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Editorial

Welcome to the latest issue of Moore Stephens *European Tax Brief*. This newsletter summarises important recent tax developments of international interest taking place in Europe and in other countries within the Moore Stephens European Region. If you would like more information on any of the items featured, or would like to discuss their implications for you or your business, please contact the person named under the item(s). The material discussed in this newsletter is meant to provide general information only and should not be acted upon without first obtaining professional advice tailored to your particular needs. *European Tax Brief* is published by Moore Stephens Europe Ltd in Brussels. If you have any comments or suggestions concerning *European Tax Brief*, please contact the Editor, Zigurds Kronbergs, at the MSEL Office by e-mail at zigurds.kronbergs@moorestephens-europe.com or by telephone on +32 (0)2 627 1832.

Inside

Belgium: Dividends to Dutch FIIs not exempt from withholding tax.
Page 2

European Union: EU consults on VAT fraud.
Page 5

Germany: Retroactive change of loss-setoff rules for companies from 1 January 2016.
Page 6

Italy: New relief for incoming expatriates.
Page 8

Switzerland: Popular vote rejects corporate tax reform.
Page 9

United Kingdom: New criminal offence of facilitating tax evasion.
Page 10

»

Belgium

Dividends to Dutch FIIs not exempt from withholding tax

The Court of Justice of the European Union (CJEU) has confirmed that the Belgian tax authorities were correct in denying exemption from Belgian withholding tax on dividends paid by a Belgian REIT (real-estate investment company) to its Netherlands parent company, which took the form of a fiscal investment institution (*fiscale beleggingsinstelling – FII*).

In *Belgische Staat v Comm. VA Wereldhave Belgium and others* (Case C-448/15), the Belgian tax authorities refused to allow exemption from withholding tax under the EU Parent Subsidiary Directive on the grounds that the parent FII was effectively exempt from corporation tax in the Netherlands.

Under the Directive, exemption applies only where the recipient of the dividend is subject to a corporate income tax in its home state but also is neither exempt from that tax nor has an option to become exempt. In the Netherlands, FIIs are subject to corporate income tax but qualify for a 0% rate provided that they distribute all of their profits to their shareholders.

The Court held that the Directive contains both a subjective and an objective liability to tax. The FII was indeed in principle subject to Netherlands corporate tax but was able to put itself in a situation where it did not actually pay that tax and hence did not satisfy the second, objective arm of the test.

Although the judgment is specific to FIIs and similar tax-free investment funds, it could potentially be applied to recipient companies, such as holding companies, all or the majority of whose income consists of exempt dividends, especially since the Court laid stress in its reasoning that the purpose of the Directive was to prevent *double* taxation. Where a holding company in one Member State receives 100% of its income, say, from dividends in another Member State that does not charge withholding tax on those dividends, and the dividends when received are exempt under a participation exemption in the first Member State, it could be argued that, in the words of the Court in the *Wereldhave* case, 'the risk of double taxation on the part of that [holding] company of profits which were distributed to it by its subsidiary is ruled out'.

koen.vandorpe@moorestephens.be
an.lettens@moorestephens.be

Deduction for Innovation Revenue

A brief history

The summer of 2016 saw the end of the Belgian tax-friendly régime for income from intellectual property (IP) rights as it had been known. Thanks to this preferential régime – the so-called 'patent box' – companies were able to deduct 80% of their gross revenue from patents from their profits for the taxable period. So tax for this patent income amounted to 33.99% of 20% of the revenue, which boiled down to actual taxation of a mere 6.80%.

The OECD's BEPS plan (Action 5) required member states to review, no later than 30 June 2016, their preferential régimes for income from intellectual property obtained through research and development activities. As of 1 July 2016 the OECD member states were expected to have reformed their IP régimes so that they complied with the principles set out in the OECD recommendations.

The Belgian government eventually agreed on a new IP regime, to be known as the 'deduction for innovation revenue', which is applicable as of 1 July 2016. Income derived from patents that are applied for as of 1 July 2016 as well as amended patents and licences obtained after 1 July 2016 will consequently no longer be subject to the old patent box. Taxpayers whose income from intellectual property benefited from the old patent box before 1 July 2016, may opt for a five-year transitional scheme. The new scheme became law on 2 February 2017.

The most significant characteristics of the new deduction for innovation revenue are as follows:

1. **Qualifying beneficiaries**

The new deduction for innovation revenue applies to Belgian companies or permanent Belgian establishments of foreign companies that are the full owner, co-owner, usufructuary or licence or (exclusive) rights holder thereof.

2. **Qualifying intellectual property rights**

The new deduction for innovation revenue has a wider scope than the old patent box (which was limited to patents and supplementary rights alone, which ostensibly excluded the entire software industry from the deduction). The deduction for innovation revenue is applicable to the following intellectual property rights:

- Patents or supplementary protection certificates
- Plant variety (breeders') rights
- 'Orphan' drugs (i.e. drugs designed exclusively to treat rare diseases)
- Medicines or pesticides protected by data or market exclusivity and
- Copyright-protected software

Copyright-protected software qualifies as long as it is the result of a research & development project or programme as defined in the facility for the partial exemption of the payment from withholding tax for scientific research or as long as binding advice is received from BELSPO (Belgian Science Policy). The software must not have generated any income prior to 1 July 2016. Any changes or upgrades to software that existed prior to 1 July 2016 that result in income after 1 July 2016 are eligible, but only for that income that is due to the change or upgrade.

The new deduction can be applied to income from intellectual-property rights irrespective of the country in which the

product, service or method receives protection. This new régime is applicable (with the exception of patents that could already benefit from the patent box) insofar as the abovementioned rights were obtained or applied for after 1 July 2016.

It is important to note also that a part of the profits may already be exempted as of the time that an application for an intellectual-property right is submitted, while the patent box could only be employed for a recognised patent. In this event a temporary exemption will be awarded by means of an exempted reserve, in anticipation of the final approval of the intellectual right (subject to the repayment thereof if the intellectual property right is not awarded).

3. **Qualifying income**

The deduction for innovation revenue is applicable to income from qualifying intellectual-property rights. When compared to the previous patent box, the new version includes a much wider range when it comes to qualifying income: licensing payments, royalties included in the price of (protected) goods or services, royalties for (protected) products or methods included in the 'production process' of commercialised goods or services, income from the sale of intellectual-property rights and compensation resulting from an infringement of an intellectual-property right.

4. **Calculating the deduction for innovation revenue:**

Rate

The deduction for innovation revenue allows for 85% (compared to 80% under the patent box) of the net income (compared to the gross income under the patent box) derived from intellectual property to be deducted from the tax base of the company or permanent establishment for its corporation tax.

Deduction of net income

The deduction for innovation income is calculated using the net sum of the income from intellectual-property rights. This means that the expenses incurred by the company or permanent establishment for research & development for the year concerned are deducted from the revenue from intellectual rights. Moreover, the historical expenses

incurred for research & development in previous taxable periods (insofar as those periods end after 30 June 2016) must also be deducted. When it comes to historical costs, the law allows for them to be spread across a maximum of seven tax years, which means that taxpayers who have incurred significant costs and investment in the start-up phase can still benefit from the favourable tax environment in respect of the revenue generated by their intellectual-property rights. The choice of spreading the historical costs and the number of years over which they are depreciated are irrevocable. Should the deduction of the aforementioned research & development costs from the revenue lead to a negative balance, then this balance is carried forward to following years.

The Nexus approach

The biggest change introduced by the new tax regime for deductions for innovation revenue is that the calculation of the new deduction is linked to the so-called Nexus fraction, an amendment that legislators were compelled to introduce on the basis of the directives released by the OECD within the scope of the BEPS plan. The goal of this directive is to reserve tax-friendly régimes for companies that have sufficient economic substance at a local level.

In concrete terms this means that the calculation of the deduction will be subject to a fraction that represents the ratio between the costs for the research & development activities the company has performed itself (the numerator) and the total research & development costs (the denominator). The expenditure on research & development activities performed by the company itself also includes those costs paid to unaffiliated companies, or paid to an affiliated company if it pays the consideration on to an unaffiliated company without deducting a margin. The numerator of the Nexus ratio will be automatically increased by 30% (so-called uplift), but can never exceed the total sum of the costs incurred for research & development in the denominator. In order to compile this Nexus fraction, all expenditure for research & development in preceding taxable periods must be included and retained without restriction.

Finally, it must be noted that the Nexus approach is considered as a rebuttable presumption. If a taxpayer can demonstrate that the fraction will lead to a lower deduction for innovation revenue on the basis of actual elements, then the taxpayer can apply for a derogation from the Nexus fraction. Such a derogation will only be permissible by means of an Advance Ruling.

5. Administrative obligations

The new deduction for innovation revenue entails administrative compliance and a documentation obligation that must not be underestimated by taxpayers who wish to employ the régime. Innovation revenue as well as the expenditure directly related thereto (for determining the Nexus fraction) must be determined separately for each intellectual-property right. Exceptionally, the obligation in respect of documentation may be kept updated for each type of product or service developed. In order to comply with these administrative obligations a specific form is to be added to the corporation tax return, both for SMEs and for larger companies.

6. Making the deduction for innovation revenue

The deduction for innovation revenue in the corporation tax return is to be made after the the definitively taxed income deduction is made and prior to the making of the notional-interest deduction.

The unused balance of the deduction for innovation revenue may (as opposed to the patent box régime) be wholly carried forward to following tax years.

Neither will the deduction be henceforth lost in the event of a company restructuring (merger, demerger, etc.) on the part of the taxpayer concerned.

In conclusion, we also note that the application of the deduction for innovation revenue does not threaten the application of the investment deduction with respect to the same intellectual property right.

7. Choosing between the old and new regimes for revenue from intellectual property rights

Some taxpayers will be able to opt for the transitional scheme of the former patent box or for the new deduction for innovation revenue for certain

intellectual-property rights. Depending on the specific characteristics of each case and, more specifically, the structure of certain corporate groups, it could in some cases be more advantageous to opt for the former patent box. When a taxpayer settles on the transitional scheme of the old patent box, this is an irrevocable choice and the taxpayer will be unable to switch to the deduction for innovation revenue before 30 June 2021.

Finally, it is handy to know that some taxpayers will have to apply both the 'old' patent box and the 'new' deduction for innovation revenue in the same tax return, which is possible as long as this is not done for the same property rights.

an.lettens@moorestephens.be
annesophie.vandenbosch@moorestephens.be

European Union

EU consults on VAT fraud

The European Commission has launched a consultation exercise on how best to tackle VAT fraud. It estimates the 'VAT gap' (the difference between the VAT that should have been collected and the VAT that was actually collected) in the European Union in 2014 at EUR 159 500 million or 14% overall. The VAT gap in Romania is thought to be as high as 37.9%.

VAT fraud was one of the topics discussed at the recent Moore Stephens European Tax Meeting in Barcelona in February.

t.vanden.berg@mth.nl

EU agrees further anti-avoidance directive on hybrid mismatches

The European Council of Economic and Finance Ministers (ECOFIN) agreed a compromise package on the draft Directive to close down tax advantages arising from hybrid mismatches with the tax systems of third countries at its meeting on 21 February.

Compromise amendments to the original Commission draft concern a temporary carve-out for the banking sector, a delimited approach for financial traders, and a delayed implementation period.

If the directive (popularly referred to as 'ATAD II') is approved by the European Parliament, it must then be adopted unanimously by the 28 heads of government. Member States would have until 31 December 2019 to transpose it into their domestic law.

zigurds.kronbergs@moorestephens-europe.com

Financial Transfer Tax encounters further delays

At an inconclusive meeting in February of the 10 EU Member States committed to the introduction of a common financial transactions tax, there was a growing demand for an exemption for pension funds. It was agreed that technical analysis of the effects of both a mandatory and an optional exemption would be carried out before the next meeting, which will take place shortly.

The 10 Member States concerned are Austria, Belgium, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and Spain.

zigurds.kronbergs@moorestephens-europe.com

New work and new chair for EU Code of Conduct group

The EU's Business Code of Conduct working group has a new Chair and an expanded work programme.

Dr Fabrizia Lapecorella, from the Italian Ministry of Economy and Finance, has been appointed to chair the group. She takes over from her Austrian predecessor Dr Wolfgang Nolz, who has chaired the group since 2009.

The group's main task is to assess tax measures in the Member States that potentially encourage harmful tax competition. Its expanded brief now extends to anti-abuse measures, transparency in the area of transfer pricing, administrative practices and links to third countries.

Its main immediate task is to establish the EU's list of non-cooperative jurisdictions, as reported in previous issues of *European Tax Brief*. It began this process on 1 February, by writing to 92 third-country jurisdictions, requesting information.

zigurds.kronbergs@moorestephens-europe.com

Dividends to Dutch FIIs not exempt from Belgian withholding tax

See under Belgium.

Germany

Retroactive change of loss-setoff rules for companies from 1 January 2016

Where there is an acquisition of a significant shareholding or participation in a German company, the question may arise as to how to make sure that an existing tax-loss carry-forward may be retained for future set-off. In order to avoid abuse, e.g. trading in inactive shelf companies with tax-loss carry-forwards, section 8c of the German Corporation Tax Act (*Körperschaftsteuergesetz* – KStG) provides that an existing tax-loss carry-forward ceases to be available in part to a German company where within a five-year period more than 25% of the participation in its capital and/or its voting rights is directly or indirectly transferred. Where there is a direct or indirect transfer of capital or voting rights amounting to more than 50%, a set-off for tax purposes is fully denied. Exceptions to this rule apply to certain transfers within a group of companies but only where it can be established that at the time the transfer took place, the corporation had hidden reserves which were subject to German tax and which were equal to or greater than the tax-loss carry-forward. Proof of hidden reserves is typically provided via a valuation opinion prepared by a German chartered accountant.

On 23 December 2016, these rules were complemented via the enactment of the Company Loss Set-Off (Refinement) Act (*Gezetz zur Weiterentwicklung der steurlichen Verlustverrechnung bei Körperschaften*). This is intended to

improve investment in, and the provision of equity to, German companies, in particular young enterprises with innovative business ideas ('start-ups'). Under the provisions of the new section 8d KStG, which is retroactively applicable from 1 January 2016, a tax-loss carry-forward will not in future be forfeited in the case of changes to the shareholder structure that are either due to share transfers or an entry of new shareholders via a capital increase, provided that the company applies for such treatment and satisfies the necessary condition. The condition is that the company has completely maintained its business

operations since its formation or at least since the beginning of the third financial year prior to the one in which the share transfer in question takes place. The application has to be made in the tax return for the financial year in which the share transfer takes place. The amount of the tax-loss carry-forward as at the end of this financial year will be determined by the German tax authorities in a separate tax assessment note. This so-called 'Going-concern-related tax-loss carry forward' will nevertheless be forfeited where:

- The company ceases, temporarily suspends or redirects its existing business operations
- Takes up additional business operations of a different nature
- Participates in a partnership which generates, or under German law is deemed to generate, business income
- Becomes the controlling entity within a German tax group (*Organschaft*) or
- Where assets are transferred to the company at a tax value below fair market value.

The new rules provide significant tax-planning opportunities. However, given their complexity, transactions should be carefully planned.

frank.behrenz@sp-wp.de

New draft transfer pricing rules published

The Federal Ministry of Finance recently published draft amendments to the rules governing transfer-pricing documentation, in the light of BEPS Action 13, which has been incorporated into the latest version of the OECD's *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.*

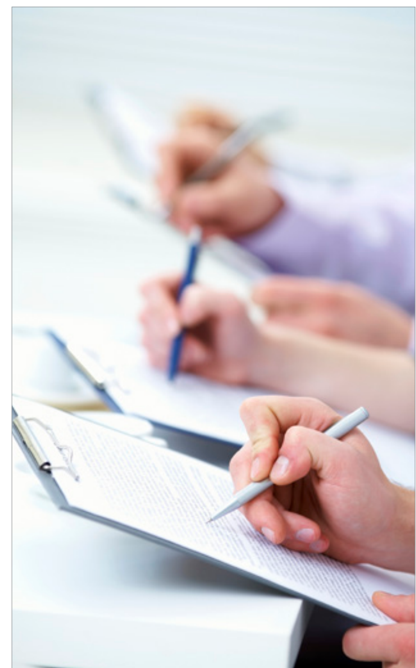
BEPS Action 13, it will be recalled, called on countries to re-examine their requirements relating to the documentation companies are required to produce concerning their transfer-pricing policies, increase the amount of information required, as well as to introduce country-by-country (CbC) reporting for the largest multinational groups.

However, the proposed new German rules are considered to go beyond what the OECD strictly requires. Among the additional requirements Germany would require are:

- Naming of the person who made the decisions in respect of each intra-group transaction in question
- Access by tax auditors to all the databases the taxpayers and/or their advisers used for benchmarking analysis, including to the version in existence at the time the database was consulted

In addition, taxpayers wishing to prepare the documentation in languages other than German would be required to undergo a separate application process.

sven.helm@mstk.de



Isle of Man

Isle of Man introduces CBC reporting

The Isle of Man has become the latest jurisdiction to introduce compulsory country-by-country (CBC) reporting for multinational groups whose annual turnover exceeds EUR 750 million. Mandatory reporting will begin with respect to financial years beginning after 31 December 2016.

clive.dixon@msiom.com

Italy

New relief for incoming expatriates

A new favourable régime for individuals becoming resident in Italy has been introduced with effect from the 2017 tax year.

Provided that they have not been resident in Italy for at least nine out of the previous 10 years, individuals who transfer their tax residence to Italy may opt to pay an annual lump-sum substitute tax in return for exemption from income tax for all foreign-source income and capital gains (except for gains in the first five years of residence arising from the disposal of significant participations) and exemption from wealth and inheritance taxes.

The lump sum payable annually is EUR 100 000, plus EUR 25 000 for each family member wishing to benefit from the same régime, so is likely to benefit largely high-income and high net-wealth individuals. The régime lapses after 15 years but individuals may withdraw from it at any time. Individuals wishing to benefit must file an application with the tax authorities.

paolo.borghi@studiopdb.com

Netherlands

Dividends to Dutch FIIs not exempt from Belgian withholding tax

See under Belgium.

Serbia

Changes to VAT law largely aligned to EU rules

A number of important changes have been made to Serbian VAT rules with effect from 1 January 2017. The most important of these concern the place-of-supply rules (effective from 1 April 2017) and the liability of foreign taxable persons to register for VAT in Serbia.

As in the European Union, the general rule for supplies of services is now that for B2B services (services supplied to a taxable person), the supply takes place where the customer (the recipient of the service) is established, whereas B2C supplies (services supplied to non-taxable persons, such as private consumers) are generally regarded as taking place where the supplier is established.

There are a number of exceptions to the general rule, which will also be familiar to those conversant with EU rules. Thus:

- Supplies relating to immovable property are supplied where the property is situated
- Services relating to cultural, sporting and entertainment events are supplied where the event takes place
- Telecommunications services, electronic services and certain other services are supplied where the customer is located, whether or not the customer is a taxable person

Foreign suppliers are obliged to register for VAT in Serbia, and appoint a tax representative, only if their Serbian customer is a non-taxable person, and there is no registration threshold (i.e. registration is obligatory whatever the supplier's annual turnover).

Failure to register may incur a penalty of up to RSD 2 million.

beljkas@revizija.co.rs

Switzerland

Popular vote rejects corporate tax reform

By 60% to 40%, Swiss voters rejected the comprehensive tax reform package (Corporate Tax Reform III) in a referendum held on Sunday 12 February.

The reform package, strongly supported by the business community, involved removal of various special tax régimes for foreign companies in return for the introduction of reliefs such as the notional-interest deduction and the patent box.

The reform would also have resulted in a general lowing of cantonal corporate tax rates (in order to compensate multinationals for the loss of the special régimes). The resulting loss in revenue would have been partially compensated by federal funding.

Following the negative vote, the Swiss government instructed the Swiss Ministry of Finance to draw up a new tax-reform proposal to replace the package rejected by voters.

'Substantive parameters' of the new proposal are to be completed by the middle of this year. They must, like the previous proposal, find a balance between Switzerland's international commitments to abolish the special tax arrangements on the one hand while safeguarding tax revenues for the federal government and the cantons and communes and maintaining Switzerland's competitiveness on the other.

Any new package that eventually emerges will need to be put to a referendum also.

The Government and Parliament now have a year in which to agree an alternative plan.

hstaudt@ms-zurich.com

United Kingdom

Enabler penalty confirmed

The UK government has confirmed that the new penalty for those who 'enable' abusive tax-avoidance arrangements that are subsequently defeated will apply from the date on which the Finance Bill 2017 (published on 20 March) is passed into law (expected to be in July 2017).

'Enablers' are anyone who designs, manages, markets or otherwise facilitates the arrangements.

The penalty is to be set at 100% of the fee received for the arrangement. The government has indicated that professional advisers acting wholly within the spirit of the code of practice (Professional Conduct in Relation to Taxation') published in February 2017 would not normally be affected by the penalty.

dominic.arnold@moorestephens.com

UK corporation tax set to decrease from 1 April 2017

The rate of corporation tax has been reduced from 20% to 19% from 1 April, as previously legislated. No further changes were announced in the Budget delivered on 8 March.

With effect from 1 April 2020, the rate is set to fall further to 17%.

timothy.fussell@moorestephens.com

Scottish income tax rates & bands frozen

The Scottish Government has confirmed that for the tax year 2017-18 (beginning 6 April 2017), all rates and bands of income tax are to remain exactly as they were in 2016-17.

The practical consequence of this is that in 2017-18, Scottish taxpayers will begin to pay the 40% higher rate of income tax on that part of their non-savings, non-dividend taxable income (i.e. primarily income from employment, self-employment, partnerships and land and property) exceeding GBP 31 500 (i.e. after deducting the personal allowance), whereas taxpayers in the rest of the United Kingdom will do so only on income exceeding GBP 33 500. Savings and dividend income received by Scottish taxpayers will continue to be tested against the main UK threshold of GBP 33 500.

The Scottish Parliament has the right to set income tax rates, bands and allowances for Scottish taxpayers independently as from the tax year 2017-18.

morag.watson@moorestephens.com

New criminal offence of facilitating tax evasion

The Criminal Finances Bill, due to complete its progress through Parliament at the beginning of May, will introduce a new criminal offence of corporate failure to prevent tax evasion, of both UK and foreign tax.

The new legislation will render a body corporate (such as a company) or a partnership ('the relevant body') open to prosecution for failure to prevent the facilitation of tax evasion where:

- An 'associate' of that body facilitates the evasion of tax by another person and
- The relevant body is unable to show it had 'reasonable prevention procedures' in place to prevent that facilitation (or that it would have been unreasonable to expect any prevention procedures to be in place)

An 'associate' may be an employee or any person who performs services for or on behalf of the relevant body. However, bodies will not be held liable for acts committed by their associates acting in a private capacity.

Offences can either be 'domestic' (relating to evasion of UK tax) or 'foreign' (relation to criminal evasion of tax levied by a foreign jurisdiction). For the domestic offence, it will not matter where the relevant body is established or does business or where the facilitation actually took place, as long as the tax evaded is UK tax. For the foreign offence, however, either (a) the relevant body must be established in the United Kingdom or carry on any part of its business there or (b) some part of the facilitation must have taken place in the United Kingdom.

Final guidance about what measures to prevent facilitation are to be regarded as reasonable will be published in due course. Draft guidance published in October 2016 stated that measures to prevent facilitation should be guided by the principles of risk assessment, proportionality, top-level commitment, due diligence, communication, and monitoring and review.

dominic.arnold@moorestephens.com

Currency table

For ease of comparison, we reproduce below exchange rates against the euro and the US dollar of the various currencies mentioned in this newsletter. The rates are quoted as at 3 April 2017, and are for illustrative purposes only.

Currency	Equivalent in euros (EUR)	Equivalent in US dollars (USD)
Euro (EUR)	1.0000	1.0661
Pound sterling (GBP)	1.1672	1.2442
Serbian dinar (RSD)	0.0081	0.0086

Up-to-the-minute exchange rates can be obtained from a variety of free internet sources (e.g. http://www.oanda.com/currency/converter).

For more information please visit:
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