

PKF worldwide tax update

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Welcome

In this third quarterly issue for 2020, 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 400 offices, operating in over 150 countries across our 5 regions. Our tax experts specialise in providing high quality tax advisory services to international and domestic organisations in all our markets.

This issue features articles on:

- COVID-19 tax measures and guidelines in Austria, Bulgaria, Ecuador, Hong Kong, South Africa and Switzerland.
- DAC6 (reporting of cross-border tax arrangements) in Poland.
- VAT developments in Bulgaria, Chile, Italy, Nepal and Mexico.
- Double tax treaty updates and related case law in Austria, Belgium, China, India, Luxembourg and Turkey.
- Recent comprehensive tax changes in Jamaica, Kenya and Nepal.
- International tax developments (CbC Reporting, BEPS, Transfer Pricing) in the UAE, Ukraine and the U.S.

We trust you find this update informative and interesting. 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.

2020/21 Worldwide Tax Guide

The latest PKF Worldwide Tax Guide features 146 jurisdictions. Its resounding success is a result of the energy, time and support of individuals and firms within the PKF family. We thank you all for your support. We are extremely grateful to all those who have provided country submissions, and to each person who has supported this very marketable and impressive publication.



Austria

Guidelines for the application and interpretation of double tax treaties further to COVID-19

On 22 May 2020, the Austrian Minister of Finance announced some guidelines for the application and interpretation of double tax treaties (DTTs) in light of the COVID-19 pandemic:

Salaries in connection with activities performed in the home office

- DTT with Art. 15 clause corresponding to OECD-MA (taxation based on the place of employment principle): treatment of salaries for cross-border employees in accordance with DTT; any bilateral consultation agreements take priority.
- Consultation agreement with Germany: COVID-19-related home office days are deemed to be exercised in the “normal country of activity”; for cross-border commuters, these do not count as days of non-return.
- Cross-border commuter regulation with Liechtenstein: people who were previously classified as cross-border commuters because they commuted “usually every working day” but now work from their home office to curb the further spread of the COVID-19 pandemic do not lose their cross-border commuter status.

Short-time work benefits

Short-time work benefits paid by an employer to his employee are taxable within the scope of a



provision modelled on Art 15 OECD-MA based on the principle of causality in the country in which the activity to which they relate to would have been carried out. If a DTT contains a separate provision for income from statutory social insurance or similar income, remuneration for short-time work is not covered under Art 15 OECD-MA, but basically falls under the respective special provision of the DTT, which usually gives the right to tax to the state of the allocated health insurance fund.

Permanent establishment

If an Austrian-based employee of a company domiciled abroad performs work out of the home office during the COVID-19 pandemic, this will be considered force majeure and will, in principle, not create a permanent establishment within the meaning of Art 5 OECD-MA at the level of the foreign company.

Construction work and assembly

With regard to construction work or assembly, a permanent establishment under regular law is only established when its duration exceeds a certain period - usually twelve months. If the construction or assembly is temporarily interrupted, these periods should always be included in the calculation of the threshold. If there are temporary interruptions due to the COVID-19 pandemic, these do not - in principle, subject to any deviating bilateral agreement - lead to a suspension of the threshold.

PKF COMMENT

The COVID-19 pandemic might also impact the application and interpretation of international treaties. For some cases, the Austrian government recently issued guidelines principally considering the pandemic as an (unpredicted) exceptional situation, which should allow flexible handling of existing DTT clauses. For further information or advice please contact Thomas Ausserlechner at thomas.ausserlechner@pkf.at or call +43 1 512 87 80.

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Belgium

Antwerp Court rules that Dutch expatriate tax allowances are also tax-free in Belgium

On 26 November 2019, the Antwerp Court of Appeal rendered its decision concerning the classification for Belgium personal tax purposes of the 30% expatriate costs compensation under the Dutch 30% ruling ("the 30% ruling").

Under the 30% ruling, highly qualified employees temporarily assigned to the Netherlands are entitled to receive 30% of their employment income tax-free

as compensation for incurring specific expatriate costs. Such costs include, among others, double housing costs, home country travelling costs, storage of furniture costs, additional costs of living incurred because prices in the Netherlands are higher than those in the home country, and costs incurred in having official documents drawn up. The taxpayer concerned was employed as an expatriate in the Netherlands in 2013 and 2014. As such, he was entitled to the 30% ruling implying that 30% of his salary was tax-exempt in the Netherlands as compensation for extraterritorial costs. The taxpayer did not declare the 30% costs compensation when filing his Belgian personal tax returns. However, the Belgian tax authorities took the view that the 30% costs compensation should have been declared because it constituted a hidden salary payment. The taxpayer then appealed that decision.

Summarised, the Antwerp Court stated that the Belgian tax authorities can only tax business costs compensation if they demonstrate that the compensation constitutes a hidden salary payment. However, in the case at hand, the Belgium tax authorities did not provide that evidence. As a result, the Court of Appeal was of the opinion that the Belgium tax authorities had not refuted the presumption that the 30% cost compensation is not taxable. Therefore, the Court of Appeal decided in favour of the taxpayer and held that the exempt compensation of up to 30% of the salary paid constitutes a compensation for extraterritorial costs incurred by expatriates in the Netherlands, which does not have to be declared as taxable salary in Belgium.



PKF COMMENT

This case law is a clear example of a case where the Belgium tax authorities unrightfully tried to reverse the burden of proof to the taxpayer. It is therefore highly welcomed that the Antwerp Court applied Belgium tax procedure in a strict and correct way and ruled in favour of the taxpayer. If you believe the above ruling may impact your personal situation or require any advice with respect to Belgium taxation, do not hesitate to contact Kurt De Haen at kurt.dehaen@pkf-vmv.be or call +32 2 460 0960.

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One-off tax loss carry-back

Belgium tax legislation does not feature a tax loss carry-back rule. Tax losses can only be carried-forward, without limitation in terms of time and amount. However, the corona crisis struck hard resulting in many companies incurring current-year losses related to FY 2020.

In particular, in order to support companies from a cash-flow perspective, they are allowed to exceptionally carry-back the “expected” 2020 tax losses in order to offset them against FY 2019 (tax assessment year 2020) taxable profit. The Belgium corporate tax return for the tax year 2020 is to be filed in principle by 24 September 2020. As a result, the 2019 Belgium corporate tax liability decreases for eligible taxpayers. Hereafter, you will find some best-practice guidelines in this respect:

- When making use of the carry-back of tax loss rule, no BE GAAP accounting entries are required. Only the appropriate boxes of the “tax-free reserves” as laid down in the corporate tax return of the tax year 2020 need to be duly completed.
- The financial year 2020 is obviously still running. That is why the “expected” tax losses of this financial year need to be estimated as accurately as possible. This is important, because if it appears after that the actual tax loss is less than 90% of the estimated tax loss, additional tax will be due on the difference. The tax rate will range from 2%-40% depending on the difference. The bigger the difference, the higher the tax rate.
- The Belgium corporate tax rate has decreased from 29.58% to 25% with respect to financial years 2019 and 2020. As the carry-back of tax losses may not lead to positive tax arbitrage, the 2020 taxable basis will be adjusted to neutralise the difference in corporate tax rates.
- The Belgium company at hand may have made advance tax payments in 2019 which may now end up being pointless or excessive because of the use of carry-back tax losses. As such, this should not lead to adverse tax consequences as the company will get the excessive advance tax payments refunded (be it interest-free) within two months as from the date of the assessment notice.
- There is no impact on the BE GAAP annual accounts of the financial year 2019 which are finalised already. Indeed, a tax saving should only be recorded in the profit and loss account of the financial year in which the tax loss has been incurred, i.e. financial year 2020.
- However, if the company proceeded to a dividend distribution, a capital reduction or a redemption of own shares in the period between 12 March 2020 and the moment when the corporate tax return for the tax year 2021 is filed, it cannot make use of the carry-back of tax loss rule. The same applies to a company which has a shareholding in a company located in a tax haven or to a company making tainted payments exceeding EUR 100,000 to a beneficiary residing in a tax haven.
- For completeness’ sake, the carry-back of tax loss rule can be combined with Belgium group relief for corporate tax purposes. Needless to say, this requires careful tailored planning, but also offers interesting opportunities.

PKF COMMENT

The introduction of the exceptional tax loss carry-back rule is fairly unique in Belgium but is nevertheless highly welcomed by taxpayers under the current delicate economic circumstances. Those who want to make use of this rule should do so by duly completing their Belgium corporate tax return for the tax year 2020. For further details, please contact Kurt De Haen at kurt.dehaen@pkf-vmv.be or call +32 2 460 0960.

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Bulgaria

Introduction of reduced VAT rate for books, restaurant and catering services further to COVID-19

In early June 2020, changes to the Bulgarian VAT Act were announced encompassing a 9% reduced VAT rate for the sale of books (including e-versions), restaurant and catering services (excluding alcoholic beverages), as well as for baby foods and products. The reduced rate for the abovementioned goods and services is temporary and will apply from 1 July 2020 to 31 December 2021.

PKF COMMENT

The tax consultancy team of PKF Bulgaria has substantial knowledge and expertise and can provide assistance at each stage of Bulgarian tax planning and compliance procedures to both foreign and local individuals. We have successfully consulted our PKF clients who operate in various fields of business on how to be compliant with the rapid changes of the tax legislation in the everchanging business environment. For further information or advice concerning Bulgarian tax planning, please contact Venzi Vassilev at venzi.vassilev@pkf.bg or call +359 2439 4242.

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Chile

New VAT measures enacted

The Tax Reform Package has modified the VAT Act by subjecting digital services, and the like, rendered by non-resident companies to a 19% VAT rate. That means that these companies have to charge the 19% rate to the price of their services. The following are the new services subject to VAT as from 1 June 2020:

- Intermediation of services provided in Chile, whatever their nature, or of sales made in Chile or abroad whenever the latter give rise to an import
- The provision of digital entertainment content, such as videos, music, games or other analogues, through download, streaming or other technology, including texts, magazines, newspapers and digital entertainment books
- Making available software, storage, platforms or computer infrastructure
- Advertising, regardless of the medium or medium through which it is delivered, materialised or executed.

When the abovementioned services are rendered to consumers (B2C), the law states that non-resident companies must register with the Chilean IRS and will be subject to a special regime to allocate and pay the VAT return. Some of the rules making the tax compliance easier for them are as follows:

- Companies can choose to file the VAT return and pay the tax monthly or every calendar quarter

- They can apply for foreign currency tax calculation and payment
- They do not have to issue invoices controlled by the Chilean IRS.

Non-resident companies have to charge VAT on service prices, unless the customer gives them notice that it is a Chilean VAT taxpayer, in which case the VAT will be withheld by that taxpayer.



PKF COMMENT

The Chilean IRS may designate credit card issuers, debit card issuers or other similar payment systems as withholding agents by way of assuming the taxable person's obligations. Another important aspect is that the software impacted by these measures will not be subject to VAT.

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

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China

How to declare corporate income tax under the WFOE and branch office model in China

What is the WFOE and branch office model?

The WFOE (“Wholly Foreign Owned Enterprise”) and branch office model means that after a WFOE is established in China, it could then open its branch offices in different regions of China, and the WFOE will become the head office of those branch offices.



The process of setting up a branch office is easier and less expensive than setting up a new WFOE. Apart from that, the branch does not require registered capital, while the head office needs a capital contribution. Since a branch office has its own business license and seal, it could sign off on business contracts on its own behalf and hire

employees. The profit and loss of a branch office could be consolidated at the head office level. Hence, this model could be a good choice to expand business throughout China rapidly and easily.

However, there are disadvantages to the branch office model as well. Its business scope is limited to the head office’s business scope, it cannot export or import on its own, and the head office is liable for activities performed by the branch office as the branch office is not an independent legal entity.

Tax administration for the branch office

A new branch office must be registered with the local tax bureau within 30 days after obtaining the business licence and report its head office’s information as well, after which, the branch office will have a tax ID and is able to issue invoices to its customers. The branch office needs to declare VAT locally, on a monthly or quarterly basis, which is similar to what a WFOE does. For most of the taxes, for example, individual income tax, and stamp duty etc., the same tax declaration requirements are applied to a branch office, except for Corporate Income Tax (“CIT”).

How to pay CIT under the WFOE and branch office model

China CIT is levied on each legal entity purpose, so a head office and its branches need to calculate CIT on a consolidated basis. This means the loss and profit of a head office and branches are added together to reach a tax payable amount.

According to PRC Tax Regulation, SAT [2012] Bulletin 57, the WFOE and its branch offices located in different regions should pay CIT to the local tax authorities respectively in their own registered locations on the basis of the following allocation method:

- The head office will first consolidate and calculate the taxable profit and CIT payable of itself and its branches as a whole for both quarterly and annual filing purposes

- For each quarterly filing, 50% of the tax payable will be allocated to the branches and 50% to the head office. The allocation proportion among the branches is calculated based on three factors of the previous year, i.e. operating revenue, total assets and employee remuneration, with the weighting index at 0.35, 0.3 and 0.35 respectively.
- Proportion of tax payment allocated to a single branch = $0.35 \times (\text{amount of operating revenue of a branch} / \text{amount of total operating revenue of all branches}) + 0.35 \times (\text{amount of employee remuneration of the branch} / \text{amount of total employee remuneration of all branches}) + 0.3 \times (\text{total assets of the branch} / \text{total assets of all branches})$.
- Tax payment amount for a branch equals the total tax payable of the company $\times$ 50% $\times$ proportion of tax payment allocated to this single branch.
- For CIT annual settlement before 31 May of the next year, the head office and the branches shall pay their own under-paid CIT or claim CIT refund/offsetting for over-paid CIT with its respective in-charge tax bureau based on the above consolidation calculation and allocation method.

Nevertheless, the following types of branch offices could be exempt from making CIT payments locally under the WFOE and branch office model:

- Branch offices that only have auxiliary functions (e.g. after-sales services, internal research and development, warehousing)
- The first year of a newly established branch
- The head office is recognised as a small-scale enterprise in the previous year
- Wound-up branch offices after the tax de-registration formalities are duly completed.



PKF COMMENT

- *The WFOE and branch office model may be an easier way to expand business in China. However, there are also other options; setting up new WFOEs, or a representative office etc. Each structure has its own pros and cons, so foreign investors may want to plan carefully in order to find the appropriate and tax-effective structure for their business.*
- *A branch office may be an efficient vehicle to hold part of the functions of a company at a specific location to meet the business development needs in future.*
- *The CIT allocation method is quite complex and if the branch offices might have to deal with different local tax practices in different regions. It is suggested to well understand the related tax regulations and local practices before the CIT declaration or seek the help from tax professionals*
- *It is important to calculate the allocation proportion correctly, because it will affect all the CIT payments among branches.*

If you believe the above may impact your business or require any advice with respect to China taxation, please contact Allan Jiang at allan.jiang@pkfchina.com or call +86 21 6076 0876.

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Tax treatment of cross-border royalty payments in China

Nowadays, more and more multinational companies (“MNCs”) offer know-how, technology, process techniques, trademarks, brands etc to their invested companies in China and consider royalty payments as an effective way for repatriating profits out of China. However, it may also entail tax risks if such arrangements fail to comply with China tax laws.

Tax implications of cross-border royalty payments

(1) Withholding Income Tax

Royalties derived from a Chinese enterprise by a non-resident enterprise are subject to China Enterprise Income Tax (“EIT”) on a withholding basis at the current 10% rate (the standard rate is 20% according to China EIT Law), which could be further reduced subject to the application of a double tax treaty. When the royalty payment is due according to the relevant contract, the tax withholding obligation arises at the level of the Chinese enterprise making the payment.

(2) Withholding Value Added Tax (“VAT”) and Surcharges

The payment of royalties would also be subject to VAT at a standard rate of 6%, as well as surcharges (urban construction and maintenance taxes, education surcharge, and local education surcharge). which shall also be withheld by the Chinese enterprise at the time of remittance. The 6% VAT can be claimed as VAT input by the Chinese enterprise to offset against its VAT payables if it is a general VAT taxpayer in China.

(3) Transfer Pricing Regulations

China implemented transfer pricing regulations many years ago and the principles are consistent with OECD guidelines, such as the arm’s length principle to be adhered by regarding transactions between an enterprise and its related party. If a payment made to a related party overseas is found to be not in accordance with the arms-length principle or the profit distribution does not match the value

contribution, the tax authority can carry out a tax audit to impose a tax adjustment any time within 10 years from the date of the transaction. The adjustment may result in the payment not being allowed for EIT deduction at the level of the Chinese enterprise.

(4) Tax Treaty Benefits

China has entered into double tax treaties (“DTTs”) with more than 100 tax jurisdictions, and certain DTAs offer favourable withholding tax rates on royalties paid by Chinese enterprises to non-resident enterprises. For example, a withholding income tax rate of 7%, rather than 10% tax rate under the China-Hong Kong DTT.

If the DTT benefits are applicable to royalty payments, then the non-resident enterprise, when qualifying as the beneficial owner, can enjoy preferential withholding tax rates upon withholding tax filing without pre-approval from the tax bureaus. However, the tax bureau will scrutinise the application afterwards and the following materials should be submitted to the tax authorities:

- Tax resident certificate of non-resident enterprise
- Payment receipt, contracts or agreements regarding the royalty payment
- Documents that can prove the non-resident enterprise is the beneficial owner of the royalties.





(5) *Beneficial Owner Assessment on Royalties Payment*

The non-resident enterprise will not qualify as a beneficial owner, if it does any of the following.

- The recipient pays more than 50% of the income to a resident(s) of a third jurisdiction within 12 months after it receives the income
- The business activities carried out by the recipient of the income do not qualify as substantive business activities, including substantive manufacturing, trading and management activities. Whether the recipient has carried out substantive business activities will be judged based on the functions performed and risks assumed by the recipient. Substantive investment management activities can qualify as substantive business activities
- The recipient is exempt from tax on the relevant income or the income is not taxable in the residence jurisdiction, and if the income is taxable, the effective tax rate is extremely low
- A licence or transfer agreement exists between the non-resident and a third party relating to the transfer of the ownership of, or right to use, the copyright, patent or technology covered by the licence agreement, based on which a royalty is derived and paid.

China tax regulations also offer safe harbour rules to qualify for beneficial ownership, the assessment of which would be determined on a case by case basis.

Tax risks of cross-border royalty payments

In recent years, royalty payments to related parties have been a main target of tax audits. We summarise the key areas from those audit cases hereafter:

1. Many MNCs have production subsidiaries in China that operate at a reasonable level of gross profit margin, but have consistently experienced year-over-year losses or marginal profits in net profit. The reason for this is mainly due to the payment of large royalties to offshore affiliates
2. Domestic enterprises that have made a special contribution to the value of the technologies or the technologies themselves have devalued and they still pay high royalties to offshore affiliates
3. Royalties paid to offshore affiliates registered in tax havens or tax jurisdictions offering DTT benefits
4. Royalties paid to the mere owner of certain intangible assets (which owner actually makes no contribution to the value of usage of the intangible assets) may not constitute business substance to the royalty payment
5. High and new technology enterprises that are supposed to own their own core technology while they still pay huge technology-related royalties to offshore affiliates
6. Related parties change the payment of royalties into the payment of technical services. Instead of charging royalty payments, the overseas companies may charge technical services and justify that most of the services are provided outside China. According to China tax regulations, royalty-related services such as training and support services could also be considered royalty payments.

China's tax authorities would investigate whether royalty payments are made based on the arm's-length principle, and if the recipient has business substance or not. If the royalty payments do not match the economic benefits they generate, the tax authorities could make special tax adjustments to

said payments. Also, the royalty payment lacking business substance might not be considered a deductible item for EIT purposes at the level of the Chinese subsidiary.

When the royalty payment is related to imported goods, it may also trigger import customs duties and import VAT. This potential risk is to be further analysed on a case by case basis.



PKF COMMENT

Regarding cross-border royalty payments, MNCs are advised to revisit their transfer pricing policies and supporting documents to enjoy tax treaty benefits and should be fully prepared in order to ensure tax efficiency and manage related tax risks at the same time.

Since royalty tax treatment may involve the assessment of tax treaty application and may also be related to differentiation between pure labour service and royalty, permanent establishment assessment, as well as import taxes, tax professionals can be of assistance to MNCs in order to more accurately assess their tax implications when deriving royalties from China, and to properly optimise favourable tax policies when structuring royalty transactions.

If you believe the above may impact your business or require any advice with respect to China taxation, please contact Allan Jiang at allan.jiang@pkfchina.com or call +86 21 6076 0876.

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Cyprus

Notional interest deduction provisions amended

On 16 June 2020, the provisions of the Notional Interest Deduction (NID) on new equity used for the production of taxable income were amended.

Background

As from 1 January 2015, Cyprus tax resident entities were entitled to deduct from their taxable profits, a notional interest (NID) arising out of new equity introduced which produces taxable income. This NID is subject to a number of conditions including a taxable income limitation.

In brief, the NID is equal to the amount of the new equity introduced for business purposes multiplied by the relevant “reference rate”, subject to an annual cap of 80% of the taxable profits (as calculated prior to the NID) arising from the new equity.

New Provisions

(a) Reference rate

Until 31 December 2019

The reference rate was the yield of the 10-year government bond (as at 31 December of the year preceding the tax year the NID is claimed) of the country in which the new equity is employed/invested plus 3%. The minimum reference rate was the yield of the Cyprus 10-year government bond (as at 31 December of the relevant year) plus 3%.

From 1 January 2020

As of 1 January 2020, the relevant 10-year government bond yield will no longer be determined by taking the higher of: (i) the Cyprus yield rate; and (ii) the yield of the country in which the new equity is invested into.

Instead, the 10-year government bond yield will be determined only with reference to the jurisdiction of investment (i.e. the Cypriot yield rate will no longer serve as a minimum).

The reference rate is the yield of the 10-year government bond (as at 31 December of the year preceding the tax year the NID is claimed) of the country where the new equity is employed/invested plus 5%, and there is no minimum reference rate.

In case the country in which the new equity is invested into has not issued a government bond on 31 December of the year preceding the tax year, the “reference interest rate” will be based on the government bond yield of Cyprus plus 5%.

(b) New Equity

Under the existing provisions, “new equity” refers to any equity introduced into the business on or after 1 January 2015 and used for producing taxable income but excludes any equity created from the capitalisation of reserves existing on 31 December 2014. An exception to this exclusion rule is when the capitalisation of such “old” reserves creates new business assets which did not exist on 31 December 2014.

“New equity” is now defined as equity introduced into the business on or after 1 January 2015. Therefore, as from 1 January 2021, the NID can no longer be claimed on equity arising from the capitalisation of reserves existing on 31 December 2014 regardless of whether such equity is funding new business assets.

(c) 80% Restriction

A clarification on the calculation of the 80% restriction, in that the relevant taxable profits are those relating to the new equity, so that the NID can only be claimed against such profits. It also clarifies that the cap applies separately to the taxable profits derived from each business asset that is financed by the new equity (i.e. 80% restriction should apply separately to the taxable income arising from each business asset which is financed by new equity).

If tax losses arise from the use of new equity into the business, no NID should be available in the relevant year.

The amendments for the 80% restriction will apply retroactively as from 1 January 2015.



PKF COMMENT

The amendments provide additional incentives to eliminate the thin capitalisation concept, by increasing the notional interest reference rate and abolishing the restriction on pre-2015 profits' eligibility of having been capitalised into share capital.

For further information or advice on any Cyprus tax matter, please contact Nicholas Stavrinos at nicholas.s@pkf.com.cy or call +357 258 68000.

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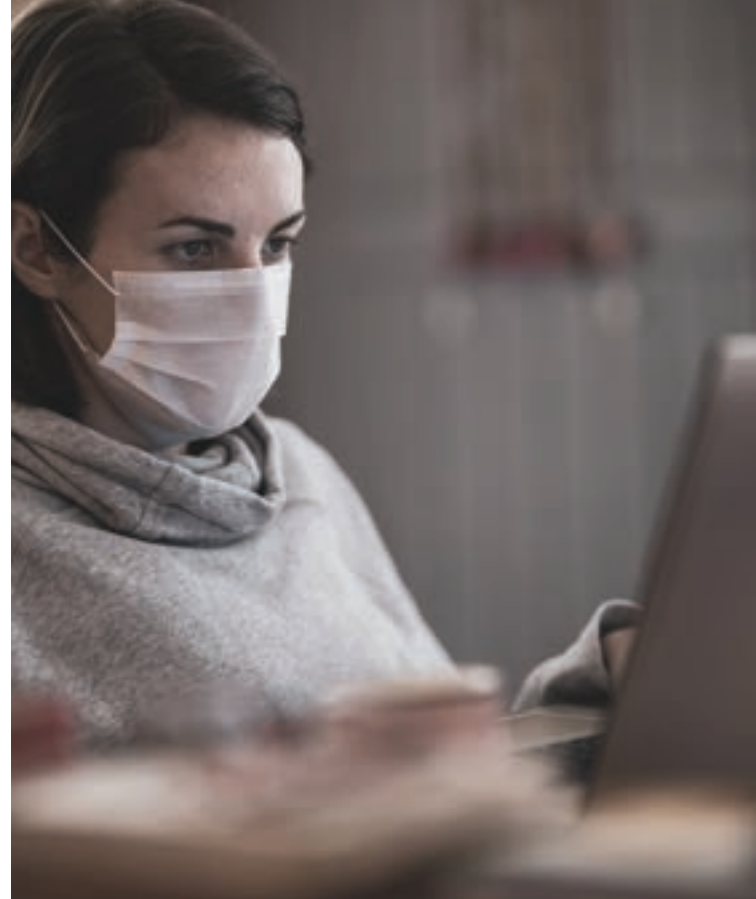
Ecuador

Tax reliefs to counteract COVID-19-induced economic crisis

On 16 March 2020, President Lenin Moreno declared the state of emergency due to the COVID-19 pandemic, suspending all non-essential economic activity and forcing the population to go into lockdown in an attempt to slow the spread.

To reduce the impact on taxpayers' liquidity, the government has since implemented the following measures:

- Deferred payment of (i) VAT payable in April, May and June 2020 and (ii) income tax for year 2019, through six (6) instalments from the original submission deadline. This measure is only applicable for micro, small and medium-sized companies; taxpayers domiciled in the Galapagos islands; airline companies, taxpayers from the tourism and agriculture sector; and recurrent exporters and taxpayers deriving more than 50% of their income from exporting goods
- Extended deadlines for tax filing, which was originally due in March and April 2020
- Extended deadlines for administrative-tax processes and for the statute of limitations of tax-related debt collection.



On 19 June 2020, the National Assembly approved the “Law for Humanitarian Support”. Regarding tax matters, this Law includes benefits for financial entities providing productive loans to the private sector in order to reactivate the economy and preserve employment.

PKF COMMENT

President Moreno finally obtained approval of the “Law for Humanitarian Support”, although not as he initially intended to. His major setback was the exclusion of contributions to companies with earnings exceeding USD 1 million and to individuals with monthly income exceeding USD 500. In recent interviews, the President and top government officials declared that a Decree will be issued aiming at the advance payment of income tax at the level of companies with earnings exceeding USD 5 million and that have not been affected by the COVID-19 pandemic. Under the premise that “those earning more, should contribute more”, the resources obtained from these contributions are intended to be allocated to credit lines and food supplies.

For further information or advice concerning tax amnesty or any advice with respect to Ecuador taxation, please contact Edgar Naranjo at enaranjo@pkfecuador.com or call +593 4 236 7833.

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Germany

Check-the-box in Germany: Partnerships can opt for corporate income tax in the future

On 3 June 2020, Germany's federal government agreed on a comprehensive financial aid package to stimulate and reinvigorate the economy, part of which is an option model for partnerships. According to this model, the shareholders can decide that a partnership will be treated as a corporation for income tax purposes.

1. Who can opt and how?

The option is to be available for all partnerships that generate income from business operations. The option is exercised by the shareholders passing a resolution. Subsequently, the legal representatives have to file an application with the tax office.

2. Effects of the option

2.1 Scope of application

The resolution and the application to the tax office lead to the partnership being treated as a corporation for income tax purposes.

Note: an option term of seven years must be taken into account; only after this period is a re-option for taxation as a partnership possible again.

2.2 Fictional transformation of form

By exercising the option, the partnership is fictionally transformed into a corporation for income tax purposes. Shareholders are deemed to be granted shares in a corporation, as in the case of a change of legal form.

3. Taxation after exercise of the option

3.1 Qualification and determination of income

After exercising the option, trade and corporate tax principles for corporations are to be applied. In accordance with the separation principle, the corporation and the shareholders now each represent independent tax subjects. Contractual relationships under the law of obligations (e.g. loan agreements) between the shareholder and the company are now recognised for tax purposes. This also applies to shareholder-manager contracts. The income is subsequently no longer considered business income, but income from employment. Social insurance obligations might arise.

3.2 Distributions of profits

In the case of "normal" corporations, profits generally remain in the company and are recognised as retained earnings under equity. Only when the shareholders explicitly decide to distribute all or part of the profit is capital gains tax (CGT) - a kind of withholding tax - to be paid and the net dividends are paid out or credited to the shareholders' accounts.

In contrast, the reverse is true for partnerships even after exercising the option. The so-called full distribution principle still applies. This means that the company has to withhold CGT on all taxed profits and the net dividend is credited to the shareholders' accounts. If a retention or strengthening of equity capital is desired, there must be a provision under company law that profits are credited to a reserve account. Only in this case will no CGT be levied on the retained profits.



4. Exemplary comparison of tax burdens

The following assumptions are made:

- Partnership generates a taxable profit of EUR 100,000
- Trade tax 13.3%, corporate income tax (CIT) 15%, income tax with a marginal tax rate of 42% and CGT 25% are taken into account
- Tax allowances, church tax and solidarity surcharge are not included in the calculations for reasons of simplification.

A distinction is now made between three cases:

(1) *Taxation without option:*

tax of EUR 13,300 on the profit, the shareholder account is credited with EUR 86,700. Shareholders have taxable income of EUR 100,000. Trade tax can be credited against the income tax of EUR 42,000. So, shareholders pay EUR 28,700.

Result: After taxes, shareholders have EUR 58,000 at their free disposal, the company has zero.

(2) *Taxation with option without retention:*

The partnership owes EUR 13,300 trade tax and EUR 15,000 CIT. Of the remaining amount of EUR 71,700, the company has to withhold EUR 17,925 CGT. Shareholders have to tax EUR 71,700 as income from capital assets; the tax is fully covered by the creditable CGT.

Result: After taxes, EUR 53,775 remains at the free disposal of the shareholders, zero for the company.

(3) *Taxation with option with retention:*

The partnership owes EUR 13,300 trade tax and EUR 15,000 CIT. EUR 71,700 can be added to the reserves.

Result: In so far as taxed income is retained at the level of the partnership, it is not

available to the shareholders. Only after a distribution has been passed is CGT to be withheld and taxation to be carried out at the level of the shareholders, which, however, is offset against CGT.

5. Conclusion

The example shows that the partnership does not necessarily enjoy tax advantages if it opts for corporation tax. The advantage of the option model is that a “company” level is also formed and that, in the event of a retention, approximately EUR 13,700 less tax must initially be paid per EUR 100,000 of income and stays available for internal financing. It remains to be seen how the option model will be specifically drafted in the further legislative process.



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.

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Hong Kong

COVID-19 stimulus packages provided by the HK Government

The Legislative Council Finance Committee approved a second round of the Anti-epidemic Fund (“AEF”) stimulus package on 18 April 2020, granting a budget of HKD 137.5 billion to specifically target (i) job retention, job creation and job advancement; (ii) sector-specific relief; (iii) reduction of financial burden through governmental rental concessions, fee waivers, provision of loans and loan repayment deferrals; and (iv) other relief through government facilitation. The first round of the AEF stimulus package was approved in February 2020, in which a budget of HKD 30 billion had been granted for the purpose of enhancing the capabilities of the government and other relevant parties to combat the epidemic and to provide relief to members of the public that were significantly affected by the epidemic.

Various tax relief measures were granted, including postponing the issuance of tax returns by one month, the automatic extension of tax filing deadlines which originally fall between March and May 2020, and the 3-month postponement of tax payments falling due in April to June 2020. One of the focal points of the second round of the AEF stimulus package is the Employment Support Scheme (“ESS”), in which a monthly subsidy of up to HKD 9,000 per employee (for a period of 6 months)

would be granted to eligible employers, subject to certain conditions (e.g. undertaking to not implement redundancies, restrictions on the wage subsidy usage, etc.). Most of the subsidies and financial assistances granted under the AEF are specifically exempt from the Hong Kong Profits Tax.



PKF COMMENT

Although the application period for the first tranche of the ESS wage subsidies has already lapsed on 14 June 2020, the application period for the second tranche of subsidies (i.e. the subsidy period for the second tranche is from September to November 2020) is fast approaching. Please let us know if you have any questions on your eligibility for the second tranche of ESS wage subsidies or require our assistance for the application process.

For further information or advice concerning the above or any advice with respect to Hong Kong taxation, please contact Henry Fung at henryfung@pkf-hk.com or call +852 2806 3822.

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Hungary

Introduction of a special retail tax

Further to new legislation published on 9 June 2020, the special retail tax introduced by government decree during the state of COVID emergency and originally planned to be a temporary tax became a permanent feature of the Hungarian tax system.

The tax liability applies to retail activity (specified by NACE classes), and covers all transactions where a domestic or a foreign person or entity carries out

retail activity in a business-like manner, including where a foreign-registered person sells goods to its customers via channels other than a branch office in Hungary.

The basis of the special retail tax is the net revenue (as defined in the decree) derived from the retail activity. In certain cases, the net revenue of related companies shall be aggregated and a progressive tax rate shall be applied to this aggregate amount in order to calculate the tax amount due. As a result, the related taxable persons bear the calculated tax burden in proportion to respective taxable income.

The tax rate is determined as follows:

- 0% on a taxable amount not exceeding HUF 500 million (approximately EUR 1.4 million)
- 0.1% on a taxable amount in excess of HUF 500 million but not exceeding HUF 30 billion (approximately EUR 85 million)
- 0.4 % on a taxable amount in excess of HUF 30 billion but not exceeding HUF 100 billion
- 2.5 % on a taxable amount in excess of HUF 100 billion (approximately EUR 280 million).

Taxpayers have to record and pay tax instalments, and the filing deadline of the yearly tax return is 31 May. As the legislation entered into force during the course of the year, it contains specific rules for the first year. Taxpayers who are not obliged to pay tax do not have to file a tax return.



PKF COMMENT

The introduction of the new tax is in line with government policy aiming at shifting the focus to consumption taxes when shaping the tax system and in parallel decreasing labour taxes. Under this policy, the rate of the social contribution tax will be reduced from 17.5% to 15.5% as from 1 July 2020.

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.

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India

Recent tax developments

Section 115AD – Eligible foreign investors as under SEBI to be FII

Section 115AD of the Income-Tax Act depicts the tax on income of Foreign Institutional Investors (FII) from transfer of securities.

The Central Board of Direct Taxes (CBDT) has provided an explanation to Section 115AD of the

Act that a non-resident being an Eligible Foreign Investor which operates in accordance with the Securities and Exchange Board of India, shall be deemed as Foreign Institutional Investor for the purposes of transactions in securities made on a recognised stock exchange located in any International Financial Services Centre (IFSC), where the consideration for such transaction is paid or payable in foreign currency.

PKF COMMENT

By providing the explanation, The Government of India intends to encourage foreign investment in India and route the investments through the Securities Exchange Board of India (SEBI). As the investments are routed through a reliable organisation like the SEBI it is expected to provide a sense of security to the investors and in turn help to boost foreign investment.



PKF COMMENT

Consideration and relaxation given to business travelers amidst the pandemic situation by the Indian Government comes in as a relief to the individuals in India.

Clarification on Residential Status calculation for Individual for the FY 2019-20- Section 6 of the Income Tax Act (the Act)

The CBDT has made amendments for the individuals who were not able to leave India on or before 31 March 2020 due to the pandemic situation in calculation of days of stay for the purpose of ascertaining the residential status in India for the Financial Year (FY) 2019-20.

On account of genuine hardship faced in leaving India before 31 March 2020, the stay in India from 22 March 2020 to 31 March 2020 shall not be considered for the purpose of ascertaining residential status in India.

India issued safe harbour rates for FY 2019-20 for determining arm's length price

The notification issued by the CBDT states that the same rates as were applicable during the last three financial years, i.e., FY 2016-17 to FY 2018-19, would be applicable for FY 2019-20, for determining

arm's length rates for certain specified industries. Further, the Finance Act, 2020 had amended safe harbour provisions in the Income-Tax Act, 1961, to cover profit attribution for permanent establishments.

PKF COMMENT

This notification indicates that India is attaching importance to profit attribution on global transactions.

India amends Mutual Agreement Procedure (MAP) rules for speedy resolutions

The MAP application can be filed by the Indian resident, aggrieved by the action of the tax authority of any other country outside India. Application is required to be made in a prescribed Form (Form 34F).

The Indian Competent Authority shall receive a reference from the competent authority of the other

country once the MAP application is filed in the country concerned. The Indian Competent Authority shall then convey its acceptance or otherwise for taking up the case in MAP.

The new procedure for giving effect to MAP resolution is proposed to ensure timely closure of the cases resolved under MAP.

PKF COMMENT

The new rules try to make the MAP process more efficient and time bound. It is expected that these rules would lead to speedy settlement of taxpayers' cases.

Key rulings

Paradigm Geophysical Pty Ltd vs. CIT (Delhi Tribunal)

Income from provision of services through high end customised software does not constitute "Fees for Technical Services", u/s 9(1)(vii) as the definition excludes income from "mining or like project".

The question whether income from composite software and maintenance services constitutes "royalty" for purposes of s.44DA would have to be decided based upon the nature of services.

The assessee is eligible to take benefit of the definition of 'royalty' as per the double tax treaty (DTT) for the purpose of applicability of s.44DA.

PKF COMMENT

The Tribunal showed the importance in ascertaining the nature of fees to determine the tax rates. Accordingly, Article 12 of the India USA DTT was considered, and the transaction was taxed as royalty. The Tribunal further dismissed the contention of CIT(A) that the fees attributable to PE are taxable as business income under Article 7. However, considering that this is a tribunal ruling and it may be further deliberated at the higher judicial level.

UOI vs. U.A.E. Exchange Centre (Supreme Court)

Taxability of Liaison Offices under DTTs: The activities carried on by the liaison office of the non-resident in India as permitted by the RBI, demonstrate that the liaison office must steer away from engaging in any primary business activity and in establishing business connection as such. It can

carry on activities of preparatory or auxiliary nature only. A liaison office which is only carrying on such activity of a “preparatory or auxiliary” character is not a PE in terms of Article 5 of the DTT. The deeming provisions in Sections 5 and 9 of the Income tax Act can have no bearing whatsoever (all important judgements referred).

PKF COMMENT

The Hon'ble SC, in the case under consideration, has observed that considering stringent RBI conditions provided in a liaison office approval, the approved activities were preparatory and auxiliary in nature. This ruling comes in as a relief to liaison offices in India.

PILCOM vs. CIT (Supreme Court)

TDS u/s 115BBA, 194E & DTT: As the payments to the Non-Resident Sports Associations represented their income which accrued or arose in India u/s 115BBA, the assessee was liable to deduct Tax at Source u/s 194E. The obligation to deduct Tax at

Source u/s 194E is not affected by the DTT. In case the eligibility to tax is disputed by the recipient, the benefit of DTT can be pleaded and the amount in question will be refunded with interest. However, that by itself, cannot absolve the liability to deduct TDS u/s 194E of the Act.

PKF COMMENT

This ruling lays down the principle that withholding tax obligation under Section 194E of the Income Tax Act is not affected by taxability under the DTT. Hence, it would be prudent for taxpayers to consider the impact of the local laws while making payments to non-residents.

If you believe the above measures may impact your business or require any advice with respect to india taxation, please contact Sudha Ashok at sudha.a@pkfindia.in or call +91 44 2811 2985.

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Italy

Nautical charter services: VAT territoriality

The Revenue Agency has recently published a draft of the measure concerning the so-called “adequate means of proof” with regard to the non-EU navigation of pleasure boats used for leasing (including financial) and chartering.



The aim of the measure is to identify the methods and means to demonstrate the effective use outside the EU territory of “short-term nautical charter” services (as per art. 7-quater, paragraph 1, letter ‘e’ of Presidential Decree no. 633/72 on VAT), i.e. those contracts that provide for the continuous possession or use of pleasure craft for a period not exceeding 90 days.

In particular, it seems that only the test methods used up until now, represented by the lease, charter and other similar (short-term) contracts, normally accompanied by the declaration made by the user of the boat under his own responsibility, are no longer sufficient.

In fact, the Agency specifies that these elements will have to be supported by further specific “means of proof”, differentiated according to whether they are “pleasure boats equipped with satellite navigation systems” or “pleasure boats without satellite navigation systems”.

In the first case, reference shall be made to the information extracted from the satellite navigation systems or transponders (such as A.I.S., “Automatic Identification System”), which shall indicate the sea distance carried out by the vessel.

In the second case, (units without satellite navigation systems) it will be necessary to show at least two of the following means of proof:

- paper or digital navigation logbook or logbook data
- digital photographs of the Vessel Point for each week of navigation identified by any device and recorded at a frequency of at least two for each week of navigation

- documentation proving the mooring of the recreational craft in ports outside the European Union, such as invoices, contracts, tax receipts and related means of payment
- documentation proving the purchase of goods and/or services, in commercial establishments located outside the European Union, relating to the use of the recreational craft outside the European Union, such as invoices, contracts, tax receipts and related means of payment.

Furthermore, it is expected that the supplier and user of the boat will be obliged to keep all the above mentioned documentation (to be made available in case of request by the Financial Administration) for a period of 10 years starting from the year in which the use of the boat started.

We are therefore moving towards the archiving of the system of the so-called “presumed use percentages” of pleasure craft outside EU waters, which has also earned Italy an infringement procedure.



PKF COMMENT

We focused on this matter because in Italy (and especially in a seaside city as Genova) there are a lot of foreign VAT registered companies with an Italian tax representative that provide this type of services.

*If you believe the above measures may impact your business or require any advice with respect to Italian taxation, please contact Stefano Quaglia at s.quaglia@pkf-tclsquare.it or Matteo Macciò at m.maccio@pkf-tclsquare.it or call **+39 0108 183 250**.*

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Jamaica

2020 tax updates

In March 2020, a range of revenue measures aimed at stimulating and growing the economy were introduced for 2020/2021. These are summarized below:

- Reduction in the standard rate of General Consumption Tax (GCT) from 16.5% to 15%
- Reduction in the rate of Assets Tax for Specified Regulated Entities from 0.25% to 0.125%
- MSME Income Tax credit in the amount of JMD 375,000
- Reduction in JACRA/Trade Board Fees.



Reduction in the standard rate of General Consumption Tax (GCT)

Effective 1 April 2020, the standard rate of GCT was decreased from 16.5% to 15%. The other rates of GCT applicable are 25% on telecommunications services and handsets and 10% on tourism activities licensed by the Tourist Board.

This reduction in the standard rate follows on from the increase in the GCT threshold for registration to ten million dollars (\$10M) effective 1 April 2019.

PKF COMMENT

The combination of the two measures, namely the increase of the income threshold to ten million dollars (\$10M) and the reduction of the standard rate of GCT, were intended to encourage growth in the economy but the impact of COVID 19 has been devastating. It is hoped that the economy will rebound soon, as the country, and the world at large, are slowly reopened for business.

Reduction in the rate of Assets Tax for Financial Institutions

For year of assessment 2021, the assets tax payable by specified regulated entities, namely financial institutions and insurance companies, will be reduced by fifty percent (50%) from 0.25% to 0.125%.

Specified regulated entities are therefore still required to file their Assets Tax declaration and settle the assets tax payable. It is to be noted that this tax is not a deductible expense and it has to be passed on to customers of these entities, resulting in high interest rates and financial fees

PKF COMMENT

The assets tax was abolished for non-financial institutions in 2019 and its reduction by fifty percent (50%) for specified regulated entities is welcomed. The Finance Minister has indicated that the assets tax is unproductive and distortive. It disincentivizes these entities from creating assets and encourages those who are able to, particularly international firms, to shift their assets outside of Jamaica to avoid the assets tax. It is hoped that this assets tax will be abolished in the near future.

MSME Income Tax credit in the amount of JMD 375,000

From calendar year 2020, Micro, Small and Medium Enterprises (MSMEs) will be able to access a non-refundable income tax credit of JMD 375,000 once tax returns are filed.

The income tax credit will be available for entities with annual revenues of JMD 500 million or less. The credit may be claimed in addition to any Employment Tax Credit (ETC) available. ETC is available once the business pays its employees' taxes by the due date. The income tax credit must be utilised in the year in which it is granted. It may not be carried forward to be claimed against income tax liabilities in subsequent years of assessment.

PKF COMMENT

Employed and self-employed individuals are not liable for income tax unless their taxable income exceeds an annual tax-free threshold, which is currently JMD 1,500,096 annually. This income tax credit would therefore benefit MSMEs which are incorporated, i.e. companies which are not now entitled to any tax free benefits of this kind. This income tax credit will therefore extend a similar level of tax relief to MSMEs that are in reality self-employed persons who operate on an incorporated basis as companies. This may encourage self employed persons in business to incorporate their business, resulting in the added benefit of limited liability.

Reduction in JACRA/Trade Board Fees

The Jamaica Agricultural Commodities Regulatory Authority (JACRA) is a statutory body responsible for the regulation, standardisation and promotion of the agricultural commodities industry which includes products such as cocoa, coffee, coconut and spices. Farmers are required to pay for licences in order to deal in specified produce and importing or exporting said produce. The Trade Board Limited is a regulatory agency of government which certifies Jamaican exports and issues import and export licences for a fee. The fees charged by JACRA and

the Trade Board were reduced by fifty percent (50%) from 1 April 2020. The reduction in the fees will not apply to motor vehicle related activities. They will both receive government subventions to replace this loss in income.



PKF COMMENT

Statutory bodies and executive agencies have been required to generate sufficient revenues to meet their budgetary requirements so that they are not a burden on the Central Government budget. This has often resulted in increased fees and charges for services or licences or approvals issued by these statutory bodies and agencies. The levels of fees charged by JACRA were placing a significant burden on especially small farmers and was a deterrent to economic growth in the agricultural and business sectors. This initiative is welcomed and should stimulate growth.

If you believe any of the above measures may impact your business or require any advice with respect to Jamaica taxation, please contact Charmaine Madden at charmaine.madden@afmpkf.com or call +1 876 922 1074.

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Kenya

Tax Laws (Amendment) Act, 2020

On 25 April 2020, the President of Kenya assented to the Tax Laws (Amendment) Act, 2020 (the Act). The Act makes various changes to the prevailing tax laws in Kenya. The following tax laws have been amended: The Income Tax Act (ITA), Value-Added Tax (VAT), Excise Duty Act, Tax Procedures Act, Miscellaneous Fees and Levies Act and the Kenya Revenue Authority Act.

This contribution summarises the key changes included in the Act. Unless noted otherwise, the provisions are effective as of 25 April 2020.

Income tax changes

Base for qualifying interest expanded

The Act has amended the definition of qualifying interest to include all interest, discount or original issue discount, receivable by a resident individual in any year of income irrespective of the payer. Prior to this amendment, qualifying interest meant interest earned from a bank or financial institution licenced under the Banking Act, or a building society registered under the Building Societies Act or the Central Bank of Kenya. The amendment allows resident individuals to invest their money in various investment vehicles without paying additional taxes on the interest earned. The applicable tax rate for qualifying interest earned by an individual is 15% and is a final tax.

Broadening the tax net

The Act has introduced withholding tax at the rate of 20% on sales promotion, marketing, advertising services and transportation of goods (excluding air and shipping transport services) paid to non-resident persons not having a permanent establishment in Kenya. However, this will not be applicable for transportation of goods by East African Community citizens.



This amendment is aimed at widening the tax net in order to collect more taxes from non-resident persons who offer the above-mentioned services in Kenya. For instance, payments made to online social media and advertising platforms and other e-commerce platforms for online advertising will now attract withholding tax at 20%. Whereas this is a welcome move to ensure the tax territoriality, i.e. income derived from or accrued in Kenya is taxed in Kenya, it remains a challenge to administer such a tax due to the intangible and fluid nature of such transactions.

Finally, turnover tax grows legs

Since the introduction of turnover tax more than ten years ago, this tax remained a paradox of sorts. It failed to achieve the intended purpose of easing administration of tax for businesses in the informal sector. The sector has largely remained untaxed due to its amorphous nature. After a retinue of amendments to turnover tax provisions, the desired results were never achieved as the tax yield in this category remained inconsequential. It now appears that the government is keen to bring this sector into the tax net in a more robust manner. The Act has thus reduced the turnover tax rate from 3% to 1% and increased its scope to include resident persons with annual turnover of between KES 1 Million and KES 50 million. Previously turnover tax was applicable to resident persons whose annual turnover did not exceed KES 5 million. Additionally, the Act has retained the provision on non-applicability of turnover tax from rental income, professional income and any income which is subject to a final withholding tax. However, incorporated companies, which were previously excluded from the turnover tax regime, can now pay tax under this regime. Further, the Act has scrapped the requirement to pay presumptive tax at the rate of 15% of the amount payable for a business permit. As a consequence, micro-businesses that earn less than KES 1 million are no longer subject to corporation tax.

Higher withholding tax on dividends payments to non-residents

The Act has increased the non-resident withholding tax rate applicable on dividend payments from 10% to 15%. However, the withholding tax rate on dividend payments to citizens of the East African Community Partner States remains at 5% of the gross amount payable.

Electricity rebates for manufacturing sector scrapped

The electricity rebate introduced with effect from January 2019 with a view to cushion manufacturers from heavy costs of production has been scrapped barely 18 months later. The rationale for scrapping this rebate is not clear since the electricity tariff for manufacturers remains unacceptably high. This amendment gives credence to the critique that the income tax laws in Kenya are unpredictable and thus unattractive to investors. One of the basic canons of a good tax system is the principle of certainty, which does not seem to matter to the Kenyan lawmakers.

Clarity on imposition of withholding tax on insurance and re-insurance premiums

The Finance Act, 2018 introduced withholding tax at the rate of 5% on insurance premiums excluding insurance premiums paid for aircrafts. Further, the Finance Act 2019 amended Section 10 to include reinsurance premiums because there was no clarity on the applicability of withholding tax on reinsurance premiums paid to non-residents. However, there was no amendment to Section 34(2) and the Third Schedule to the ITA to complete the withholding tax circuit. The Act has cured this omission. The withholding tax rate applicable to these payments to non-residents still remains 5%.

First Schedule – changes on incomes and persons exempt from tax

Part I of the First Schedule to the Act has been amended to scrap the following income tax exemptions:

Previously exempt income under the First Schedule of the ITA, now taxable
The income of: • The Tea Board of Kenya • The Pyrethrum Board of Kenya • The Sisal Board of Kenya • The Kenya Dairy Board • The Canning Crops Board • The Central Agricultural Board • The Pig Industry Board • The Pineapple Development Authority • The Horticultural Crops Development Authority • The Kenya Tea Development Authority • The National Irrigation Board • The Mombasa Pipeline Board • The Settlement Fund Trustees • The Kenya Post Office Savings Bank • The Cotton Board of Kenya
Profits or gains of an agricultural society accrued in or derived from Kenya from any exhibition or show held for the purposes of the society, which are applied solely to those purposes, and the interest on investments of that society.
Interest on any tax reserve certificates which may be issued by authority of the Government.
Any payment in respect of disturbance, not exceeding three months' salary, made in connexion with a change in the constitution of the Government of a Partner State or the Community to any person who, before such change, was employed in the public service of any of those Governments or of the Community.
The emoluments of any officer of the Desert Locust Survey who is not resident in Kenya.
Any education grant paid by the Government of the United Kingdom under any agreement between that Government and the Government of Kenya and received by any person who is employed in the public service of Kenya or by the Community.
The income received by way of remuneration under any contract which was entered into consequent upon financial assistance being received from the International Co-operation Administration for the enterprise in respect of which the contract was so entered into and which provides that the income shall be exempt from tax.
The income received by virtue of their employment by citizens of the United States of America who are employed by the Department of Agriculture of the United States of America on research work in co-operation with Government.
Gains or profits resultant from any reward paid by the United Kingdom Atomic Energy Authority for the discovery of uranium ore in Kenya, except to the extent that such reward is liable to income tax in a country outside Kenya and there is, between that country and Kenya, provision for any form of double taxation relief.

Previously exempt income under the First Schedule of the ITA, now taxable
All income of any non-resident person not having a permanent establishment in Kenya accrued in or derived from Kenya after 17 June, 1971, and which consists of interest or management and professional fees paid by the Tana River Development Company Limited or its successors in title.
Such part of the income of the East African Power and Lighting Company accrued in or derived from Kenya as is certified from time to time by the Minister to have been expended (whether before or after the date of commencement of this Act) at the request of the Government either— (a) in searching for a natural source in Kenya of geothermal energy; or (b) on investigations concerning the development in Kenya of electric power generation or supply, such exemption to take effect in the year in which the expenditure is incurred.
The income of the General Superintendence Company Limited, a company incorporated in Switzerland, accrued in or derived from Kenya under an agreement dated 18th October, 1972, between the said company and the Central Bank of Kenya.
Such part of the income of an individual, chargeable to tax under section 3(2) (f) as consists of a gain derived from the transfer of— (a) shares in the stock or funds of the Government, the High Commission or the Authority established under the Organization or the Community; (b) shares of a local authority; (c) land which has been adjudicated under the Land Consolidation Act (Cap. 283) or the Land Adjudication Act (Cap. 284) when the title to such land has been registered under the Registered Land Act (Cap.300) and transferred for the first time;
Interest earned on contributions paid into the Deposit Protection Fund established under the Banking Act (Cap. 488).
Interest paid on loans granted by the Local Government Loans Authority established by section 3 of the Local Government Loans Act
Dividends received by a registered venture capital company special economic zone enterprises, developers and operators licensed under the Special Economic zones Act.
Gains arising from trade in shares of a venture company earned by a registered venture capital company within the first ten years from the date of first investment in that venture company by the venture capital company: Provided that the venture company has not been listed in any securities exchange operating in Kenya for a period of more than two years.
Interest income generated from cash flows passed to the investor in the form of asset-backed securities.
Dividends paid by Special Economic Zone Enterprise, developers or operators to any non-resident person.
Compensating tax accruing to a power producer under a power purchase agreement.

Part II of the First Schedule to the ITA has been repealed in its entirety. This schedule exempted from taxes income such as interest payable to non-resident persons on securities such as Kenya Government stocks, Nairobi City Council stocks and East African High Commissions stocks. Most of the exemptions under this part were redundant anyway.

Second Schedule – changes on Capital Allowances

The Act has overhauled the Second Schedule of the ITA on deductions in respect of capital expenditure incurred by a person in the ordinary course of business. The new capital deduction rates are effective immediately, except for Paragraph 24E of

the repealed Schedule, which shall continue to be in force until 31 December 2021.

Paragraph 24E of the Second Schedule was introduced by the Business Laws Amendment Act 2020 assented by the President on 18 March 2020. The provision allows a person who incurs capital expenditure of at least KES 5 billion on the construction of bulk storage and handling facilities for supporting the Standard Gauge Railway operations of a minimum storage of one hundred thousand metric tonnes of supplies to claim investment deduction at the rate of 150% of the capital expenditure.

The new rates are tabled below:

Capital expenditure on	New investment allowance	Previous investment allowance rates	Comments/Notes
a) Buildings			- In case of change of user of a building, investment allowance shall be restricted to unclaimed amount or residual amount - Capital expenditure on the construction of a building excludes cost of acquisition of, or of rights in or over land - Apportionment of investment allowance where the building is put into mixed use.
i. Hotel building	50% - First year of use 25% per year - reducing balance	100% or 150% (if construction cost over KShs 200 Million and constructed outside Nairobi, Mombasa and Kisumu) in the first year of use	

Capital expenditure on	New investment allowance	Previous investment allowance rates	Comments/Notes
ii. Building used for manufacture	50% - First year of use 25% per year - reducing balance	100% or 150% (if construction cost over KShs 200 Million and constructed outside Nairobi, Mombasa and Kisumu) in the first year of use	<i>Building used for manufacture includes any structure or civil works deemed to be part of a building where the structure or civil works relates or contributes to the use of the building)</i>
iii. Hospital building	50% - First year of use 25% per year - reducing balance	0% or 150% (if construction cost over KShs 200 Million and constructed outside Nairobi, Mombasa and Kisumu)	<i>Companies that construct hospital buildings will now enjoy investments allowance at the new rates. This will encourage investment into the sector especially during the COVID pandemic.</i>
iv. Petroleum or gas storage facilities	50% - First year of use 25% per year - reducing balance	10% p.a. on straight-line	
v. Educational buildings including student hostels	10% per year - reducing balance	50% straight line	<i>The educational institution has to be licenced by a competent authority</i>
vi. Commercial building	10% per year – reducing balance	25% per annum straight line for commercial buildings with services or 150% (if construction cost over KShs 200 Million and constructed outside Nairobi, Mombasa and Kisumu)	<i>Commercial building has been defined to include building used as an office, shop, showroom, go down, storehouse, or warehouse used for storage of raw materials for manufacture of finished or semi-finished goods; or civil works relating to water or electric power undertaking, but does not include an undertaking not carried on by way of trade.</i>

	New investment allowance	Previous investment allowance
b) Machinery		
i. Machinery used for manufacture	50% - First year of use 25% per year - reducing balance	100% or 150% (if cost over KShs 200 Million and constructed outside Nairobi, Mombasa and Kisumu) in the first year of use
ii. Hospital Equipment	50% - First year of use 25% per year - reducing balance	12.5% per annum on reducing balance
iii. Ships or Aircrafts	50% - First year of use 25% per year - reducing balance	25% per annum for aircrafts 12.5% per annum for ships of less than 125 tonnes 100% for ships of more than 125 tonnes
iv. Motor vehicles and heavy earth moving equipment	25% per year, - reducing balance <i>Capping on value of non-commercial motor vehicles increased from KShs 2 Million to KShs 3 Million</i>	25% for motor vehicles and 37.5% for heavy earth moving equipment
v. Computer and peripheral computer hardware and software, calculators, copiers duplicating machines	25% per year, - reducing balance	30% for computer hardware on reducing balance and 20% for software on straight line basis
vi. Furniture and fittings	10% per year - reducing balance	12.5 percent per annum on reducing balance basis
vii. Telecommunications equipment	10% per year - reducing balance	20% per annum on straight-line basis
viii. Filming equipment by a local film producer licenced by the cabinet secretary responsible for filming	25% per year - reducing balance	100% allowance
ix. Machinery used to undertake operations under a prospecting right	50% - First year of use 25% per year - reducing balance	20% p.a. on straight-line
x. Machinery used to undertake exploration operations under a mining right	50% - First year of use 25% per year - reducing balance	20% p.a. on straight-line
xi. Other machinery	10% per year - reducing balance	12.5 % per annum
c) Purchase of an acquisition of an indefeasible right to use fibre optic cable by a telecommunication operator	10% per year - reducing balance	5% per annum
d) Farm works	50% - First year of use 25% per year - reducing balance	100% for the first year. Only one-thirds of a farm house would qualify

Third Schedule Head A- Revised Resident Tax Relief

Personal relief has been increased from KES16,896 per annum (KES 1,408 per month) to KES 28,800 per annum (KES 2,400). This means that persons earning a monthly income of KES 24,000 or less will not pay tax on their income with effect from April 2020.

Third Schedule Head B - Revised resident individual tax rates

The Act has widened the resident individual income tax bands as follows:

Monthly Taxable Pay (KShs)	Annual Taxable Pay (KShs)	Rate of Tax (%)
Up to 24,000	Up to 288,000	10
24,001 - 40,667	288,001 - 488,000	15
40,668 - 57,333	488,001 - 688,000	20
Above 57,333	Above 688,000	25

The above amendments are aimed at cushioning individuals from the economic impacts of the COVID-19 pandemic with a view to ensure that individuals have increased disposable income.

Previous resident individual tax rates are tabulated below:

	Monthly Taxable Pay (KShs)	Annual Taxable Pay (KShs)	Rate of Tax (%)
On the first	12,298	147,580	10
On the next	11,587	139,043	15
On the next	11,587	139,043	20
On the next	11,587	139,043	25
On all income over	47,059	564,709	30

Revised Withholding Tax rate on pension/ provident withdrawals

The Act has also amended the withholding tax rates for pension/provident fund withdrawals and lump sum payments beyond exempt limits as follows.

a) Withdrawal before 15 years expires

Rate of Tax (%)		Old Tax Bands (KShs)	New Tax Bands (KShs)
10	On the first	147,580	288,000
15	On the next	139,043	200,000
20	On the next	139,043	200,000
25	On the next	139,043	688,000 and above
30	On all income over	564,709	

In addition to the above, the applicable tax rate for withdrawal or refund of surplus funds to an employer in respect of registered pension or registered provident funds, has reduced from 30% to 25% of the gross sum payable.

b) Withdrawal after 15 years, attaining age of 50 years or retirement on health grounds

Rate of Tax		Old tax bands	New tax bands
10%	On the first	400,000	400,000
15%	On the next	400,000	400,000
20%	On the next	400,000	400,000
25%	On the next	400,000	1,200,000 and above
30%	On all income over	1,600,000	

Third Schedule Head B - Revised corporate tax rates

The Act has amended the corporate tax rates as follows:

Corporate entity	New corporate tax rate	Previous corporate tax rate	Impact
Resident company	25%	30%	The new income tax is applicable with effect from 25 April 2020. The amendment is aimed at cushioning taxpayers from the economic impacts of COVID-19
Life insurance income earned by a resident insurance company	25% based on specific criteria	30% based on specific criteria	The effective date is 25 April 2020. Similarly, this is aimed at mitigating the impact of COVID-19
Newly listed company with over 30% capital listed	25%	25% for the first five years	The original intention for the reduced rate of tax was to encourage listing in the NSE. This incentive should have been transient and since the NSE has become of age.
Newly listed company with over 40% capital listed	25%	20% for the first five years	The original intention for the reduced rate of tax was to encourage listing in the NSE. This incentive should have been transient and since the NSE has become of age
Company introducing shares through listing	25%	25% for the period of five years commencing after listing	The original intention for the reduced rate of tax was to encourage listing in the NSE. This incentive should have been transient and since the NSE has become of age
Company operating a plastics recycling plant	25%	15% for the first five years	The 15% rate was introduced in 2019 year of income. The scrapping of this rate even before it has benefitted the entities that invested in this sector with the incentive in mind is very unfortunate. It paints Kenyan tax system as being very uncertain.
Company operating under a special operating framework arrangement with the Government	The rate specified in the agreement shall continue to apply for the unexpired period as provided under the agreement.	To the extent provided in the arrangement.	This arrangement will be very useful post COVID -19 as global companies are likely to be looking for new production sites to reduce over reliance on China as the global manufacturing hub. This framework can be used to target strategic investors to position Kenya as a manufacturing hub.

Value Added Tax changes

Expanded base for VAT on petroleum products

With effect from 15 May 2020 the base for computation of VAT on petroleum products has been changed to include excise duty, fees and other charges. These were previously excluded from the taxable value for petroleum products. The impact of this is to increase the cost of petroleum products to the end consumer.

Issue of credit notes

The Act has introduced a thirty-day window for issuance of credit notes where there is a commercial dispute in court with respect to the price payable. The credit note should be issued within thirty days after the determination of the matter.

This is a welcome provision because it will allow taxpayers to claim VAT upon determination of a dispute in court with regard to the price payable. Previously, such VAT would be lost because credit notes were limited to a period of six months from the date of issuance of a tax invoice.

Refund arising from bad debts

The Act has reduced the period for making an application for refund arising on bad debts from five years to four years from the date of the supply.

Reclassification of zero rated category to exempt category

The following vaccines and medicaments, which were previously zero rated, are now VAT exempt.

3002.20.00	Vaccines for human medicine
3002.30.00	Vaccines for veterinary medicine
3003.10.00	Medicaments containing penicillin or derivatives thereof, with penicillanic acid structure, or streptomycin or their derivatives
3003.39.00	Other medicaments, containing hormones or other products of heading No. 29.37 but not containing antibiotics, not put up in measured doses or in forms or packings for retail sale.
3003.40.00	Medicaments containing alkaloids or derivatives thereof but not containing hormones or other products of heading No. 29.37 or antibiotics, not put up in measured doses or in forms or packings for retail sale
3003.90.00	Other
3003.90.10	Infusion solutions for ingestion other than by mouth not put up in measured doses or in forms or packings for retail sale.

3003.90.90	Other medicaments (excluding goods of heading No. 30.02, 30.05 or 30.06) consisting of two or more constituents which have been mixed together for therapeutic or prophylactic uses, not put up in measured doses or in forms or packings for retail sale.
3004.10.00	Medicaments containing penicillin or derivatives thereof, with a penicillanic acid structure, or streptomycin or their derivatives, put up in measured doses or in forms or packings for retail sale.
3004.20.00	Medicaments containing other antibiotics, put up in measured doses or in forms or packings for retail sale.
3004.32.00	Medicaments containing adrenal cortical hormones, put up in measured doses or in forms or packings for retail sale.
3004.39.00	Other medicaments containing hormones or other products of heading No. 29.37 but not containing antibiotics, put up in measured doses or in forms or packings for retail sale
3004.41.00	Containing ephedrine or its salts
3004.42.00	Containing pseudoephedrine (INN) or its salts.
3004.49.00	Other
3004.50.00	Other medicaments containing vitamins or other products of heading No. 29.36 put up in measured doses or in forms or packings for retail sale.
3004.90.00	Other medicaments (excluding goods of heading No. 30.02, 30.05 or 30.06) consisting of mixed or unmixed products, for therapeutic or prophylactic uses, put up in measured doses or in forms or packings for retail sale.
3004.90.90	Other medicaments (excluding goods of heading No. 30.02, 30.05 or 30.06) consisting of mixed or unmixed products, for therapeutic or prophylactic uses, put up in measured doses or in forms or packings for retail sale.

Additionally, personal protective equipment, including facemasks, for use by medical personnel in registered hospitals and clinics, or by members of the public in the case of a pandemic or a notifiable infectious disease are now exempt from VAT. These were previously Vatable. It should be recognised that exemption of previously zero-rated items will in fact increase their cost of manufacture as suppliers of such items will be unable to claim VAT on their inputs.

Re-classification of Exempt supplies to taxable supplies

The following supplies which were exempt from VAT under the First Schedule to the VAT Act, 2013 will now attract VAT at a rate of 14%:

- Plant and machinery of chapter 84 and 85 used for the manufacture of goods
- Taxable supplies, excluding motor vehicles, imported or purchased for direct and exclusive use in the construction of a power generating plant, by a company, to supply electricity to the national grid approved by Cabinet Secretary for National Treasury upon recommendation by the Cabinet Secretary responsible for energy

- Taxable supplies, excluding motor vehicles, imported or purchased for direct and exclusive use in geothermal, oil or mining prospecting or exploration, by a company granted prospecting or exploration license in accordance with Geothermal Resources Act (Cap. 314A), production sharing contracts in accordance with the provisions of Petroleum (Exploration and Production) Act (Cap. 308) or mining licence in accordance with the Mining Act (Cap. 306), upon recommendation by the Cabinet Secretary responsible for energy or the Cabinet Secretary responsible for mining, as the case may be
- Taxable supplies, procured locally or imported for the construction of liquefied petroleum gas storage facilities with a minimum capital investment of KES 4 billion and a minimum storage capacity of fifteen thousand metric tonnes as approved by the Cabinet Secretary for National Treasury upon recommendation by the Cabinet Secretary responsible for liquefied petroleum gas
- Plastic bag biogas digesters
- Biogas
- Leasing of biogas producing equipment
- Parts imported or purchased locally for the assembly of primary school laptop tablets, subject to approval by the Cabinet Secretary for the National Treasury, on recommendation by the Cabinet Secretary responsible for matters relating to information technology
- Taxable goods purchased or imported for direct and exclusive use in the construction and infrastructural works in industrial parks of one hundred acres or more including those outside special economic zones approved by the Cabinet Secretary for the National Treasury
- Museum and natural history exhibits and specimens and scientific equipment for public museums
- Chemicals, reagents, films, film strips and visual aid equipment imported or purchased prior to clearance through the customs by the National Museums of Kenya
- Goods falling under tariff number 4907.00.90
- Materials for the construction of grain storage,



upon recommendation by the Cabinet Secretary for the time being responsible for agriculture

- The transfer of a business as a going concern by a registered person to another registered person
- Taxable goods supplied to marine fisheries and fish processors upon recommendation by the relevant state department
- Goods imported or purchased locally for direct and exclusive use in the implementation of projects under a special operating framework arrangements with the Government
- Taxable services provided for direct and exclusive use in the construction and infrastructural works in industrial parks of one hundred acres or more including those outside special economic zones approved by the Cabinet Secretary for the National Treasury
- Taxable services, procured locally or imported for the construction of liquefied petroleum gas storage facilities with a minimum capital investment of KES 4 billion and a minimum storage capacity of fifteen thousand metric tonnes as approved by Cabinet Secretary for National Treasury upon recommendation by the Cabinet Secretary responsible for liquefied petroleum gas
- Asset transfers and other transactions related to the transfer of assets into real estate investment trusts and asset backed securities
- Services imported or purchased locally for direct and exclusive use in the implementation of projects under special operating framework arrangements with the Government
- Insurance agency, insurance brokerage and stock exchange brokerage services.

Excise Duty Act changes

Clarification on applicability of excise duty on financial services

The Act has amended the definition of 'other fees' subject to excise duty by deleting the phrase 'licenced financial institutions' and replacing it with 'licenced activities'. This amends a previous drafting error in the definition but also clarifies that excise duty is only applicable on fees charged by financial institutions on their licenced activities but not on all activities they undertake. This creates a level playing field as some financial institutions undertake similar activities to non-financial institutions that do not charge excise duty on their activities.

Repealed excise duty exemptions

The following excise duty exemptions have been repealed:

- Goods imported or purchased locally for direct and exclusive use in the implementation of projects under special operating framework arrangements with the Government
- One personal motor vehicle imported by a public officer returning from a mission abroad and another one by their spouse.

Tax Procedures Act changes

Private rulings

The Act has extended the timeline within which the Commissioner is required to respond to private rulings from 45 days to 60 days. An extension of time is viewed as an attempt by the Commissioner to meet the deadlines. However, our recommendation is that the Commissioner needs to actually work within these timelines since delays in issuance of private rulings affect business decisions and investments.

Publication of private rulings

The Act has repealed the section requiring the Commissioner to publish private rulings in at least two daily newspapers with national circulation. This can be viewed as an attempt by the Commissioner to avoid administrative burdens and costs of having to publish private rulings despite the fact that he was

required to maintain the confidentiality of the applicant.

Turnover tax late return submission penalty

The Act has reduced the late filing return filing penalty for resident persons under turnover tax from KES 5,000 to KES 1,000. This move is aimed at ensuring that resident persons in the informal sector are not heavily penalised for non-compliance and should encourage uptake of the turnover tax regime.

Miscellaneous Fees and Levies Act changes

No Import Declaration Fee reprieve for approved manufacturers

Under the Act, Import Declaration Fee at the blanket rate of 1.5% of the CIF value would be applicable to raw materials and intermediate products imported by approved manufacturers only upon recommendation and approval by the Cabinet Secretaries in charge of the Ministry of Industrialisation and the National Treasury respectively. However, we hope that the introduction of this mandatory requirement will not introduce bottlenecks to manufacturers.

Introduction of processing fee on motor vehicle imports

The Act has introduced a processing fee of KES 10,000 on all motor vehicles excluding motorcycles imported or purchased duty free prior to clearance by certain privileged persons under the Fifth Schedule to the East African Community Customs Management Act.



Repealed Import Declaration Fee and Railway Development Levy exemptions

The following would no longer be exempt from IDF and/or RDL:

- Gifts or donations, excluding motor vehicles, by foreign residents to their relatives in Kenya for their personal use
- Samples which in the opinion of the Commissioner have no commercial value
- Raw materials for direct and exclusive use in construction by developers or investors in industrial parks
- Goods imported for the construction of liquefied petroleum gas storage facilities

- Goods imported for implementation of projects under the special operating framework arrangement with the government

The Kenya Revenue Authority Act changes

Appointment of agents

The Act has given the Commissioner of KRA powers to appoint any person registered under the Banking Act to act as KRA's agent for revenue banking services through an agreement. This measure is aimed at streamlining KRA's enforcement measures.

PKF COMMENT

For further information or advice on Kenyan taxation, please contact Michael Mburugu at mmburugu@ke.pkfea.com or call +254 20 42 70000.

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Luxembourg

Non-deductibility of interest and royalties paid to group entities located in blacklisted countries

On 30 March 2020, the Luxembourg government published bill No. 7547, amending article 168(4) of the income tax law (ITL).

This proposal has been made in light of the European Union Council's conclusions issued on 5 December 2017 whose purpose was the adoption of defensive measures against non-cooperative countries.

Based on the text of the bill, as from 1st January 2021, interest and royalties paid or due will not be tax deductible when the following conditions are cumulatively met:

- Only payments made between associated enterprises pursuant to art. 56 ITL are covered by this measure.
- The beneficiary must be located in a blacklisted jurisdiction. Please note that only the beneficial owner of the payments must be considered as beneficiary for this purpose (look-through approach).

The blacklist should be published before 1st January 2021 and updated once a year in the Luxembourg Budget Law (based on the list published in the EU Official Journal).

New additions to the list would be taken into account as from the 1st January of the following year. Any withdrawals would be taken into account as from the publication date of the list in the Official Journal of the EU.

For the time being, and since 27 February 2020, this EU blacklist includes 12 jurisdictions: American Samoa, Cayman Islands, Fiji, Guam, Oman, Palau, Panama, Samoa, Trinidad and Tobago, Vanuatu and the US Virgin Islands.

- The beneficiary is a “collective undertaking” within the meaning of art. 159 ITL (i.e. joint-stock companies/corporate bodies).

Interest and royalty payments will however remain deductible if the operation is supported by valid commercial reasons reflecting the economic reality and to the extent that, based on the relevant facts and circumstances, these reasons can be considered as real and offering a sufficient economic advantage beyond the potential tax advantage obtained through the operation.

PKF COMMENT

Multinational groups should verify whether any interest or royalty payments involve entities located in non-cooperative jurisdictions (not only as the recipient of the payment but also as a beneficial owner of the income). In that case, it would be recommended to consider alternative options taking into account the fact that similar measures could also exist in other EU Member States.

It is also worth noting that the bill has not yet been approved by the Luxembourg Parliament.

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Upcoming modification of withholding tax rates on dividends and interest between Luxembourg and Russia

In April 2020, an official letter was addressed to the Luxembourg Ministry of Finance upon request of Russian president Vladimir Putin.

In this letter, Russia expressed its intent to renegotiate the current withholding tax rates applied on dividends and interest currently provided for by the double tax treaty concluded between Luxembourg and Russia.

The Russian Ministry of finance requested the following amendments to be implemented as from 1st January 2021:

- An increase of the withholding tax rate applied on dividends from 5% (subject to conditions) to 15% (art. 10 of the treaty); and
- An increase of the withholding tax rate applied on interest from 0% (subject to conditions) to 15% (art. 11 of the treaty).

The purpose of this modification is to avoid “treaty shopping” in situations where Luxembourg conduit companies are used, as an intermediary, to access preferential withholding tax rates.

The double tax treaty in force between Luxembourg and Russia is not the only one to be impacted by a change in withholding tax rates as similar correspondence has been received from Cyprus and Malta.



PKF COMMENT

Multinational groups should verify whether any dividend or interest payments are made between Luxembourg and Russia to determine the impact of this change on their structures.

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Upcoming changes for securitisation vehicles

On 14 May 2020, the European Commission sent letters of formal notice to Luxembourg, as part of its infringement procedure, to request the following amendments to be made to existing Luxembourg tax law:

- The inclusion of securitisation vehicles governed by EU Regulation No. 2017/2402 into the scope of the Luxembourg interest limitation rules (which are part of the so-called “ATAD I” measures).

Pursuant to art. 168bis, para. 1, 7), (j), ITL, said securitisation vehicles are currently not subject to the rules related to the limitation of

interest deductions. They were excluded as “financial undertakings” which, in the opinion of the Commission, goes beyond the permitted exclusions. However, credit institutions, insurance and reinsurance companies, AIF and UCITS should remain out of the scope of the interest limitation rules.

It is worth noting that Portugal received the same type of notice.

- Taxation of Luxembourg and foreign securitisation vehicles should be aligned. A more onerous taxation is currently applied on foreign entities having their statutory seat in another EU Member State and carrying out taxable operations in Luxembourg, which is not in line with the EU freedom of establishment.

PKF COMMENT

Securitisation vehicles in Luxembourg should expect new developments in this respect within the next few months as Luxembourg will likely align its legislation with the views of the European Commission.

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Possible switch from a vertical to a horizontal tax unity regime in Luxembourg

On 14 May 2020 (case C-749/18, B and Others v ACD), the European Court of Justice (ECJ) ruled that the Luxembourg tax unity regime is contrary to the EU freedom of establishment due to the existing distinction between “vertical” and “horizontal” tax consolidation regimes.

Indeed, based on current legislation, a group may opt either:

- for a “vertical” tax unity: integration between the integrating Luxembourg parent company and its Luxembourg subsidiaries; or
- for a “horizontal” tax unity: integration between Luxembourg sister companies (held by a non-resident and non-integrating parent company). Taxable income is then consolidated at the level of a Luxembourg integrating (top) subsidiary.

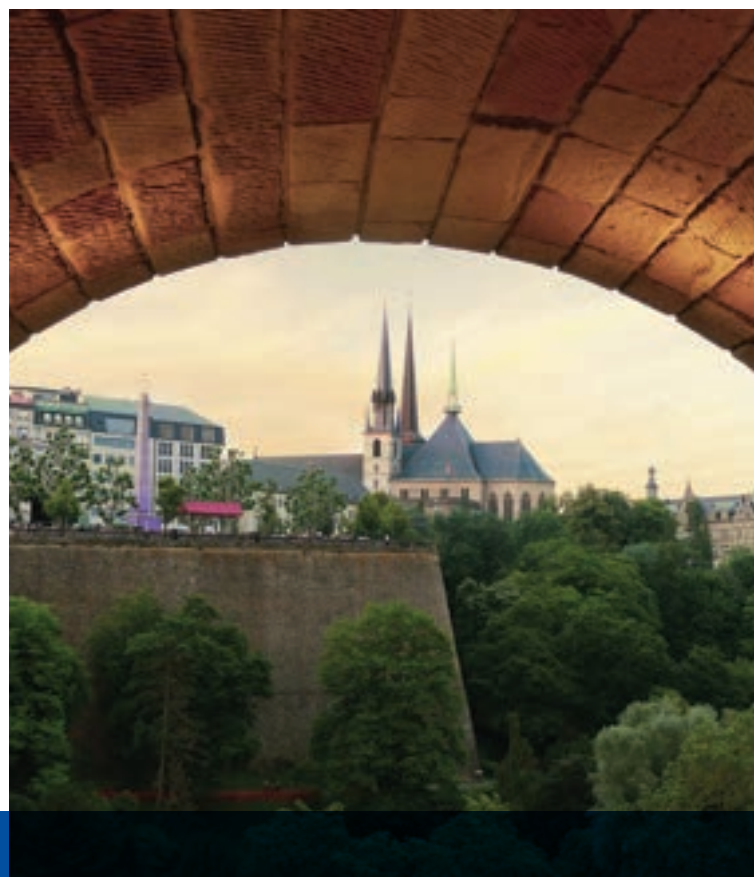
In the case at hand, a vertical tax unity was already in place between the Luxembourg parent company, LuxCo A (which was held by a French company) and several Luxembourg subsidiaries.

LuxCo B and C, although not held by LuxCo A, were indirectly owned by the same French company and wanted to become part of the existing tax unity regime. The envisaged tax unity would thus have been constituted by Luxembourg sister companies A, B and C (and potentially their Luxembourg subsidiaries) while LuxCo A would have remained the integrating company for the group, thus creating a horizontal tax unity.

The tax authorities, however, refused the request of the group to switch from a vertical to a horizontal tax unity. Indeed, based on article 164bis ITL, a company may not be part of more than one tax consolidated group at a time.

The horizontal tax unity could nevertheless have been established but it would have required the prior dissolution of the vertical tax unity.

However, a fiscal unity in Luxembourg must remain in place for at least 5 consecutive years (at the level of each participating entity). If not, a modification of the previous tax assessments is automatically performed by the tax authorities. Hence, the dissolution would have entailed adverse tax consequences (with retroactive effect) for the group.



PKF COMMENT

The ECJ ruled in favour of a more flexible approach to the tax consolidation regime in Luxembourg. Further developments are thus expected on this regime in future, assuming that the Luxembourg legislator decides to amend current tax law taking into account the comments made by the ECJ in this ruling. For further information or advice concerning recent events or any advice with respect to Luxembourg taxation, please contact Aurélie Moline at aurelie.moline@pkf.lu or call +352 39 58 42 82.

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Mexico

New tax scheme for Digital Platforms

As part of the 2020 Mexican tax reforms, a new tax scheme entered into force effective 1 June 2020 regarding foreign digital platforms at the level of both Mexican resident and non-resident entities providing services or selling goods into Mexico. The salient features of these new VAT and withholding tax obligations can be summarised as follows:

- Foreign digital platforms providing services or selling goods into Mexico will need to charge Mexican VAT on their sales and remit such tax to the Mexican tax authority;
- Likewise, foreign digital platforms intermediating between sellers and buyers of goods or services (including lodging) will need to withhold VAT and withholding tax from the Mexican sellers and remit these to the Mexican tax authority.

For compliance purposes, the foreign digital platforms will, among others, be required to appoint a Mexican legal representative and register with the Mexican tax authority.

As from 1 June 2020, digital platform operators will need to comply with the following obligations, among others:

- Registration with the Federal Taxpayers Registry in order to obtain a Mexican tax ID and electronic signature
- Payment on a monthly basis of VAT and withholding taxes
- Provide proof of withholding to service recipients
- Provide certain information about service providers to the Mexican Tax Authority on a monthly basis.

It is worth mentioning that for the provision of digital services the creation of a permanent establishment in Mexico is not required at the level of the non-resident.

PKF COMMENT

Digital Platform entities need to ensure they comply with these newly enacted tax obligations as failure to do so will result in fines.

For further information regarding these new rules or any advice with respect to Mexican taxation, please contact Antonio Garcia at antonio.garcia@pkfmexico.com or call +52 (81) 8363 8311 and Jimmy Cruz at jimmy.cruz@pkf.com.mx or call +52 (33) 3122 2081.

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Nepal



Major amendments to direct and indirect tax laws as per Finance Act 2020

On 28 May 2020, the Finance Minister, Government of Nepal presented the full budget for the FY 2020-21 together with the Finance Act, 2020 to amend the direct and indirect tax laws to facilitate the collection of revenue in the ensuing fiscal year. The major amendments made to the tax laws through the Finance Act, 2020 are as follows.

Direct tax

- Period of tax exemption for micro enterprises has been increased by 2 years, from 5 years to 7 years, and further increased by 3 years in case of micro-enterprises operated by women, i.e., to 10 years.
- The hotel, travel, trekking, transport and airline industry with annual turnover in excess of NPR 10 million shall be entitled to a 20% tax rate rebate bringing down the tax rate applicable to these industries to 20%.
- The contributions made to the Corona Fund established by the Federal, Provincial and Local Governments shall be deductible for computation of taxable income for the FY 2019-20.
- Reduction in service fee of 2% of the transaction amount to 1% in case of Radio and Television Broadcasting Institutions producing and airing their own programs. Internet service provider (via fixed broadband) will be allowed concession on telecom service fee of up to 50% of repair and maintenance expenses.
- A discount of 25% on income tax rate has been provided for the first five years of operation to special industries established in industrial areas or industrial villages.
- 100% exemption on income tax for first five years from the date of operation of business and 50% concession for next 3 years for special industries and tourism industries (except casino)

with capital investment of NPR 2 billion or more and providing direct employment to more than 300 persons throughout the year.

- 50% concession on income tax has been announced for entities established in zoological, geological, biotech park and IT parks engaged in software development, data processing, cybercafé or digital mapping.
- Rebate in the tax rates by 40% and 25% for 10 years from the date of commercial production has been granted to industries established in very undeveloped and undeveloped areas, respectively and producing brandy, wine, cider from fruits.
- Income tax has been exempted for Drinking Water and Sanitation Consumer Groups operating as per their objectives. Income tax waived on tax assessed up to FY 2019-20.
- Income tax exemption has been granted to cooperatives operating in rural municipalities whereas income tax levied at 5%, 7% and 10% on cooperatives operating in municipality, sub metropolitan and metropolitan cities, respectively conducting taxable transactions.
- Waiver in tax applicable on retirement payment if approved retirement fund operated in different institutions transferred to Social Security Fund by 13 April 2021. Other retirement funds shall be gradually phased out.

Indirect tax

- Provisions of the filing of returns and payment of taxes on a trimester basis for transportation, tourism and movie theatre sectors have been introduced as a relief measure from the COVID-19 pandemic.
- The VAT amount paid by United Nations Organisation and specialised agencies on purchase of goods and services for staying in Nepal for their objectives shall be refunded.
- Where a person requiring VAT registration, operates without a registration, such person may be penalised with 50% of payable tax amount.

The VAT paid by pharmaceutical industries on local purchases of raw materials, auxiliary and packing materials will be refunded within 60 days from the date of the application for refund of VAT on trimester basis.



PKF COMMENT

The Government of Nepal (GoN) through the budget speech and finance act has made several amendments to the direct and indirect tax laws which may affect individuals and entities in Nepal. Nepal taxpayers should familiarise themselves with these new tax rules effective for the FY 2020-21.

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Major amnesties announced by Finance Act 2020

On 28 May 2020, the GoN announced various tax amnesties through Finance Act, 2020 to provide relief to taxpayers in the midst of the current COVID-19 crisis and to expand the tax ambit for enhancing revenue collection.

Amnesty for withdrawal of appeals on disputed taxes

Where the taxpayer withdraws the appeals made at various levels on account of disputed taxes up to 16 July 2018 (Administrative Review, Revenue Tribunal or in the appellate Courts) and pays the applicable taxes and interest assessed by the tax officer as per the final assessment order, the applicable fee, additional charges and penalty shall be waived for all such cases filed under the Income Tax Act 2002, Value Added Tax Act, 1996 and Excise Act, 2002.

PKF COMMENT

This amnesty provides an opportunity to taxpayers to review their petition at various appellate authorities and consider withdrawing such cases where there is a likelihood that the decision will not be in their favour, thus saving on the payment of applicable fees, additional fee and penalty.

Amnesty for unregistered persons by submitting returns for two fiscal years

If any taxpayer registers and obtains Permanent Account Numbers (PAN) and submits the tax returns

for FY 2018-19 and 2019-20 and deposits the applicable tax by 13 March 2021, the interest and penalties for the above period and the taxes, interest and penalties for earlier years will be waived.

PKF COMMENT

This one-time opportunity should be opted for by unregistered persons having taxable income earned from legal source as the GoN, to meet its challenging revenue targets, would adopt stringent measures to collect taxes, including interest and penalties in future.

The GoN has provided this amnesty with an objective of spreading its tax net rather than raising tax rates to increase revenue collection.

Amnesty for natural persons or entities with specified turnover

If a natural person with turnover of up to NPR 5 million is already registered under PAN but has not submitted tax returns, and submits the tax returns for FY 2017-18, 2018-19 & 2019-20 and deposits the applicable taxes and 25% of the interest by 13 March 2021, the additional charges, fees and

penalties for the above period and the taxes, interest and penalties for earlier years will be waived.

Where a natural person or entity with turnover of more than NPR 5 million has obtained PAN but has not submitted the returns for FY 2017-18 and earlier, and submits the tax returns and pays the taxes and 25% of the interest by 13 March 2021, the fees and the balance interest shall be waived.

PKF COMMENT

Registered MSMEs and natural persons should opt for this amnesty to benefit from the waiver. Once taxes are paid, they shall be eligible to avail credit facilities from banks and financial institutions for the expansion of their business.

The GoN could have provided additional concessions on interest to attract more taxpayers to opt for this amnesty and extend the period until fiscal year 2075-76 for taxpayers with turnover in excess of NPR 5 million. Additionally, consideration could have been made to pay the tax in instalments due to cash crunch affecting businesses during the pandemic.

Amnesty for VAT-registered persons

Where a VAT-registered person, who has not filed and paid taxes up to mid-July 2018, submits the VAT returns and pays the applicable taxes and 50% of the interest by 13 March 2021, the applicable penalties, additional fees and remaining interest shall be waived.

Those taxpayers who have not filed their returns by Ashad 2073 will be automatically deregistered. Charges applicable for late filing of the returns shall be waived. However, the remaining due taxes, interest and fees shall be recovered.



PKF COMMENT

VAT-registered taxpayers who have defaulted by not filing the returns and depositing the taxes should opt for this amnesty as there will be significant savings from not paying interest, additional fees and penalties.



PKF COMMENT

This is a one-time opportunity to clear all taxes outstanding under the repealed laws with a discount of NPR 50,000 and to remove one's name from the list of tax defaulters. Where the due tax is less than NPR 50,000 it is assumed that the entire due is waived but the taxpayer has to update the records with the tax authorities.

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Amnesty for assessments under the repealed direct and indirect tax laws

NPR 50,000 on each assessed tax and interest thereon shall be waived if the assessed taxes outstanding under the following laws are paid:

- a) Income Tax Act, 2031 but not yet recovered; and
- b) Taxes assessed under the repealed sales tax, entertainment tax, contract tax, hotel tax which were replaced by the VAT Act, 1996 and outstanding up to mid-July fiscal year 2060.

Eligible deduction on contribution to Social Security Fund

With the 10th amendment to Income Tax Rule 2003 Rule 21, the deduction limit for amounts contributed to the Social Security Fund (SSF) has been increased to NPR 500,000 from the current NPR 300,000.

Henceforth, natural persons contributing to the SSF will be allowed to deduct an amount equal to at least the actual amount, or 1/3rd of assessable income, or NPR 500,000.

PKF COMMENT

This provision will be beneficial to natural persons earning income from employment and business and contributing to the Social Security Fund. Furthermore, such limit increase will enhance the participation in the Social Security scheme recently introduced by the Government of Nepal.

For further information or advice on Nepal tax laws or if you have any specific query about your particular tax situation, please contact Shashi Satyal at shashi.satyal@pkf.com.np or call +977 01 441 0927.

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Poland

Mandatory Disclosure Rules (MDR) in Poland

Poland was the first EU member state to implement the so-called MDR Directive, i.e. Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU regarding the mandatory automatic exchange of information in the field of taxation with respect to notifiable cross-border arrangements abbreviated as DAC6, although the transposition into domestic law only had to be done by the end of 2019. The obligation of reporting tax arrangements has been in force since 1 January 2019, i.e. 18 months earlier than the deadline required by DAC6.

The MDR Directive imposes an obligation to disclose information on tax arrangements only in cross-border transactions regarding income taxes. However, Polish legislation extends beyond the minimum requirements imposed by DAC6 to report tax benefits covering all taxes, including domestic transactions if the criterion of a qualified beneficiary is met, i.e.

- when the beneficiary is an entity with revenues, deductible costs or the value of assets exceeding the equivalent of EUR 10 million in the current or previous financial year; or
- the arrangement involves assets or rights with a fair market value exceeding EUR 2.5 million.

In addition, the reporting obligation in Poland also applies to events that took place before the provisions came into force i.e.

- after 25 June 2018 - in case of cross-border schemes; and
- after 1 November 2018 - in case of non-cross-border schemes,

so the principle of non-retroactivity has been ignored.

Moreover, Poland has introduced the obligation to report transactions by tax advisers, attorneys and legal advisors, so these provisions are undermining the foundation of these professions, i.e. professional secrecy.

There are onerous penalties in place for not reporting MDRs or reporting after the deadline. Non-fulfilment of reporting obligations will constitute a criminal offence and will be subject to a fine of up to PLN 25 million (approximately EUR 5.5 million).

The following table illustrates the differences between national and EU requirements - DAC-6 relating to MDR reporting:

National (Polish) requirements	EU requirements
National and cross-border tax schemes are reported as well within all taxes	Cross-border tax schemes are reported within income taxes
Broad definition of the tax schemes	Limited definition of cross-border tax schemes
Information on the schemes is submitted according to the so-called national scheme	Information on the schemes is submitted according to the so-called EU scheme
The MDR regulations apply from 1 January 2019.	The time for implementation DAC-6 directive was predicted for the end of 2019 for EU countries.

PKF COMMENT

The requirement to report tax arrangements is imposed by the EU directive. However, Poland has introduced much wider provisions (obligation to report domestic transactions, tax benefits regarding all taxes), but also complicated and ambiguous ones, and the wide scope of definitions of the tax arrangement may lead to the conclusion that reporting is subject to anything that can reduce taxation.

In order to avoid onerous sanctions, we recommend companies and entrepreneurs to implement the MDR procedure, as well as to analyse transactions in terms of the occurrence of the tax arrangements, and thus the obligation to report under the MDR.

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.

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Rwanda

Changes to the Quarterly Instalment Tax Regime

The Rwanda Revenue Authority has announced changes to how quarterly instalment tax (IQP) will be computed for the year 2020. This tax measure has been introduced to cushion taxpayers who are experiencing decline in business activity due to the ongoing covid-19 pandemic.

The IQP tax in Rwanda has previously been based on prior year corporate tax liability at the rate of 25% of the prior year tax. However, in 2020, the IQP will be determined based on current year quarterly revenue multiplied by the tax-to-turnover ratio of 2019.

PKF COMMENT

This is a welcome intervention since the previous regime would have been punitive to businesses that posted high profits in 2019 but who have subsequently experienced a significant slump in revenue in 2020 due to the ongoing pandemic. This will come as a huge relief for taxpayers in sectors such as hospitality and tourism, transport, manufacturing and exporters who have been disproportionately affected by the current pandemic.

For further information or advice concerning Rwanda taxation, please contact Erick Njuguna at enjuguna@rw.pkfea.com or call +250 788 454 746 and +250 788 386 565.

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South Africa

National lockdown: are there tax implications if you remain in SA for an extended period of time?

The Draft Disaster Management Tax Relief Administration Bill (the “Draft Bill”) was released for public comment on 1 April 2020. It provides inter alia for purposes of specific provisions of the Tax Administration Act No. 28 of 2011 (“the TAA”), the period of national lockdown will be regarded as having no legal effect.

In certain circumstances, the physical presence of an individual in South Africa in excess of legislated periods of time could give rise to such person triggering significant South African tax liability. Neither the Draft Bill nor the Explanatory Memorandum issued in respect thereof provides clarity in relation to the impact which the period of national lockdown may have in this regard.

Potential impact on tax residence

Firstly, the national lockdown may have adverse South African tax implications for individuals who are not tax resident in South Africa, but have been under national lockdown in South Africa. This is on the basis of the so-called “physical presence” test of tax residency contained in section 1 of the Income Tax Act No. 58 of 1962. In terms of this test, a person may be resident for tax purposes in South Africa if he/she is physically present in SA:

- for more than 91 days in aggregate during a year of assessment as well as more than 91



days in aggregate during each of the five years preceding such year of assessment; and

- for a period or periods exceeding 915 days in aggregate during those five preceding years of assessment.

The above may be of particular relevance to individuals who recently ceased to be tax resident in South Africa, but now find themselves in South Africa for the period of the national lockdown.

Potential application of the expatriate exemption

Since 1 March 2020, a South African tax resident working abroad is exempt from South African income tax in respect of the first ZAR 1.25 million of foreign employment income earned in terms of the so-called “expatriate exemption”. This exemption would only apply, however, if the South African tax resident inter alia:

- spends more than 183 days in a 12-month period abroad; and
- spends a continuous period exceeding 60 full days abroad during that 12-month period.

An individual who derives foreign employment income and ordinarily spends the majority of the year offshore may, due to the national lockdown, unexpectedly spend significantly more time in South Africa and accordingly not meet the requirements of the expatriate exemption.

PKF COMMENT

Should the above provisions be unaffected by the period of national lockdown, the resulting tax implications may be unduly harsh for some taxpayers. In the current economic climate, it is important for National Treasury to provide clarity in relation to the above in favour of such taxpayers.

If you believe any of the above measures may impact your business or personal situation or require any advice with respect to South Africa taxation, please contact Alexa Muller at alexa.muller@pkf.co.za or call +27 21 914 8880.

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Switzerland

Tax developments in response to COVID-19

In line with other countries, Switzerland is introducing particular tax measures to help mitigate the economic negative impact on people and businesses caused by the Corona crisis. We summarised hereafter the initial measures regarding Swiss VAT, Swiss Income tax and Swiss social security contributions.



Swiss VAT

- i. The Swiss tax authority is currently prioritising the review of requests for early payments of VAT credits allowing for fast settlement.
- ii. Companies must file a written request (submitted by email or post) in accordance with provisions of the VAT law to benefit from tax payment deferrals. This applies to all taxpayers including foreign companies with a Swiss tax representative.

- iii. The payment periods for Swiss VAT, customs duties, special excise taxes, and incentive taxes, may be extended without having to pay interest. For this purpose, the interest rate on late payments has been reduced to 0.0% during the period from 20 March 2020 until 31 December 2020.

Income taxes (federal tax/cantonal & communal taxes)

- i. Companies that are currently unable to pay final tax invoices due to the effects of COVID-19 can apply for an extension of the payment deadline or instalment payments. Late payments of the federal tax due in the period from 1 March 2020 to 31 December 2020 will not incur any late payment interest.
- ii. Companies currently unable to pay the provisional tax invoices for Swiss federal tax purposes due to COVID-19, can apply for an extension of the payment deadline or instalment payments.
- iii. Similar tax measures have been taken by the majority of the Swiss cantons.
- iv. By booking an accrual for impending expenses in the financial statements, a Swiss company may reduce its taxable income in the relevant year. Such accruals are generally admissible and deductible for tax purposes if these accruals are not only justified by business reasons but also related to circumstances that previously existed at the end of the financial year. Due to the COVID-19 outbreak, some cantonal tax authorities stated that they consider the COVID-19 crisis as an event that “artificially” emerged before the end of 2019, which would therefore allow for booking a tax-deductible accrual in 2019. As a result, companies incurring additional expenses or loss of income in connection with the COVID-19 crisis should consider booking corresponding accruals in their 2019 financials. In addition, companies should also analyse whether the crisis justifies additional write-downs: potential items include materials, inventories, and accounts receivable.

Social security contributions

- i. Upon request, companies affected by the COVID-19 crisis can be granted a temporary deferral of payment for social security contributions (AHV / IV / EO / ALV). No late interest will be due on deferred payments.



PKF COMMENT

PKF Zurich is monitoring the impact of the COVID-19 situation on a regular basis to ensure that our clients are being proactively informed of any changes to the authorities' practices. Our dedicated professionals would be more than happy to provide you with comprehensive insights into the current situation. Do not hesitate to reach out to us should you wish to discuss and review how the tax developments in response to COVID-19 impact your Swiss tax position or discuss the necessity and/or possibility to book the accruals and write-downs in the 2019 financial statements.

For further information or advice with respect to Swiss unilateral and international taxation, please contact Rilana Wolf-Bayard at rilana.wolf@pkf.ch or Margarita Baeriswyl at margarita.baeriswyl@pkf.ch or call +41 44 285 75 00.

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Turkey

Recent international treaty developments

- On 9 July 2020, the amending protocol to the Turkey-Uzbekistan double tax treaty entered into force. The protocol was signed on 25 October 2017 and generally applies as from 1 January 2021. Among other things, amendments were made to art. 5, para. 2 (construction PE) and art. 12, para. 3 (new definition of royalties)
- Also on 9 July 2020, the investment protection agreement (IPA) between Turkey and Uzbekistan entered into force. The IPA was also signed on 25 October 2017
- Negotiations for a tax treaty between Mauritius and Turkey commenced on 25 June 2020 according to a press release of 26 June 2020 published by the Mauritius Ministry of Finance
- On 2 June 2020, the MLI (OECD Multilateral Convention) was submitted to the Turkish Grand National Assembly. Turkey submitted its MLI position at the time of signature, listing its reservations and notifications including 90 tax treaties that it wishes to be covered for by the MLI
- On 15 May 2020, the Turkish president signed decision No. 2546, thereby ratifying the Turkey-Argentina tax treaty, gazetted on 16 May 2020 (No. 31129). The treaty has not yet entered into force.

PKF COMMENT

If you believe any of the above measures may impact your business or require any advice with respect to Turkish taxation, please contact Selman Uysal at selmanuysal@pkfizmir.com or call +90 232 466 01 22.

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Ukraine

2020 Ukrainian Tax Reform – BEPS measures have been adopted

On 23 May 2020, the Law “On amendments to the Tax Code of Ukraine regarding improvement of tax administration, elimination of technical and logical inconsistencies in tax legislation” No. 466-IX, adopted by the Verkhovna Rada of Ukraine on 16 January 2020, entered into force.

The Law introduces international tax control standards for all participants in international trade and the implementation of rules envisaged by the Base Erosion and Profit Shifting Plan (BEPS Action Plan).

Also, a number of changes have been introduced aimed at improving and simplifying the tax administration system, its harmonization with global standards and expanding the possibilities of online services for taxpayers (in particular, improved functioning of the electronic taxpayer platform).

Measures in the reform include the introduction into Ukrainian legislation of:

- general anti-abuse rules (GAAR)
- a mutual agreement procedure (MAP)
- controlled foreign company (CFC) rules

- changes to the transfer pricing rules (in particular, three-tiered TP-reporting requirements)
- amendments to the definition of a permanent establishment (PE) and its registration in Ukraine
- changes to corporate income tax for non-residents (Ukraine-sourced income);
- different amendments to corporate income tax (CIT), value added tax (VAT), personal income tax (PIT), simplified tax system, excise tax and local tax regulations
- updated administrative procedure of appeal decisions of the tax bodies
- new responsibility concept (responsibility for a tax violation depending on fault, determination of circumstances that mitigate the individual's liability for tax violation)
- elimination of technical and logical mistakes in the Tax Code of Ukraine

These amendments will come into force in several stages: from 23 May 2020, from 1 July 2020 and from 1 January 2021.

It should be noted that new CFC-rules which introduce the concept of «controlled foreign companies» into Ukrainian Law and updated TP rules that improve the control over transfer pricing enter into force as from 1 January 2021.

PKF COMMENT

The 2020 Tax Reform introduces a number of positive innovations, in particular, it is envisaged that it will contribute to the de-offshorisation of the economy, which will minimise budget losses. Also positive is the ongoing development of online tax services, which is important in today's world and continues to further the global digitalisation policy in our country. However, the 2020 Tax Reform also increases the tax burden on almost on all business entities in Ukraine (especially on non-resident companies and companies that generate foreign economic activity).

If you believe any of the above measures may impact your business or personal situation or require any advice with respect to Ukraine taxation, please contact Sviatoslav Biloblovskiy at s.biloblovskiy@pkf.kiev.ua or Dmytro Khutornyy at d.khutornyy@pkf.kiev.ua or call +380 44 501 25 31.

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United Arab Emirates

Updates on economic substance regulations, CbC Reporting and VAT and excise tax

Economic Substance Regulations (ESR)

In continuation to the earlier update summarising the compliances required under UAE ESR, given below are further key updates:

- The UAE Ministry of Finance ('UAE MOF') released the Relevant Activities Guide ('Guide') with a view to provide additional guidance on the Relevant Activities and their associated Core Income Generating Activities. The Guide provides insights to understand the scope and application of the UAE ESR.
- Certain Regulatory Authorities in the UAE have published the due date for filing ESR information notifications, some of which are summarised hereafter:

Sr No	Regulatory Authority	Deadline
1	Dubai Airport Free Zone (DAFZA)	31-May-20
2	Dubai Silicon Oasis (DSO)	31-May-20
3	Fujairah FZ	15-Jun-20
4	KIZAD	20-Jun-20
5	Dubai Aviation City Corporation (DACC)	23-Jun-20
6	Dubai Development Authority (DDA)	25-Jun-20
7	Jebel Ali Free Zone Authority (JAFZA)	30-Jun-20
8	RAK International Corporate Centre (RAKICC)	30-Jun-20
9	Dubai International Financial Centre (DIFC)	30-Jun-20
10	Ajman Free Zone	30-Jun-20
11	Dubai Multi Commodities Centre (DMCC)	30-Jun-20
12	Abu Dhabi Global Market (ADGM)	30-Jun-20
13	Sharjah Airport Free Zone (SAIF)	30-Jun-20
14	Hamriyah Free Zone (HFZA)	30-Jun-20
15	RAK Economic Zone (RAKEZ)	30-Jun-20
16	Media Zone Authority	30-Jun-20
17	Ministry of Economy	30-Jun-20
18	Dubai World Trade Center	30-Jun-20
19	Umm Al Quwain FZ	30-Jun-20

- The UAE MOF recently released an Industry Advisory Notification with respect to UAE ESR recognising the fact that COVID-19 shall have an impact on UAE business and its operational procedures. Accordingly, the UAE MOF has confirmed that it will take into consideration the impact of COVID-19 on usual operations of Licensees when making a determination of whether or not a Licensee has demonstrated sufficient economic substance in the UAE..

Guide and Industry Advisory Notification along with main regulations and other guidance concerning UAE ESR can be accessed on the following link: <https://www.mof.gov.ae/en/StrategicPartnerships/Pages/ESR.aspx>

Country-by-Country Reporting

Country-By-Country Reporting ('CbCR') requirements in the UAE are applicable to financial reporting years starting on or after 1 January 2019. Accordingly, for the financial reporting year starting on 1 January 2019, businesses have filed CbCR notification by the financial year end 31 December 2019.

Further, MNEs with reporting entities located within the UAE who already filed their CbCR notifications will now be required to compile and submit the CbC reports which are required to be filed within 12 months from the end of the respective financial years.



VAT and excise tax

The UAE Federal Tax Authority ('FTA') has issued several important user guides and public clarifications since our last tax update. Some of these updates released recently by the FTA are given below:

Date	Tax	Type of Update	Particulars of Update
March 2020	VAT	User Guide – Updated Version	VAT Administrative Exceptions
April 2020	VAT	User Guide – Updated Version	Real Estate
April 2020	VAT	User Guide – Updated Version	Charities
April 2020	VAT	Public Clarification	Change in the permitted use of a building
April 2020	Excise	User Guide	Excise Tax Clearing Company - Registration & Amendments
May 2020	Excise	Public Clarification	Postponement of the Implementation of the Final Step of Phase Two of the Marking Tobacco and Tobacco Products Scheme ("the Scheme")

Some of these key updates are discussed hereunder:

VAT Public Clarification - Input Tax Apportionment: Special Methods

- The FTA has published a public clarification VATP018 on Change in the permitted use of a building and has clarified as under:
 - The sale of a building constitutes the supply of a single indivisible good at the date of supply;
 - If the purchaser subsequently changes the permitted use of the building, it does not impact the VAT treatment of the preceding sale;
- Accordingly, the clarification addresses VAT implications under situations where the intended use of the building is subsequently changed, after the date of supply.

VAT User Guide - Real Estate

The FTA has released an updated version of this user guide which provides further guidance on certain key aspects which includes:

- Additions made to supply of accommodation in labour camps to clarify that where

accommodation is not necessary for the employee to perform its role, for example accommodation in hotel apartments, input tax shall not be recoverable;

- Amendments made under VAT refund for new residences with respect to new process for submission of refund requests of such new residences.

Excise Tax - User Guide on Excise Tax Clearing Company - Registration & Amendments

- The FTA has recently released a User Guide for Clearing Companies registered with the FTA and having a TINCO account to apply for Excise Tax Clearing Company (TINCE) registration form;
- As per guidance provided therein, Registered Clearing Companies who have a TINCO account may use the Excise Tax Clearing Company (TINCE) registration form to apply for suspension of the Excise Tax due on the Excise Goods that they will import on behalf of importer;
- Procedure to register and obtain TINCE is detailed therein;
- Further, such registration application will require providing a physical bank guarantee to the FTA by the Clearing Company.



Support provided by the UAE Government as a result of COVID-19 Scenario

- The FTA in response to Covid-19 has issued a directive, on an exceptional basis:
 - With respect to Excise Tax:
 - To extend the tax period for businesses registered for Excise Tax, which commenced on 1 March 2020 for one month;
 - Accordingly, excise tax returns for tax period March 2020 and April 2020 were required to be filed on or before 17 May 2020;
 - With respect to VAT:
 - To provide an alternative date of 28 May 2020 as the deadline for submitting VAT returns and settling payable tax for the tax periods ended 31 March 2020, allowing registered businesses sufficient time to fulfil their tax obligations before the deadline;
- The UAE Government through its various regulatory and other authorities has also been introducing various relief packages to support businesses and residents living

across the country. Such efforts to support its business and residents strengthens the faith of these businesses and residents in the UAE Government and depicts strong commitment of the UAE government



PKF COMMENT

International tax perspective

Businesses in the UAE are required to undertake the exercise of impact assessments and accordingly, identify the reporting requirements under the new regulations. Accordingly, information notification filing under ESR will need to be filed within the prescribed timelines which is likely to be on or before 30 June 2020 for the Regulatory Authorities.

Businesses also need to evaluate whether they are required to undertake any filing under UAE CbCR.

VAT & Excise tax Perspective

VAT user guides and public clarifications continue to provide valuable guidance in assessing the VAT implications of various transactions and provide further clarity thereon.

Contact us

For further information or advice concerning taxes in the UAE, please contact Ms. Sarika Dhameja at sdhameja@pkfuae.com or Mr. Chaitanya Kirtikar at cgk@pkfuae.com or call +971 4 3888 900.

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United Kingdom

Stamp Duty Land Tax: Summer economic update

As widely anticipated, in a move to boost confidence in the property market and increase momentum in property transactions, on 8 July 2020 Rishi Sunak announced a temporary reduction of Stamp Duty Land Tax (SDLT) rates on residential property purchases.

The key measures are:

- Increase the 0% threshold to GBP 500,000. This means that you will not pay SDLT on the first GBP 500,000 of the purchase price of a new residential property where the standard rates apply
- Effective immediately and the temporary reduction is in place until 31 March 2021
- It is estimated that nine out of 10 people getting on or moving up the property ladder will pay no SDLT at all
- During this period the special first-time buyers' relief rules are effectively redundant as the 0% threshold is available to all individuals purchasing residential property
- The new 0% band will also apply to residential leasehold sales and new residential leases
- Where a purchaser meets the conditions for higher (or surcharged) rate for additional dwellings, the first 3% band is increased to GBP 500,000. This will also apply to company purchasers
- The residential rates of SDLT are as follows from 8 July 2020 to 31 March 2021:
 - If a residential property was purchased for GBP 750,000 on 7 July 2020, the SDLT payable would be GBP 27,500 under the previous rates. From 8 July 2020, the SDLT bill falls by more than half to GBP 12,500
 - The new rates will need to be considered for any linked transactions where there are multiple sales or purchases between the same (or connected) buyer and seller. A linked transaction occurring during a period of temporary reduction in rates may lead to lower SDLT than originally anticipated
 - This rate change only affects property purchased in England and Northern Ireland. Scotland and Wales are yet to announce any change
 - This measure is temporary and will last until 31 March 2021, when the previous SDLT rates will apply.



Property value or lease premium	Standard residential rates	Higher rates for additional properties (or company purchasers)
Up to £500,000	0%	3%
The next £425,000 (from £500,001 to £925,000)	5%	8%
The next £575,000 (from £925,001 to £1.5m)	10%	13%
Remaining consideration (over £1.5m)	12%	15%

PKF COMMENT

If you believe the above measures may impact your business or personal situation or require any advice with respect to UK taxation, please contact Heather Britton at heather.britton@pkf-francisclark.co.uk or call +44 1823 275925.

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United States

IRS guidance related to dual consolidated loss rules and establishing a foreign branch

On May 7, 2020, the IRS issued guidance to provide relief for U.S. companies with temporary activities in foreign countries due to COVID-19. Due to travel restrictions caused by the COVID-19 pandemic, employees of U.S. companies might not be able to return to the U.S. as planned and have to stay and work outside the U.S. longer than intended. Thus, these employees may conduct activities outside the U.S. that would not otherwise have been conducted in a foreign country.



If employees from U.S.-based companies work in a foreign country, and are not able to return to the U.S. due to COVID-19 related travel restrictions, there might be uncertainty as to whether these activities now give rise to:

- a foreign branch separate unit for purposes of the dual consolidated loss rules; or
- an obligation to file form 8858, Information Return of U.S. Persons with Respect to Foreign Disregarded Entities (FDEs) and Foreign Branches (FBs).

Typically, all facts and circumstances must be considered to determine whether the activities of a U.S. person outside the U.S. constitute a foreign

branch operation. Evidence of the existence of a foreign branch includes, but is not limited to, the existence of an office or other fixed place of business used by employees or officers of the U.S. person in carrying out business activities outside the United States and the existence of a separate set of books and records.

If the IRS concludes that a foreign branch exists, dual consolidated loss rules would limit the ability of a U.S. corporation to include a net loss attributable to a foreign branch separate unit. Furthermore, form 8858 would have to be completed and submitted to the IRS. This information return requires the taxpayer to provide detailed information about the FB and failure to file the form would come with USD 10,000 penalty.

However, the IRS guidance states that some temporary activities will not be taken into account for purposes of determining whether a U.S. corporation has a foreign branch.

Specifically, if one or more employees of a U.S. taxpayer are not able to leave a foreign country due to COVID-19 travel restrictions, and conduct activities during any single consecutive period of up to 60 calendar days within calendar year 2020, the days spent in the foreign country and activities performed will not be taken into account for purposes of determining whether a U.S. corporation has a foreign branch. It remains to be seen whether the IRS extends the 60-day period as travel restrictions will or already have exceeded this threshold.

This guidance complements IRS guidance issued on 21 April 2020, where the IRS made clear that, under certain circumstances, up to 60 consecutive calendar days of U.S. presence that are presumed to arise from travel disruptions caused by the COVID-19 emergency will not be counted for purposes of performing the substantial presence test to determine U.S. tax residency.

PKF COMMENT

It is important that taxpayers maintain contemporaneous documentation to establish that the activities are temporary activities and should be prepared to provide the documentation to the IRS upon request. The documentation must include evidence that the activities would not have been performed in the foreign country if the individual had been able to return to the U.S. If you believe the above measures may impact your business or require any advice with respect to US taxation, please contact Ralf Ruedenburg at rruedenburg@pkfod.com or call +1 646 965 7778.

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IRS Transfer Pricing Compliance Activities

It may be time for multinational companies operating in the U.S. to review and analyse the quality of their existing transfer pricing documentation or start creating one if they have not done so already. In several pronouncements over the last two years, including a recent FAQs, the IRS has made it very clear that it will be increasing its scrutiny of transfer pricing arrangements to determine whether they are adequate and reasonable. The IRS has also made it clear that detailed and well-reasoned transfer pricing documents can help avoid or limit audits, while thin or non-existent documentation will encourage greater scrutiny. This article provides an overview of recent developments in IRS transfer pricing guidance.

Captive Service Provider Campaign

In April 2019, the IRS announced the Captive Service Provider Campaign to increase enforcement of the U.S. transfer pricing rules. Internal Revenue Code (IRC) §482 and the related regulations, as well as the OECD Transfer Pricing Guidelines, provide rules for determining arm's length pricing for transactions between controlled entities. The scope of these rules includes transactions in which a foreign captive subsidiary performs services exclusively for its parent or other members of the multinational group. Excessive pricing for these services would inappropriately shift taxable income to these foreign entities and erode the U.S. tax base.

Thus, the goal of the Captive Service Provider Campaign is to ensure that U.S. multinational companies are paying their foreign captive service providers no more than arm's length prices. Resources have been allocated to the IRS Large Business and International Division (LB&I) to achieve the goal of this campaign.

Transfer Pricing Examination Process (Pub. 5300)

As part of the increased emphasis on transfer pricing enforcement, the IRS released an updated version of its publication on transfer pricing examinations (Pub. 5300) in May 2019. The document is a guide to best practices and processes to assist with the planning, execution, and resolution of transfer pricing examinations. Most importantly, the guide makes it clear that an Information Document Request (IDR) is mandatory if the IRS has determined that there are initial indications of transfer pricing compliance risks. This means that the IRS will be scrutinising a multinational company's transfer pricing documentation closely.

Key Documentation Elements (New IRS FAQs)

Given the increased emphasis on documentation, the IRS recently released frequently asked questions (FAQs) describing the key elements they are looking for in transfer pricing documentation. If these key elements are present, the IRS has indicated it may result in a more efficient audit and the deselection of certain audit issues, although it will not provide a safe harbour against either continued examination or imposition of penalties.

What is the IRS looking for in transfer pricing documentation?

- A full explanation of the data used in the analysis
- A “self-assessment” to anticipate questions from the IRS and proactively address those questions
- A description of business risks of the transactions and how these risks were allocated among controlled participants
- Adequate and reasonable justification for the comparable companies selected to demonstrate to the IRS that arm’s length prices were used
- The functional and risk analysis for each transaction
- A description of the challenges of the analysis, e.g., allocate losses among controlled participants
- An intercompany transaction summary at the beginning of the transfer pricing documentation.



PKF COMMENT

If multinational companies are uncertain whether their existing transfer pricing documentation is sufficient to meet the announced IRS standards, they should consult with their trusted tax advisors. Multinational companies without transfer pricing documentation to support intercompany transactions clearly should start preparing transfer pricing documentation. Although transfer pricing documentation isn’t mandatory, it can help protect companies from penalties incurred from unfavourable adjustments made by the IRS by reducing the risk of a detailed audit.

If you believe the above measures may impact your business or require any advice with respect to US taxation, please contact Ralf Ruedenburg at rruedenburg@pkfod.com or call +1 646 965 7778.

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