelines provided by the MOF.

Significant amendments made to the UAE VAT Executive Regulation and public clarification include instances when the services of directors would be outside the scope of UAE VAT or would be taxable, transitional provisions in relation to the same and deregistration from UAE VAT by individuals providing such director services. Amendments to Tax Procedures Law have introduced procedural changes, reduction of penalties, increases in certain time limits and other key changes.

For further information or advice concerning taxes in the UAE, please contact Mr. Shailesh Kumar at **skumar@pkfuae.com**, Mr. Chaitanya Kirtikar at **cgk@pkfuae.com**, Mr. Mradul Gupta at **mgupta@pkfuae.com**, Ms. Nandita Salgaonkar at **nsalgaonkar@pkfuae.com**, Ms. Radhika Doshi at **rdoshi@pkfuae.com**, Mr. Sharad Sharma at **sharadsharma@pkfuae.com** or Ms. Megha Lohia at **mlohia@pkfuae.com** or call **+971 4 3888 900**.

United Kingdom

Transfer pricing documentation requirements from 1 April 2023

Unlike many other economies, the UK tax code does not explicitly require UK businesses to prepare and maintain transfer pricing documentation in an OECD standard format.

Of course, many large groups do prepare such documentation, since this is recommended as best practice, but the lack of any specific requirement creates a degree of uncertainty for UK business regarding what it considered to be sufficient transfer pricing documentation.

The government has been consulting on formal transfer pricing documentation requirements that will be introduced for large businesses for accounting periods beginning on or after 1 April 2023.

What changes are being introduced?

Following consultation on the draft legislation in the last two years, the government published a draft statutory instrument in December 2022 to introduce the transfer pricing documentation requirements.

The rules are broadly as expected; they apply to multinational enterprises (MNEs) with consolidated turnover of EUR 750 million or more, operating in the UK, requiring such MNEs to keep and maintain a master file and local file in accordance with the OECD Transfer Pricing Guidelines.

Earlier drafts of the legislation also included a requirement for an accompanying summary audit trail (SAT), but this has now been delayed, pending further public consultation in 2023. The SAT would require the taxpayer to provide additional information regarding the work that they have undertaken in arriving at the conclusions set out in their transfer pricing documentation. This would represent an additional obligation beyond the standard set out in the OECD Transfer Pricing Guidelines.

The latest legislation also includes a local file exemption for UK-UK transactions, but it is important to note that this exemption does not apply where one of the parties to the transaction has elected into the Patent Box regime or is carrying on a ring fence trade (i.e. oil and gas extraction on the UK Continental Shelf).

BACK

PKF Comment

Whilst the legislation is still in draft form, it is clear that MNEs operating in the UK will be required to prepare and maintain master file and local files in accordance with the OECD Transfer Pricing Guidelines.

It is expected that many large groups with UK entities will already be preparing suitable transfer pricing documentation, since this is best practice. We would recommend that all MNEs revisit their UK transfer pricing documentation and make appropriate revisions to ensure that their documentation is compliant with the rules being introduced with effect from accounting periods beginning on or after 1 April 2023.

Electricity generator levy

In December 2022, the UK government released draft legislation covering the introduction of the electricity generator levy (EGL). The purpose of the EGL, which is effective from 1 January 2023, is to increase the amount of tax payable on the 'excess' revenues of certain electricity generating activity carried on in the UK.

Broadly, the EGL is set at the rate of 45% on electricity revenues that exceed £75 per megawatt hour. There is an annual entry threshold of 50 GWh of electricity generation before a company (or group of companies) is within the scope of the charge. Deductions for 'allowable costs' and a £10 million tax-free allowance are available to reduce the income that is subject to the charge.

The levy is expected to apply to grid connected electricity generation only, thus excluding private wire arrangements for example. It does not apply to generation activities that are fuelled by fossil fuels and therefore only applies to cleaner producing technologies such as wind, solar, biomass and nuclear.

The EGL will be collected through the corporation tax administration system, with a nominated company being responsible for the calculation and payment of the liability. The timing of payment will be aligned with the corporation tax payment dates, so the EGL may be payable in instalments during the course of the year. The EGL is not deductible for corporation tax purposes, which means that excess revenues will be taxed at an effective rate of 70%.

Although badged as a windfall tax in response to excess prices being achieved in the market in recent times, the tax is due to last until 31 March 2028. It is therefore important for any electricity generators in the UK to understand the impact of the EGL on their compliance obligations and post-tax returns.

R&D tax relief is changing

HMRC has become aware of a significant number of R&D claims which have been submitted incorrectly and, in some cases, fraudulently. HMRC moved quickly to redeploy their staff and invested in increasing the size of their R&D team to ensure that claims are appropriately reviewed and scrutinised. We are already seeing the impact of this through increased processing times for claims and it is likely that we will see more HMRC enquiries into R&D claims going forward.

In addition, there are a number of changes coming into effect for accounting periods starting on or after 1 April 2023, most of which are aimed at tackling abuse and refocusing the relief towards R&D activities undertaken in the UK. In summary these are as follows:

- Payments to overseas subcontractors and externally provided workers (such as agency staff) will no longer be treated as qualifying expenditure, except in very specific circumstances. UK companies who currently subcontract R&D activities to overseas group companies or third parties may see the value of their future R&D claims reduce significantly.
- HMRC is also looking to tackle abuse of the scheme by introducing some new steps. These include requirements for claims to be made digitally, as well as full disclosure of the technical details of the relevant projects and a breakdown of qualifying expenditure. Claims will need to be endorsed by a named senior company officer, and there will be a requirement to notify HMRC in advance of the intention to make a claim within six months of the end of the relevant accounting period (which for some will prevent last minute claims).
- Cloud computing and data costs will be included as a category of qualifying expenditure (whereas currently these are excluded). This is likely to be a benefit to technology businesses that incur substantial cloud computing and data costs for the purposes of undertaking R&D.

The government has also announced changes to the rates of R&D tax relief for expenditure incurred on or after 1 April 2023. Broadly speaking, the benefit of the research and development expenditure credit (RDEC), which typically applies to large companies, will increase from 13% to 20%. The small and medium enterprises (SME) additional deduction will decrease from 130% to 86%, and the SME credit rate (for loss-making companies) will decrease from 14.5% to 10%.

The net effect of the rate changes is to more closely align the benefit of the SME and RDEC regimes. The impact will be most keenly felt by loss-making SME claimants who will see the value of their cash credit reduce from £0.334 to £0.186 for every £1 of qualifying expenditure incurred after 1 April 2023.

The Treasury recently launched a consultation with the intention of simplifying the R&D tax reliefs by merging the current SME and RDEC schemes. It is likely that the result will be a scheme modelled on the current RDEC but there are a number of other changes that are also being considered. If implemented, it is expected that the new scheme would be in place with effect from 1 April 2024.

More structural changes to the R&D tax credits scheme have been expected for several years and the uncertainty around possible further changes – and HMRC's current approach to auditing R&D claims – is unhelpful for innovative UK businesses, but is likely to persist.

BACK

PKF Comment

This is a complex area and one we can help you navigate but, in short, care needs to be taken to ensure you don't fall foul of HMRC's changing approach and the updated rules.

If you believe any of the above measures may impact your business or require any advice with respect to UK taxation, please contact Adam Kefford at **adam.kefford@pkf-francisclark.co.uk** or Chris Rodgers at **chris.rodgers@pkf-francisclark.co.uk** or call **+44 1392 667000**.

EU Commission VAT in the Digital Age initiative

In December 2022 the EU Commission proposed wide-ranging draft legislation amending VAT Directive 2006/112/EC, Council Implementing Regulation EU 282/2011 and Council Regulation on Administrative Cooperation EU 904/2010 as part of the VAT in the Digital Age package. These far-reaching proposals aim to modernise the EU's VAT system by promoting harmonised e-invoicing and digital reporting requirements, helping to reduce fraud and VAT loss through non-reporting of VAT, as well as reducing compliance costs for businesses currently having to comply with fragmented reporting requirements across the EU.

It is proposed that the legislation will take effect in phases between 2024 and 2028, and cover three main areas of VAT policy:

1) Digital reporting requirements (DRRs), including e-invoicing;
2) The VAT treatment of the platform economy; and
3) The single place of VAT registration and one-stop shop regimes.

Digital reporting requirements and e-invoicing

The DRR will implement real-time digital reporting to the local tax authority of standardised information for B2B intra-EU transactions. It is intended that this information will feed into the risk analysis systems of EU Member States to help them counter intra-community trade VAT fraud, in particular missing trader intra-community fraud.

Real-time transactional reporting under DRR will replace the requirements for suppliers to report intra-EU transactions on quarterly or monthly recapitulative statements (commonly known as EC sales lists), and for a number of Member States requiring acquisition listings.

Member States will also have the possibility of imposing e-invoicing for domestic transactions. For Member States which introduce e-invoicing and DRR, these national requirements will need to align with the new DRR rules for intra-EU transactions.

E-invoicing for intra-community supplies

Under the proposals, an amended Article 218 of the VAT Directive will create obligatory e-invoicing for all intra-community supplies.

The proposals will now grant national authorities the right to mandate e-invoicing for domestic transactions without a specific EU derogation. Given the new mandatory requirement of e-invoicing for intra-community transactions, it can be anticipated that different EU jurisdictions will take advantage of this right to introduce requirements for e-invoicing at the domestic level.

In keeping with the aim of real-time reporting, the proposals also mandate that e-invoices be issued within two days of the supply occurring where there is an intra-community supply subject to the reverse charge by the recipient.

The VAT treatment of the platform economy

Deemed supplier regime

A 'deemed supplier' regime will be introduced from 2025 via the addition of a new Article 28a of the VAT Directive for short-term accommodation rental and passenger transport providers within the platform economy.

Under this measure, where the underlying supplier does not charge VAT because they are, for example, under the VAT registration threshold, the platform operator 'facilitating' the transaction will be obligated to charge and account for VAT on their deemed supply of accommodation or transport. An amendment to Article 136 of the VAT Directive will mean that the underlying supplier (for example, the accommodation provider) is deemed to be making a (VAT exempt) supply to the platform.

The single VAT registration and one-stop shop

These proposals provide a range of measures intending to ensure harmonised VAT treatment within the EU, reduce opportunities for VAT fraud and mitigate the need for additional VAT registration obligations. It is intended that the proposals will be effective from 2025.

Extension of reverse charge for B2B supplies of goods and services

Currently, a non-established supplier of goods is generally obligated to register for VAT in the territory where a domestic B2B supply of goods takes place (for example, if it procures or stores goods locally for an onwards supply to a business customer). A change to Article 194 makes the application of the reverse charge mechanism mandatory (it is currently only applied in specific Member States) where a business receives a domestic supply of goods or services from a non-established supplier, meaning the supplier of the goods or services will not have to register for VAT in that territory.

Extension of the one-stop shop (OSS) for margin scheme items

Article 14(4) will be modified to extend the definition of intra-community distance sales of goods to cover second-hand goods, works of art, collectors' items and antiques. This will result in the optional application of the OSS simplification scheme to such sales, potentially removing the need for the supplier to register in additional EU jurisdictions.

In conjunction with this measure, to reduce opportunities for VAT avoidance, Article 39a provides that supplies of works of art and antiques without dispatch or transport (or supplies where the dispatch or transport of the goods begins and ends in the same EU jurisdiction) are taxed at the place where the customer is established.

Extension of the deemed supplier rule to marketplaces selling on behalf of EU established traders

Modifications to Article 14a will extend the application of the deemed supplier rule. Under its expanded scope, this rule will now include all supplies of goods within the EU facilitated by an electronic interface, irrespective of where the underlying supplier is established and the status of the purchaser. This further extends the obligations of platform providers to account for VAT on the underlying sale of goods beyond those introduced on 1 July 2021 for imported goods of under EUR 150, to include intra-EU B2C sales made by a non-EU established supplier via a marketplace.

OSS to cover most B2C supplies of services for non-EU suppliers

A modification to Article 359 extends the scope of the non-Union OSS to include supplies of services by non-EU businesses to non-taxable persons which reside in the EU. Certain Member States already extend the 'use and enjoyment' provisions beyond those applicable to telecommunications and electronically supplied services, and in such cases non-EU B2C suppliers are obligated to account for local VAT on such sales. However, this currently only applies in a minority of instances.

The changes will mean that non-EU established businesses which supply B2C services not currently covered by OSS (for example, legal or accounting services) will be obligated to register for OSS (or alternatively in each EU Member State where such a supply is made), and pay local VAT. This will clearly represent an additional cost for many non-EU professional services businesses in cases where the amount charged to the customer is adversely affected by the addition of VAT.

Expansion of the import one-stop shop (IOSS)

The proposals include the mandatory use of the IOSS for B2C imports made via a 'facilitating' platform. Currently, whilst the platform provider is required to account for VAT on B2C imports of goods which the platform facilitates, it can choose to do so via a direct VAT registration in the territory of the customer. It must now declare such sales under the IOSS regime where the consignment value is not greater than EUR 150. The existing EUR 150 value limit for the use of IOSS will remain in place.

Next steps

The draft legislation may be subject to amendments and revisions before being enacted into law. Nevertheless, given the central aims of simplifying VAT compliance, and reducing the VAT gap and levels of VAT fraud, it can be envisaged that the broad thrust of the legislation will become effective in due course.

BACK

PKF Comment

If you believe the above measures may impact your business or require any advice with respect to trading within the EU, please contact Luigi Lungarella at **llungarella@pkf-l.com**; **+ 44 20 7516 2228** or Nadav Shayovitz at **nshayovitz@pkf-l.com**; **+44 20 7516 2217**.

United States

Brazil's transfer pricing changes and impact on US foreign tax credit

The Brazilian government recently issued draft legislation, Provisional Measure 1152 ('MP 1152'), to align the transfer pricing system in Brazil with the Transfer Pricing Guidelines of the OECD. MP 1152 was issued by Jair Bolsonaro but has to be ratified under the new Brazilian government led by Luiz Inácio Lula da Silva within 120 days after the issuance date. The next session of the Congress in Brazil begins on 2 February 2023. Beginning 1 January 2024, the application of the new OECD-based rules would be mandatory but early adoption for fiscal year 2023 would be possible.

The new rules could help Brazil get into the OECD, but also, importantly, could ensure that US multinationals can continue to credit taxes paid in Brazil against their US tax bills.

New US foreign tax credit rules caused concern

In years prior to 2021, US multinationals were able to apply Brazilian tax payments to their US tax liabilities and the IRS did not have many reasons to challenge that position. After updated foreign tax credit regulations were published, questions arose as to whether that position still stands.

Foreign income tax rules must largely conform to US tax laws, especially with regard to the sourcing of income, allowable deductions and the application of the arm's-length principle. The arm's-length principle says that transactions should be valued as if they were between unrelated parties, each acting in their own best interest. In limited circumstances, tax treaties might maintain creditability if similar rules do not exist in foreign tax jurisdictions. However, as a tax treaty between the US and Brazil does not exist, this option is not available. The new rules apply to foreign taxes paid or accrued in tax years beginning on or after 28 December 2021.

The current Brazilian transfer pricing rules do not conform to US tax laws as they do not include the application of the arm's-length principle. US regulations specifically require that any 'allocation to or from the resident of income, gain, deduction, or loss with respect to transactions between such resident and organisations, trades, or businesses owned or controlled directly or indirectly by the same interests (that is, any allocation made pursuant to the foreign country's transfer pricing rules) is determined under arm's-length principles, without taking into account as a significant factor the location of customers, users, or any other similar destination-based criterion.'

Thus, creditability of taxes paid in Brazil could be denied, even if taxpayers apply arm's-length principles in their transactions. Arm's-length principles must be implemented by the foreign tax jurisdiction. That is currently not the case in Brazil.

Changes to Brazilian transfer pricing rules and impact on US foreign tax credit rules

The arm's-length principle will be adopted by the Brazilian legislation if MP 1152 is ratified within 120 days after its issuance. The application of that principle will make sure that one of the requirements to conform to US law will be met and that US multinationals can continue to apply Brazilian tax payments to their US tax liability.

Other significant changes to the transfer pricing rules in Brazil will include the following:

- Selection of the most suitable method for the operation – the rules will make the transactional net margin and profit split methods available to taxpayers;
- Adoption of comparability analysis;
- Introduction of compensatory adjustments (adjustments are possible until the end of the financial year);
- Introduction of specific rules for intangibles;
- Inclusion of specific provisions to regulate intra-group services;
- Introduction of the definition of cost contribution arrangements;
- Application of transfer pricing rules to business restructurings; and
- Inclusion of all financial transactions under the scope of transfer pricing rules.

BACK

PKF Comment

US multinationals should monitor whether the new rules are finally implemented by the current government and evaluate the eligibility for foreign tax credits as they relate to Brazil.

As always, if you need any assistance, please reach out to your PKF O'Connor Davies client service team or Ralf Ruedenburg, CPA at **rruedenburg@pkfod.com** or call **+1 646 965 7778**.

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