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International Tax

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This article presents developments in international tax during 2013.[1]

I. Introduction

Governments and tax administrations have focused on protecting and increasing their national revenue base to offset increasing budget deficits. At the same time, governments and media have increasingly scrutinized the tax paid by major multinationals. Through tax planning and structuring their business operations across borders, major multinationals have reduced their global effective tax rates dramatically, to the detriment of national revenue bases, or so it is perceived. To reduce tax avoidance by multinationals, government ministers have advocated for greater information exchange and increased collaboration between jurisdictions at recent meetings of the G20.

The Organization for Economic Co-operation and Development (OECD) has been working in tandem with the G20. On February 12, 2013, the OECD published its Report Addressing Base Erosion and Profit Shifting (BEPS).[2] On July 19, 2013, the OECD published its Action Plan on BEPS (Action Plan).[3] The Action Plan identifies key pressure areas where international tax planning and structuring results in double non-taxation and (very) low taxation of income. In September of this year, the OECD Secretary-General, Angel Gurria, presented a comprehensive report to the meeting of the G20 leaders in

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1. For developments during 2012, see Luiz Felipe Centero Ferraz et al., *International Tax*, 47 INT'L LAW 355 (2013).
2. OECD, ADDRESSING BASE EROSION AND PROFIT SHIFTING (OECD Publishing 2013), *available at* http://dx.doi.org/10.1787/9789264192744-en.
3. OECD, ACTION PLAN ON BASE EROSION AND PROFIT SHIFTING (OECD Publishing 2013), *available at* http://dx.doi.org/10.1787/9789264202719-en.

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St. Petersburg, Russia.[4] The OECD worked all year to encourage jurisdictions to sign its Multilateral Convention on Mutual Administrative Assistance in Tax Matters.[5] The Action Plan sets ambitious goals and timelines.[6] The OECD's target date for the first output on its BEPS agenda is September 2014.

The European Union (EU) has announced measures to tackle tax evasion and tax avoidance. Those measures are reviewed in the next section. Nation-States have also introduced, or are taking steps to introduce, domestic measures to increase their tax revenues. The following countries and their measures are reviewed in this article: the Netherlands, Australia, South Korea, Argentina, and Peru.

II. EU Action Plan

On December 6, 2012, the European Commission presented an action plan[7] for a more effective EU response to tax evasion and tax avoidance. The plan's goal is to assist EU member States (Member States) to protect their tax bases. The EU action plan contains measures recommended to the Member States for implementation. Many of the measures are largely compliance-related and are designed to enhance administrative procedures and cooperation between EU tax administrations. Two of the recommendations, however, may have a greater impact. First, the plan recommends that the Member States introduce a "subject-to-tax" requirement in double-tax treaties and in unilateral double-tax relief rules. Second, Member States are advised to include a general anti-abuse rule (GAAR) in their domestic legislation.

On November 25, 2013, the European Commission proposed two amendments to the EU Parent-Subsidiary Directive[8] (Directive) to close loopholes (EC Proposal).[9] The Directive currently provides a withholding tax exemption and corporation tax exemption (or credit) for certain profit distributions from subsidiaries to parent companies, where both are based in Member States. The EC Proposal provides that (i) the Directive's tax exemptions shall be withdrawn for certain artificial arrangements by introducing a GAAR provision, and (ii) for hybrid loan instruments, the Member State of the parent company shall tax the parent company's profits to the extent that such profits are deductible by the sub-

4. OECD, OECD General-Secretary Report to the G20 Leaders (OECD Publishing 2013), *available at* http://www.oecd.org/ctp/SG-report-G20-Leaders-StPetersburg.pdf.

5. The Convention was developed jointly by the OECD and the Council of Europe in 1988 and amended by Protocol in 2010. The Convention is the most comprehensive multilateral instrument available for all forms of tax cooperation to tackle tax evasion and avoidance. Since 2009, the G20 has consistently encouraged countries to sign the Convention. The OECD again encouraged countries at the meeting of the G20 Leaders Summit in September 2013. Currently, over sixty countries have signed the Convention, and it has been extended to over ten jurisdictions.

6. The OECD is studying a number of action items and will be producing reports and suggesting ways in which jurisdictions may choose to address the issues it has raised. Its suggestions do not have the force of law. Implementation will depend on domestic law and bilateral double tax treaty changes.

7. *An Action Plan to Strengthen the Fight Against Tax Fraud and Tax Evasion*, COM(2012) 722 final (June 12, 2012), *available at* http://ec.europa.eu/taxation_customs/resources/documents/taxation/tax_fraud_evasion/com_2012_722_en.pdf.

8. Council Directive 2011/96/EU, 2011O.J. (EC).

9. *Amending Directive 2011/96/EU on the Common System of Taxation Applicable in the Case of Parent Companies and Subsidiaries of Different Member States*, COM(2013) 814 final (Dec. 11, 2013), *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2013:0814:FIN:EN:PDF.

sidiary. The European Council must first unanimously approve the EC Proposal for it to become effective. Member States are expected to implement it by December 31, 2014.

III. Domestic Action in Various Jurisdictions

A. The Netherlands

1. *BEPS Commitment*

The Netherlands views the BEPS agenda as a multilateral issue that must be resolved at an international level through changes to "hard law." The Netherlands believes BEPS measures should be implemented at an EU or global level. The Netherlands has committed itself to cooperating with implementation at this level.[10] In response to domestic political pressure, the Netherlands plans to codify its existing substance requirements to assist source countries in assessing whether certain Dutch-based entities are entitled to treaty benefits.

2. *Measures to Protect the Dutch Tax Base*

In 2012 and 2013, the Netherlands initiated two domestic measures to protect the Dutch tax base against erosion through excessive interest deductions by Dutch-based entities.

Effective January 1, 2012, new legislation addresses highly leveraged acquisitions of Dutch companies by private equity funds that result in excessive debt push-downs to Dutch targets. The legislation[11] restricts interest deductions through tax grouping or (de)merger on debt (from both affiliated and third-parties), where the proceeds are used to acquire or to increase an investment in a (Dutch) target. In principle, the deduction is limited to the profits of the tax group of the acquiring company, excluding the target's profits. Two thresholds apply. Disallowed interest is the lower of (i) interest expense in excess of EUR 1,000,000 per annum and (ii) interest expense on debt that exceeds 60 percent of the targets' acquisition price at the end of the year in which the targets are included in the tax group.[12] The applicable percentage is reduced by 5 percentage points each year, ultimately to 25 percent. Grandfathering applies to certain leveraged acquisitions resulting in inclusion of the Dutch target in a tax group before November 15, 2011.[13]

Effective January 1, 2013, a further restriction exists to address an imbalance occurring where interest on debt was deductible by Dutch companies for exempt equity investments in Dutch or foreign participations while income and capital gains derived from the partici-

10. EY, The Outlook for Global Tax Policy in 2014 163 (2014), *available at* http://www.ey.com/Publication/vwLUAssets/EY-the-outlook-for-global-tax-policy-in-2014/$FILE/EY-the-outlook-for-global-tax-policy-in-2014.pdf.
11. Law of December 22, 2011 Amending Some Tax Laws and Any Other Laws (Tax Plan 2012), 639 Stb. 2011, p. 1.
12. *Id.* at 27.
13. *Id.* at 59.

pations were exempt under the Dutch participation exemption.[14] This "loophole" was created in 2003 as a result of the ECJ *Bosal* judgment.[15] The 2013 amendment restricts interest deductions on debt (from affiliated and third parties) deemed to be incurred for acquisitions of and investments in subsidiaries qualifying for the Dutch participation exemption, where the acquisitions or investments are not linked to an expansion of operational activities of the group. The disallowed interest amount is calculated by dividing (i) the historic cost of qualifying participations minus the taxpayer's equity by (ii) the taxpayer's total debt amount. The taxpayer's equity is per se deemed to have been invested in qualifying investments. This mitigates the rule's impact. Further, certain internal reorganizations or investments in participations made in years commencing on or before January 1, 2006, are grandfathered in under the amendment.[16] The 2013 amendment abolished the existing thin capitalization rules based on the taxpayer's overall debt-to-equity ratio.

3. *Measures to Assist Other Countries in Protecting Their Tax Base*

Pursuant to internal Dutch political discussions on the role of the Netherlands in international tax planning, the Dutch Ministry of Finance has acknowledged that the Netherlands has a responsibility to prevent abuse of tax treaties. This does not change the Netherlands' overall stance that steps to counter tax evasion and tax avoidance should be taken globally and jointly through the OECD and EU. On August 30, 2013, the Netherlands announced measures to assist source countries in assessing whether certain entities with insufficient links to the Netherlands should receive treaty benefits.

Two categories of measures have been announced:

i. a proposal made to twenty-three developing countries with whom the Netherlands has concluded or is planning to conclude double tax treaties to include anti-abuse provisions in these treaties; and
ii. stronger enforcement of existing minimum substance requirements and exchange of information in case of non-compliance.[17]

The current minimum substance requirements were issued in 2004 and apply to Dutch-based intra-group financing/licensing companies seeking a Dutch tax ruling. These requirements provide, inter alia, that at least half of the board of a Dutch-based company must be resident in the Netherlands, management decisions must be taken in the Netherlands, and the bookkeeping function must be performed in the Netherlands.[18]

As of January 1, 2014, the minimum substance requirements will apply to all Dutch-based intra-group financing/licensing companies[19] whether they seek Dutch tax rulings or

14. LOYENS & LOEFF, YEAR END TAX BULLETIN 2012 (Dec. 2012), *available at* http://www.loyensloeff.com/nl-NL/Documents/Nieuws/Publicaties/Nieuwsbrieven/YETB_2012.pdf.

15. Case C-168/01, Bosal Holding BV v. Staatssecretaris van Financien, 2003 E.C.R. I-9446.

16. LOYENS & LOEFF, *supra* note 14, at 2.

17. Letter from Frans Weekers, State Sec. of Finance, to the Lower House Standing Committee on Finance (Aug. 30, 2013), *available at* http://www.government.nl/files/documents-and-publications/parliamentary-documents/2013/09/09/government-s-response-to-the-report-from-seo-economics-amsterdam-on-other-financial-institutions-and-the-ibfd-report-on-developing-countries/ifz-2013-320-brief-tweede-kamer-reactie-seo-en-ibfd-rapport-eng-def.pdf.

18. Decree of the Dutch Ministry of Finance dated 11 August 2004, no. IFZ2004/126M. Stb. 2004, p.1.

19. It has now been stated explicitly that this includes leasing companies.

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not.[20] The legislature intends that these new substance requirements be interpreted in the same manner as current minimum substance requirements even though the new ones are only similar, but not identical, to the current requirements. The new requirements also apply to holding companies with intra-group financing/licensing activities even if the activities are only minor. The financing/licensing company must state in its annual Dutch corporation tax return whether it meets the substance requirements. If it does not meet them, it must state which requirements are not met. Where a Dutch-based company fails to comply, the Dutch tax administration will, *sua sponte*, exchange information with the relevant treaty partner who can take this into account in assessing treaty entitlement.

Finally, as of January 1, 2014, (i) the minimum substance requirements will also apply to holding companies that seek a Dutch tax ruling, and (ii) the Netherlands intends to exchange information on any Advance Pricing Agreement (APA) involving financing/licensing companies, where the related corporate group does not have any other activities in the Netherlands, even where the minimum substance requirements are met.[21] This was announced on August 30, 2013.[22]

B. Australia

1. *Overview*

Protection of the tax base has been a chief focus of tax reform proposals in Australia in 2013. The BEPS Report and the Action Plan pushed this to the forefront. The government enacted amendments to transfer pricing (TP) and to the Australian anti-avoidance rule. Other proposals on BEPS were announced prior to federal elections in September 2013 but have not yet been enacted. The new government has included these proposals in a wider review it is making of changes proposed by its predecessor.[23] The new government has indicated it largely supports the announced proposals on BEPS.[24] No deadline has been set for enacting these proposals.[25] It seems unlikely that any new tax legislation will be passed before July 2014.

The previous government's BEPS policy was outlined in four key announcements:

i. an issues paper released in May 2013 identifying challenges posed by BEPS and the relevance of international events;[26]
ii. a scoping paper released in July 2013 outlining potential risks BEPS posed to Australia's tax system;[27]

20. Draft Decree DCM/MA-216/2013 (Oct. 18, 2013).
21. Letter from Frans Weekers, *supra* note 17, at 4.
22. *Id.* at 1.
23. Press Release, Liberal Party of Australia, Restoring Integrity in the Australian Tax System (November 6, 2013) [hereinafter November 2013 Release].
24. *Id.*
25. *Id.*
26. The Australian Government the Treasury, *Implications of the Modern Global Economy for the Taxation of Multinational Enterprises*, (Issues Paper May 2013) *available at* http://www.treasury.gov.au/~/media/Treasury/Consultations%20and%20Reviews/2013/Taxation%20of%20Multinational%20Enterprises/Key%20Documents/PDF/IssuesPaper.ashx.
27. The Australian Government the Treasury, *Risks to the Sustainability of Australia's Corporate Tax Base*, (Scoping Paper July 2013) *available at* http://www.treasury.gov.au/~/media/Treasury/Publications%20and

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iii. a proposals paper dated May 14, 2013, focusing on thin capitalization and reforms to foreign non-portfolio dividends[28] (Proposals Paper); and
iv. a press release of May 14, 2013, explaining the importance of the Proposals Paper and relating it to additional measures including changes to capital gains tax (CGT) affecting foreign residents, the offshore banking units regime and measures on dividend washing.

2. *2013 Amendments*

a. Transfer Pricing Rules

The government passed amendments to Australia's domestic TP rules on June 30, 2013.[29] For tax purposes, these require both associated and non-associated entities to comply with arm's length principles, regardless of whether a double-tax treaty would otherwise apply.[30] The substantiation requirements were also changed.[31]

b. Anti-Avoidance Reform

The government passed amendments to Australia's GAAR regime in June 2013[32] to apply retrospectively as of November 16, 2012.[33] The GAAR applies if:
i. a taxpayer enters into a 'scheme' (a scheme includes any form of agreement, understanding or arrangement;
ii. as a result of the scheme any person obtains a 'tax benefit.' A tax benefit means either a deduction allowed from assessable income that would or might reasonably be expected not to have been allowed but for the scheme or income being excluded from assessable income that would or might reasonably be expected to have been included in assessable income but for the scheme. The tax effect that would or might reasonably have been expected is tested by reference to an alternative course of action the taxpayer would or might reasonably have been expected to have undertaken; and
iii. whether the sole or dominant purpose of any party entering into a scheme is to obtain a tax benefit. The amendments set forth eight specific factors to weigh in determining the purpose.

The key change goes to the threshold question when considering whether a tax benefit arises in connection with a scheme. The court may not weigh the tax consequences of an

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%20Media/Publications/2013/Aus%20Corporate%20Tax%20Base%20Sustainability/Downloads/PDF/BEPSscoping_paper.ashx.

28. The Australian Government Treasury, *Addressing Profit Shifting Through the Artificial Loading of Debt in Australia*, (Proposals Paper May 24, 2013) *available at* http://www.treasury.gov.au/~/media/Treasury/Consultations%20and%20Reviews/2013/Profit%20shifting/Key%20Documents/PDF/Proposals_Paper_Profit_shifting.ashx.

29. Tax Laws Amendment (Countering Tax Avoidance and Multinational Profit Shifting) Bill 2013 (Cth) (Austl.) [hereinafter Tax Laws Amendment].

30. Explanatory Memorandum, Tax Laws Amendment (Countering Tax Avoidance and Multinational Profit Shifting) Bill 2013 (Cth) p. 33 (Austl.) [hereinafter Explanatory Memorandum].

31. *Id.* at 36.

32. Tax Laws Amendment, *supra* note 29, at 1.

33. *Id.* at 4; Explanatory Memorandum, *supra* note 30, at 13–14.

alternative to the scheme when determining whether the alternative is reasonable.[34] That is, a particular alternative cannot be disregarded merely because a taxpayer would never have entered into the alternative transaction at all because of the tax cost of that alternative.[35] This change resulted from recent Federal Court cases decided under the previous law where the government lost.[36] The stated object of the amendments is to require that an examination of the objective purpose for entering into a scheme be the primary inquiry.[37]

c. Policy Announcements Not Yet Enacted

i. Thin Capitalization Regime

Treasury has engaged in consultation on proposed amendments to the thin capitalization rules that will impact the regime's scope. The new government plans to implement the amendments included in the Proposals Paper.[38] They include:

i. reducing the safe harbor debt limit for general (non-bank/non-financial) entities from a 3:1 to a 1.5:1 debt-to-equity ratio;
ii. reducing the safe harbor debt limit for non-bank financial entities (such as securities dealers) from a 20:1 to a 15:1 debt-to-equity ratio;
iii. increasing the safe harbor capital limit for banks from 4 percent to 6 percent; and
iv. reducing a worldwide gearing ratio for outbound investors from 120 percent to 100 percent.

Currently, only outbound investors can apply the worldwide gearing ratio. There is a proposal to make the test available to inbound investors[39] and to increase the scheme's de minimis threshold to AUS $2 million in deductions.

ii. Foreign Non-Portfolio Dividends

In May 2013, a proposal to amend the existing tax exclusion for foreign non-portfolio dividends was announced. A foreign non-portfolio dividend is a dividend received from a shareholding that represents a voting power of 10 percent or greater.[40] Currently, a foreign non-portfolio dividend received by an Australian resident shareholder is not assessable income and not exempt income in Australia.[41]

The previous government explained in the Proposals Paper that the policy underlying this tax exclusion was intended only to apply to non-portfolio dividends received on equity holdings of 10 percent or greater. Treasury expressed concerns that the current wording of the provision has allowed its application to dividends from holdings that are, in substance, debt interests or portfolio interests. It was also suggested that the provision interacts unfavorably with section 25-90 of the Income Tax Assessment Act 1997 (Cth), which

34. Tax Laws Amendment, *supra* note 29, at 4; Explanatory Memorandum, *supra* note 30, at 13–14.
35. *See Commissioner of Taxation v Futuris Corporation Limited* [2012] FCAFC 32; *see also RCI Pty Limited v Commissioner of Taxation* [2011] FCAFC 104.
36. Explanatory Memorandum, *supra* note 30, at 14–15.
37. November 2013 Release, *supra* note 23, at 7.
38. *Id.* at 8. Treasury has verbally advised that the threshold to apply to inbound investors will also be 100 percent.
39. *Id.* at 7.
40. Income Tax Assessment Act 1936 (Cth) s 317.
41. *Id.* s 23AJ.

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provides a deduction for costs associated with an entity's debt interests (section 25-90). For example, if an Australian taxpayer finances the purchase of redeemable preferred shares by borrowing, the taxpayer may claim a deduction for the interest due while dividends received on the redeemable preference shares would not be assessable income.[42] But the new government has indicated it will not repeal section 25-90.[43] Instead, it will seek to improve the integrity of section 25-90 through targeted anti-avoidance measures.[44]

iii. Offshore Banking Unit (OBU) Regime

The previous government proposed to review the list of eligible OBU activities and to make the following types of dealings ineligible for OBU treatment:

i. dealings between related parties (including those that convert non-OBU income to OBU income); and
ii. dealings between OBUs, including between unrelated OBUs.[45]

The new government has indicated that it will amend these proposals and release details after further consultation.[46] It has abandoned the initial start date of October 1, 2013.[47]

iv. Foreign Resident CGT

Amendments passed in June 2013 deny the 50 percent capital gains discount to the extent a capital gain is accrued by a taxpayer while he is a foreign or temporary resident.[48] The new government has committed to implementing the proposed changes to foreign resident CGT.[49] Foreign residents are only taxed on the capital gains they make on direct or indirect interests in taxable Australian real property (TARP) or an asset used at any time in an Australian permanent establishment.[50] A 10 percent non-final withholding tax[51] will be imposed on the sale of certain TARP by non-residents (except for residential property worth less than AUS $2.5 million) effective as of July 1, 2016.[52]

There are also plans to amend the principal asset test used to determine whether an indirect property interest is TARP for CGT purposes. TARP will be redefined so that intangible assets, including "mining, quarrying or prospecting information, rights to such information and goodwill," will be valued together with the mining rights to which they

42. *Id.*
43. November 2013 Release, *supra* note 23.
44. *Id.*
45. Media Release, David Bradbury, Assistant Treasurer, Protecting the Corporate Tax Base from Erosion and Loopholes–Measures and Consultation Arrangements, Attachment C (No. 071, May 14, 2013) [hereinafter May 2013 Release].
46. *Id.*
47. Media Release, Offshore Banking Unit: Deferral of Start Date (Sept. 29, 2013).
48. Income Tax Assessment Act 1997 (Cth) s 115-105; *Tax Laws Amendment (2013 Measures No. 2) Act 2013*, No. 124.
49. November 2013 Release, *supra* note 23, item 9.
50. Income Tax Assessment Act 1997 s 855-1.
51. As this is a non-final withholding tax, taxpayers will be required to lodge a tax return for the amount withheld but may be later entitled to a refund if they have withheld an amount in excess of their liability.
52. May 2013 Release, *supra* note 45, attachment B.

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relate.[53] Dealings between entities in the same corporate group will not be relevant to calculations of this test.[54]

v. Dividend Washing

Rather than adopting a transparent entity approach, Australia reduces double-taxation of company profits by allowing shareholders to claim tax credits against dividend income for the tax paid by the company (known as "imputation credits"). But not all shareholders are able to (fully) use imputation credits. While there are restrictions to prevent trading in imputation credits, the previous government announced further changes to deny what was effectively a second application of imputation credits to shareholders who sell shares ex-dividend (after claiming the imputation credit) and purchase equivalent cum-dividend shares (on which the imputation credit may also be claimed).[55] The proposal has the new government's support.[56]

C. South Korea

1. *Overview*

For the Korean government, expanding its tax base to secure tax revenues to deliver on its welfare pledges conveniently coincides with the current discussions on BEPS.

In recent years, the Korean government has focused on combating tax avoidance or tax evasion through intensive tax audits. Tax law amendments were announced on August 8, 2013 (Proposal). The Proposal includes some notable changes corresponding to the BEPS theme, such as tightening the existing controlled foreign corporation (CFC) regime, down-sizing long-standing tax incentives granted to qualifying foreign investments (QFI), and strengthening disclosure obligations and penalties for non-compliance. The Proposal was submitted to the National Assembly on September 30, 2013. If passed into law, it will be effective in 2014.

2. *Tightening CFC Regime*

The Korean CFC rules are intended to prevent Korean multinationals from deferring Korean tax by retaining income in a foreign corporation located in a low tax jurisdiction. Under the Korean CFC rules, a CFC is a foreign corporation that has an effective tax rate of 15 percent or lower during the immediately preceding three tax years and is specially-related to (i.e., controlled by way of share ownership, business dependency, or certain other means) a Korean major shareholder (and its related parties). A Korean major shareholder is a Korean corporation or resident that holds, directly or indirectly, at least 10 percent of the shares in a foreign corporation.[57]

If a foreign corporation is a CFC, the current rules stipulate that all retained income of the CFC is deemed to be distributed to Korean major shareholders, subjecting such share-

53. *Id.*
54. *Id.* attachment F.
55. *Id.*
56. November 2013 Release, *supra* note 23, item 11.
57. Law on Coordination of International Tax Affairs, art. 17 (hereinafter LCITA).

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holders to Korean income tax on a current basis.[58] Currently, an active business exception applies. A foreign corporation predominantly engaged in an active business with an office, store, plant or other fixed facility in its jurisdiction that meets certain requirements is not subject to the CFC rules. The Proposal would carve-out an exception to this exception. It provides that, even where the CFC rules are not currently applicable, if the level of the foreign corporation's passive income exceeds a certain benchmark (to be prescribed by presidential decree), the passive income retained by the CFC (but not the CFC's retained non-passive income) will be deemed to have been distributed as dividend to its Korean major shareholders. Passive income is defined as income derived from (i) holding shares or bonds; (ii) holding intellectual property; (iii) leasing ships, aircraft, or equipment; and (iv) investments made through investment trusts or funds. The purpose of this proposed amendment is to prevent any tax deferral of passive income using a foreign subsidiary, even if it has a substantive business overseas.[59]

To strengthen reporting obligations for Korean major shareholders (for computing the CFC's retained income), the Proposal introduces penalties for failure to submit requisite documentation equal to 0.5 percent of the CFC's retained income, up to a cap of KRW 100 million (approximately U.S. $90,000). For small and medium businesses, this cap is KRW 50 million (approximately U.S. $45,000).[60]

3. *Reducing Tax Incentives for QFIs*

a. Tax Exemption for Certain Dividends from QFIs

Korea has a long-standing regime, whereby certain QFIs in a Korean company (usually those with cutting-edge technologies or those housed in designated foreign investment promotion districts accepted by the Korean authorities), can enjoy a 100 percent exemption from Korean corporate income tax for three to five years and a 50 percent exemption for two additional years.[61] In addition, a dividend distributed by the QFI to its foreign shareholders is eligible for an equivalent tax exemption during the same period.[62] In the Proposal, however, the Korean government pointed out that no other OECD country provides tax exemptions for dividends to a foreign investor and raised the concern that these exemptions would create disparity between Korean resident and foreign shareholders. Consequently, the Proposal will discontinue this tax incentive for dividend payments. The amendment will apply to QFIs that are recognized as of January 1, 2014. The Proposal grandfathers dividends paid by QFIs accepted before January 1, 2014.[63]

b. Excluding Foreign Investment Tax Incentives for Certain Foreign Investments

The Proposal would also disallow the tax incentives for QFIs made by a foreign investor from a designated jurisdiction without a tax treaty or a bilateral investment treaty with

58. *Id.* art. 18(1); Enforcement Decree Under the LCITA, art. 36.
59. LOYENS & LOEFF, ASIA NEWSLETTER 14 (Autumn 2013), *available at* http://www.loyensloeff.com/nl-NL/News/Publications/Newsletters/Asia%20Newsletter/Asia_Newsletter_Autumn_2013.pdf.
60. CHOON CO, PHILIPPE SHIN & IN-HWA CHUNG, 2014 TAX LAW AMENDMENTS 3 (Jan, 13, 2014), *available at* http://www.shinkim.com/upload_files/newsletter/SHIN&KIM_TAX_Legal_Update_201401_en.pdf.
61. Special Tax Treatment Control Law, art. 121-2.
62. *Id.* art. 121-2(3).
63. LOYENS & LOEFF, ASIA NEWSLETTER, *supra* note 59.

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Korea.[64] In addition, the Proposal would require foreign-invested companies in Korea applying for qualification for foreign investment tax incentives to submit a list of their substantive shareholders. Any Korean investors disguised as foreign investors and foreign investors with a suspect identity will be excluded. The Korean government's intent to exclude unwarranted tax incentives to such investors is understandable. The Proposal requires a high level of precision in tracing foreign funds, however. In this global era, it is unclear whether this tracing exercise is workable.

4. *Information Obligations and Penalties for Non-Compliance*

Under the Proposal, a Korean corporation investing overseas would have a duty to report not only the transaction records of existing foreign subsidiaries but also the documents related to their loss generating transactions. Further, the Proposal would significantly expand the scope of Korean corporations subject to such reporting obligations. Corporations with 50 percent or more ownership interests in a foreign corporation come under the current rule.[65] The Proposal extends the reporting duty to corporations and individuals holding 10 percent or more interests. It also imposes a penalty of up to KRW 10 million for non-compliance. This Proposal is intended to expand the government's pool of information on taxpayers' financial conditions and to enable it to detect tax evasion through a disguised loss from business operations overseas.[66]

To secure the efficacy of the foreign financial account reporting (FFAR) system, the Proposal introduces draconian measures to ensure enforcement by requiring a Korean taxpayer who fails to report required financial assets to disclose their source. The Proposal imposes a penalty for non-compliance equal to 10 percent of the unaccounted funds, regardless of whether there is any deficiency in tax payment.[67]

5. *Expanded Exchange of Financial Information Under Treaties*

Under the Proposal, the scope of treaty-based inter-governmental information exchanges is expanded. The existing provision is the legal basis for the Korean tax authority to obtain financial information from financial institutions concerning a foreign or Korean individual or corporation. The Proposal adds a legal basis for obtaining financial information concerning two or more unidentifiable persons involved in a specific financial transaction. This enables Korea to respond to exchange-of-information requests from treaty partners.[68] While existing law provides a legal basis for the Korean tax administration to obtain financial information on non-resident individuals and foreign corporations for periodic exchanges of information with treaty partners,[69] the Proposal expands that scope to include financial information on both Korean resident individuals and Korean corpora-

64. Co, Shin & Chung, *supra* note 60, at 2–3.
65. Corporate Income Tax Law, art. 119.
66. EY, Global Tax Alert: Korea Announces 2013 Tax Reform Proposals 2 (2013), *available at* http://tmagazine.ey.com/wp-content/uploads/2013/09/2013G_CM3780_Korea-announces-2013-tax-reform-proposals.pdf.
67. Co, Shin & Chung, *supra* note 64, at 2.
68. LCITA, art. 31(2).
69. *Id.*

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tions.[70] Financial institutions that do not comply with information requests will be subject to penalties up to KRW 30 million.

D. Argentina

1. *Overview*

Argentina is also seeking to protect its tax base. Two relevant developments in the international tax domain are (i) the repeal of the exemption from capital gains tax that benefited non-resident shareholders in Argentine companies, and (ii) a Tax Court ruling applying the Argentine GAAR to disallow an international structure that could be construed as compliant under applicable laws.

2. *Non-Resident Capital Gains Taxation*

Effective as of September 23, 2013,[71] non-resident shareholders are subject to tax on capital gains from the sale of their shares in Argentine companies. This change, which also introduced a 10 percent dividend withholding tax, repealed an exemption that had been in place for almost twelve years.

The main aspects of the new rules are:

i. capital gains from the sale of shares, other equity participations, bonds, and securities realized by non-resident companies are subject to Argentine tax at an effective tax rate of 13.5 percent (on the gross price), or—at the non-resident's option—15 percent (on the actual capital gains realized);
ii. this treatment does not apply to non-resident individuals. They will be taxed on the gross transaction price at the residual 31.5 percent withholding tax rate. They do not have the option of being taxed on a net basis;
iii. of Argentina's double tax treaties, only treaties with Denmark, Germany, Italy, the Netherlands, Sweden, and the United Kingdom provide some relief. Even then, the relief is not uniform. Only Italian residents and German individuals benefit from full exemption from the Argentine tax. Residents in the other listed countries may see their Argentine tax burden reduced to 10 percent or 15 percent of the net gain, depending on their ownership percentage in the Argentine company (25 percent or less), and their character (corporate or individual);
iv. this tax treatment applies to non-residents, regardless of whether the Argentine shares or securities are traded on a stock market or have authorization for public offering;
v. the Argentine tax applies to transactions between two non-residents. In that case, the purchaser has a duty to assess and pay the Argentine withholding tax. While indirect transfers of Argentine companies are still outside the scope of Argentine tax, it is arguable that imposing payment liability on a non-resident would also be outside the scope of Argentine law. Consequently, collection of the Argentine capital gains tax may not be feasible. Tax collection may also be problematic for

70. *Id.*
71. Law No. 26893, Sept. 12, 2013, [CXXI] B.O. 32.728 (Arg.).

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transactions on foreign stock markets, where the non-resident purchaser of Argentine securities would not know who the seller is; and

vi. specific tax exemptions exist for certain classes of securities (e.g., publicly traded Argentine issued corporate bonds)[72] and for Argentine sovereign bonds; and

vii. profit distributions will be subject to 10 percent dividend withholding tax, regardless of whether the profits are remitted by Argentine companies or permanent establishments, increasing the Argentine tax burden on corporate profits to 41.5 percent. If distributions are made out of profits that have not been subject to Argentine income tax, both the 35 percent compensatory tax and the 10 percent dividend withholding tax apply, to equalize taxed and untaxed dividend distributions.

Argentina's double tax treaties provide relief in theory, but no actual relief is granted in practice because the minimum withholding treaty tax rate is 10 percent.

3. *Tax Court's Ruling on GAAR and International Structures*

Just before the reform was enacted, the Argentine Tax Court delivered a ruling disallowing an international tax planning structure based on the Argentine GAAR (economic reality principle). At issue in *Molinos Río de la Plata*[73] was whether the use of a Chilean holding company was a permissible business decision in light of the loss of tax revenue resulting from its interposition.

Molinos Río de la Plata S.A., an Argentine company, set up a Chilean company that applied for the Chilean holding company status. Under Chilean tax law, foreign source dividends and capital gains were not subject to Chilean tax. Dividends from the Chilean holding company were exempt from Chilean taxation. Further, under the then-applicable tax treaty between Argentina and Chile, dividends received by Argentine shareholders from a Chilean company were exempt from Argentine tax. Based on these rules, Molinos controlled its foreign companies through its Chilean holding company.[74]

The tax treaty between Argentina and Chile—which was terminated effective January 1, 2013—relied on the Andean Pact Model treaty under which resident countries surrender taxing jurisdiction in favor of source countries. The treaty did not contain limitation on benefits clauses or references to "conduit companies" or "beneficial owners." Nevertheless, the Tax Court referred to these concepts in a lengthy ruling and disallowed the structure based on the economic reality principle, finding it inherently "abusive."[75]

Argentina's GAAR provides that a transaction must be taxed according to its substance if the forms used are inadequate to achieve the participants' economic goals. Therefore, when forms are abused, they are to be disregarded. But Molinos did not abuse forms. On the contrary, the form was consistent with Molinos' economic purpose. An argument on which the Tax Court relied was that the result of implementing the legal forms was abusive because no tax revenue was generated for the Argentine government. But there are

72. Law No. 23576, July 19, 1988, [XCVI] B.O. 26.431 (Arg.).
73. Tribunal Fiscal de la Nación [Argentine Tax Court], Sala D, 14/8/2013.
74. *Id.*
75. *Id.*

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no Argentine rules preventing taxpayers from positioning themselves in situations where no tax is to be paid, whether transactions are cross-border or domestic.[76]

The Tax Court found that the Chilean holding company regime was created after the Chile-Argentina double tax treaty became effective. Consequently, Chilean holding companies were not originally within the ambit of the treaty. In so finding, the Court disregarded the ruling of the Chilean tax administration. More importantly, the Argentine tax administration had not issued a ruling stating that it would not apply treaty benefits to dividends from Chilean holding companies. Argentina and Chile renegotiated the treaty without referring to this holding regime. The Tax Court ruling is currently on appeal to the Argentine Supreme Court.[77]

E. Peru

1. *Overview*

The Peruvian government has also shown its determination to protect its tax base, particularly in the current economic climate that has made it difficult for the tax administration to collect sufficient tax.

In July and August 2012, new legislation was passed to modify, amongst others: the Tax Code, Income and Value Added Tax, Customs Duties, and Criminal Tax. Most of this legislation is effective as of January 1, 2013. The changes in Peru mainly impact specific and general anti-avoidance provisions, taxation of indirect share transfers, and CFC and TP rules.

2. *Specific Anti-Avoidance Rules*

a. Taxable Capital Reduction

As a general rule, dividend distributions are subject to 4.1 percent withholding tax when made to resident or non-resident individuals or resident entities. The concept of dividend distribution has been extended, inter alia, to include capital reductions up to the limit of profits, revaluation surplus, adjustment by inflation, premiums, and freely disposable reserves (Profits) if these have been previously capitalized, except to cover losses.[78]

To prevent entities from avoiding immediate application of the 4.1 percent withholding tax by reducing capital before distributing or capitalizing Profits, a new rule, effective January 1, 2013, deems dividends to be distributed up to the amount of Profits of an entity, as of the date of adopting the capital reduction agreement, regardless of whether Profits have been previously capitalized. Any future distribution of Profits or capital reduction will be tax exempt, to the extent that those amounts have been previously taxed.[79]

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76. *Id.*
77. *Id.*
78. PwC, 2012: Doing Deals in Peru 13 (2012), *available at* http://www.pwc.com/es_PE/pe/doing-deals/assets/doing-deals-in-peru-2012.pdf.
79. PwC, Latin America Mining Taxation Symposium: Lunch and Panel Discussion (Nov. 28 2012), *available at* https://www.pwc.com/ca/en/mining/publications/pwc-latin-america-tax-symposium-lunch-panel-presentations-brochure-2013-03-en.pdf.

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b. Indirect Deductions of Provisions for Bad Debts Between Related Parties

Capital losses are generally deductible. Provisions for bad debts between related parties, however, are not. As of January 1, 2013, the difference between the nominal value of a debt between related parties and the value for which it is subsequently transferred to a non-related party with full debtor credit risk will not be deductible to the transferor. When the debt transfer generates an account receivable for the transferor, any provision or write-off related to that account receivable will also be a non-deductible expense.[80]

c. Non Deductibility of Losses on Sale of Stock

Effective January 1, 2013, "wash-sales" losses are no longer deductible. Capital losses generated on the sale of securities will not be deductible if (i) on the date of sale or within the following thirty days, the seller acquires securities or a purchase option of the same kind; and/or (ii) within thirty days before the sale, the seller acquires securities or a purchase option of the same kind. This rule will not apply if, after the sale, the seller no longer owns any security of the same kind (*i.e.*, any security that grants the same rights and has been issued by the same entity).[81]

3. *GAAR*

The most significant change to the Peruvian Tax Code came with the introduction of "Rule XVI,"[82] a GAAR, enacted on July 18, 2012. The scope of the GAAR's application remains unclear since regulations are still pending.

The GAAR allows the tax administration to consider the actions, situations, and economic relations effectively performed, established, or intended by taxpayers to determine the substance of the taxable event. Circumstances that are deemed artificial or improper to achieve the intended result and that imply a tax benefit that otherwise would not have been obtained will be subject to re-characterization.[83]

To this extent, the GAAR establishes that, if tax avoidance is detected, the tax administration is entitled to collect the tax and impose fines, reduce the amount of tax credits and tax losses, or eliminate any tax advantage. The tax administration may also demand the return of any amount that may have been unduly refunded to a taxpayer.[84]

4. *Indirect Share Transfers*

Effective January 1, 2013, income generated from an indirect transfer of shares of Peruvian entities is considered Peruvian-sourced income and, therefore, subject to Peruvian income tax. Under this new rule, an indirect share transfer occurs where shares of a non-Peruvian entity that owns shares of a Peruvian entity, directly or indirectly, are transferred, and,

80. *Id.*
81. *Id.*
82. Decreto Legislativo No. 1121, Julio 18, 2012, NORMAS LEGALES (Peru).
83. *Id.*
84. *Id.*

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(i) within twelve months before the transfer, the fair market value (FMV) of the equity of the Peruvian entity owned by the foreign entity is equal to 50 percent or more of the FMV of the foreign entity's total equity; and
(ii) in that twelve month period, 10 percent or more of the capital of the non-Peruvian entity is transferred.

Where shares of a tax haven resident entity are transferred, the taxpayer bears the burden to prove that an indirect share transfer has not occurred.[85]

5. *CFC Rules*

Peru introduced CFC rules effective January 1, 2013, to counter tax deferral of passive income earned by certain foreign entities controlled by Peruvian taxpayers. The CFC rules provide that, if a Peruvian taxpayer has a direct or indirect interest of more than 50 percent in a foreign entity located in a tax haven jurisdiction,[86] the passive income of the entity will automatically be attributed to the Peruvian taxpayer. The taxpayer will be subject to Peruvian income tax in that year and not when a future dividend is distributed by the CFC to the taxpayer. If the passive income is equal to or greater than 80 percent of all income of the CFC, all of its income will be considered passive income. Unless proven otherwise, all income generated by a CFC incorporated in a tax haven is presumed passive and presumed to generate an annual passive income equal to the maximum interest rate charged by banks multiplied by the purchase value of its shares or the value of its participation in net equity, whichever result is higher.[87]

6. *Transfer Pricing*

Effective January 1, 2013, three relevant changes were made to the existing TP regime, which applies to all transactions between related parties or to those carried on from, to or through tax havens.

a. Price Adjustments

Adjustments are made whenever prices agreed generate lower taxable income in Peru than the arm's length standard would. Under the new rules, the authorities must consider each transaction individually as long as this is consistent with the TP method used in the evaluation. The only transactions that will be adjusted are those that, when considered individually, generate lower Peruvian taxable income. The net effect (i.e., between "positive" and "negative" adjustments) of all transactions is no longer considered.[88]

85. PwC, 2012: Doing Deals in Peru, *supra* note 78, at 179.
86. Peru has both a black list and a general definition for tax haven. The definition includes low tax countries where the effective income tax rate is equal to or less than 50 percent of the Peruvian income tax rate applicable to income of the same character and meets one of the following criteria: the country (i) is reluctant to provide information related to taxpayers subject to low taxation, (ii) has a ring-fencing regime, or (iii) advertises itself (or is perceived) as being able to be used by non-residents to escape from taxation in their residence country.
87. *See* PwC, 2012: Doing Deals in Peru, *supra* note 78, at 181.
88. PwC, International Transfer Pricing 2013/14 670 (2013), http://www.pwc.com/gx/en/international-transfer-pricing/assets/itp-2013-final.pdf.

The adjustment will be effective for both parties, irrespective of their tax residence. Previously, both parties had to be Peruvian residents for bilateral adjustment to attach. That requirement has been eliminated. For non-resident parties, bilateral adjustments will only apply to transactions that could trigger taxable income in Peru and/or deductions in determining Peruvian income tax.[89]

Adjustments are attributed to the corresponding tax period, according to attribution rules in the tax law (accrual regime for corporate taxpayers). If, under these rules, the adjustment cannot be attributed to a particular period, it will be allocated proportionally among all tax periods to which income or expense has been allocated.[90]

b. Commodities

To determine prices of internationally-traded commodities, a specific method has been included within the comparable uncontrolled price method. This method has been imported from Argentina. Ecuador, Uruguay and, to some extent, Brazil, also use it. The pricing of a specific transaction will be based on the international price without taking into account the particularities of each case. This method does not apply where the taxpayer has entered into futures contracts to hedge the import or export of commodities or where there is irrefutable evidence that the international intermediary has real presence in its territory of residence and its core business does not consist of obtaining passive income or of acting as an intermediary in trading transactions with members of the same group.[91]

7. *APAs*

The scope of APAs has been extended. In the past, the tax administration could only enter into APAs with resident taxpayers regarding international operations. The tax administration may now enter into APAs with resident taxpayers relating to domestic or international operations and with other tax administrations in jurisdictions with which Peru has concluded a double tax treaty.[92]

89. *Id.*

90. *Id.*

91. KPMG, PERU: MODIFICATIONS TO TRANSFER PRICING REGULATIONS (Aug. 14, 2012), *available at* http://www.kpmg.com/Global/en/IssuesAndInsights/ArticlesPublications/taxnewsflash/Documents/peru-aug14-2012.pdf.

92. Monica Calijuri et al., *Base Erosion and Profit Shifting: Views from Peru, Brazil and Mexico*, TAXES: NEWSLETTER OF THE INT'L BAR ASSOC. LEGAL PRACTICE DIV. (Int'l Bar Assoc., London, Eng.), Feb. 2014, at 72.

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