2018 June

tax newsletter

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PKF Worldwide Tax Update

Welcome

In this second quarterly issue for 2018, the PKF Worldwide Tax Update newsletter 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, and its tax experts specialise in providing high quality tax advisory services to international and domestic organisations in all our markets.

In this issue featured articles include discussions on:

- Key tax changes for 2018 (and beyond) in Malaysia, Taiwan, Turkey and the UK
- Interesting (upcoming) European Court of Justice case law in Austria and Germany
- VAT developments in Austria, Italy, Romania and the United Arab Emirates
- Tax amnesty developments in Italy and Russia
- Developments in the area of international corporate income tax in Portugal (capital gains, PEs), Slovakia (exit tax) and South Africa (CFC legislation)
- Changes to the participation exemption regime in Belgium
- An update on C Corporations as a result of the recent US Tax Bill.

The PKF Worldwide Tax Update for the second quarter of 2018 is informative and interesting. Please contact the PKF tax expert directly (mentioned at the foot of the respective PKF Commentary) to discuss any tax matter further or, alternatively, contact any PKF firm (by country) at www.pkf.com/pkf-firms.

2018/19 Worldwide Tax Guide

Last year's PKF Worldwide Tax Guide featured 130 countries and was a resounding success with almost 2,000 distributed globally. We are extremely grateful to all those that provided country submissions, and of course, to each person who ordered a guide and supported this very marketable and impressive publication. The production of the 2018/19 Worldwide Tax Guide is underway and we look forward to your continued support. An **Order Form** is provided at the end of this PKF newsletter. Thank you for your continued support.

Contents

Contents continued...

PKF

Chartered Accountants
& Business Advisers

Austria

ECJ VAT case law – 'Active' supply in a chain transaction

In its ruling of 21 February 2018 (C-628/16, Kreuzmayr GmbH) the ECJ consolidates its case-law on the assignment regarding the 'active' supply in the course of successive supplies relating to the same goods. Consideration of the questions referred:

- In order to determine which of the two supplies the intra-Community transport should be ascribed to, it is necessary to undertake an overall assessment of all the specific circumstances of the case. In that assessment, it is necessary to determine, in particular, when the second transfer of the right to dispose of the goods as owner, to the person finally acquiring the goods, has taken place (see, to that effect, judgment of 26 July 2017, *Toridas*, C 386/16, EU:C:2017:599, paragraphs 35 and 36 and the case law cited).

- In a situation where the second transfer of the right to dispose of the goods as owner took place before the intra-Community transport occurs, the intra-Community transport cannot be ascribed to the first supply to the first person acquiring the goods (judgment of 26 July 2017, *Toridas*, C 386/16, EU:C:2017:599, paragraph 36 and the case law cited).

- In order to determine whether a supply may be classified as an 'intra-Community supply', account must be taken of the purchaser's intentions at the time of the acquisition of the goods in question, provided that they are supported by objective evidence (see, to that effect, judgment of 16 December 2010, *Euro Tyre Holding*, C 430/09, EU:C:2010:786, paragraph 34 and the case law cited).

- If the ultimate buyer was the owner of the goods before the intra-Community transport took place, it follows that the intra-Community transport must be ascribed to the supply which took place between the intermediary operator and the person ultimately acquiring the goods, and that the first paragraph of article 32 of the VAT Directive is applicable only to the second supply.

PKF Comment

The interpretation of the European Court of Justice is problematic because, if rigorously implemented, the simplification rule for intra-community triangular transactions (art 141 VAT Directive) would become obsolete if the intermediary operator is responsible for the transport. The simplification assumes that, in an IC triangular transaction, the 'active' supply is the first one and not the second one. However, as in a triangular transaction the ultimate buyer is already known at the beginning of the transport, the first supply could no longer be considered as the 'active' supply. In order to gain legal certainty we have to wait for further case law. However, we recommend to always consult with the intermediary operator in a triangular transaction before contracting transport.

For further information or advice on Austrian taxation, please contact Thomas Außerlechner at ***thomas.ausserlechner@pkf.at*** *or call* ***+43 1 51 28 780****.*

»BACK

Belgium

Belgium introduces 100% dividend participation exemption

Following a tax reform of 25 December 2017, Belgium has not only decreased its Belgium corporate tax rate to 20.4% - 29.58% (2018-2019) and 20% - 25% (as of 2020), but has also increased its participation exemption from 95% to 100% as far as qualifying dividend income is concerned. This new rule enters into force as of 2018. In summary, "qualifying dividend income" is dividend income (including liquidation proceeds) derived from shareholdings (i) representing a minimum shareholding value of 10% or EUR 2,500,000, (ii) which has been held for at least 1 year (prior to or after the dividend distribution date) and (iii) whereby the corresponding subsidiary is "normally taxed". Note that "investment companies" based in Belgium only need to comply with the subject-to-tax test, but not with the minimum shareholding test to benefit from the participation exemption. As was the case before, if the Belgium shareholder has insufficient tax capacity to fully deduct the participation exemption in a given financial year, the excess participation exemption can be carried forward to future financial years without limitation in terms of time and amount. Currency gains relating to dividend income (and capital gains on shares) also qualify for the Belgium participation exemption. Following this change in Belgium tax law, both dividend income and realized capital gains on shares are now eligible for a 100% participation exemption subject to satisfying the same conditions.

PKF Comment

This change in Belgium tax law is highly welcomed by the Belgium and international business community as it further enhances the attractiveness of Belgium as a traditional holding company location. Feel free to reach out to Kurt De Haen at ***kurt.dehaen@pkf-vmb.be*** *or call* ***+32 2 460 0960*** *with any further questions.*

»BACK

Bulgaria

Dormant companies no longer required to submit annual financial statements with the Company Register

As from 1 January 2018 legal entities that have not performed any trading activities during the preceding financial year are no longer obliged to submit their Annual Financial Statements with the Bulgarian Company Register. However, the fact that the company was non-operational in the past tax year should still be declared with the Company Register. The deadline for this is 31 March 2018. It should also be noted that dormant companies shall continue to submit their Annual Tax Returns with the tax authorities as per the regulations of the Corporate Income Tax Act.

PKF Comment

The tax consultancy team of PKF Bulgaria has substantial knowledge and expertise. They are in the position to 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 on* ***venzi.vassilev@pkf.bg*** *or call* ***+359 2439 4242****.*

»BACK

Germany

Unrestricted tax exemption for capital gains derived from disposal of shares between corporations in an inbound situation

In general, gains derived from the disposal of investments in other corporations are exempt from German corporate income tax. However, 5% of these gains are considered to be non-deductible business expenses at the level of the parent corporation (in German the so-called *Schachtelstrafe* according to sec. 8b para. 3 German Income Tax Code).

In May 2017, the Supreme Tax Court (BFH) judged that the *Schachtelstrafe* is not applicable to foreign corporations – due to a minimum holding requirement of 1% in corporations based in Germany – subject to limited tax liability in Germany (inbound-case). The court held that adding back deemed non-deductible business expenses is only justified if there is a connecting factor, e.g. the allocation of the shares to a permanent establishment in Germany. The decision is not only relevant to companies domiciled in non-treaty countries because the *Schachtelstrafe* does not apply anyway if a corporation is subject to limited tax liability, which is determined at the time of its initial assessment for tax purposes and not at treaty level.

Whereas German corporations have to consider the add-backs concerning their dividends received from foreign companies (outbound case), this judgment is the next step in creating legal certainty with regard to the tax exemption of capital gains derived from a disposal in an international context. Nevertheless, the BFH enforces its previous decisions in which it held that the national rules on deductions from dividend income override any relevant treaty provisions.

PKF Comment

Since the above mentioned BFH judgment is not in line with the current administrative practice, the taxpayer should apply to amend the underlying tax assessment notices, if still possible. It remains to be seen how the tax authorities and the legislator will react to the judgment, so this aspect should be kept in mind whenever such disposals are made in the future. For further information or advice concerning German dividend received deduction or any advice with respect to German taxation, please contact Isabee Falkenburg at ***isabee.falkenburg@pkf-fasselt.de*** *or Thomas Rauert at* ***thomas.rauert@pkf-fasselt.de*** *or call* ***+49 40 35552 137****.*

»BACK

Is German trade tax on dividend income in line with EU law?

German tax law usually exempts foreign dividends from trade tax to avoid double taxation and to ensure equal treatment of investments in domestic and foreign corporations (according to sec. 9 no. 7 German Trade Tax Act). Although the rules are intended to ensure equal tax treatment, EU and non-EU dividends have to meet different exemption requirements, generally speaking:

i. 15% minimum holding requirement for investments in third-country companies while only 10% for investments in EU-companies.

ii. For investments in third-countries only: proof that the dividends were received from an active business.

Against this background the European Court of Justice (ECJ) has to decide whether German dividend taxation violates the free movement of capital according to Art. 63 TFEU. Since these are fundamental issues of taxation the ECJ has to deal with (case pending before the ECJ C-685/16, EV v Finanzamt Lippstadt) the decision will not only affect Germany. There will also be an impact on international group tax law in general. The opinion of Advocate General (AG) Melchior Wathelet (published on 7 February 2018) might be seen as a pioneering preliminary decision. The AG first focused on which freedom was applicable: the free movement of capital or the freedom of establishment by concluding that the German rules should be analysed under the free movement of capital. The AG further concluded that the German legislation is not compatible with the free movement of capital as it sets stricter requirements for exempt dividends received from a non-resident company than those applicable to a German resident paying company. We will have to wait and see whether the ECJ follows its AG.

PKF Comment

*Since the expected decision is a landmark decision, current issues and the related assessment notices should be kept pending and any related provisions would also need to be checked to meet the requirement of worldwide equal tax treatment. For further information or any advice with respect to German taxation, please feel free to contact Isabee Falkenburg at **isabee.falkenburg@pkf-fasselt.de** or Thomas Rauert at **thomas.rauert@pkf-fasselt.de** or call **+49 40 35552 138**.*

»BACK

Hungary

'Tax Authority 2.0' – improvements for a competitive and effective tax authority

Paperless tax audit

From 1 January 2018 the Hungarian Tax Authority has introduced a paperless, electronic tax audit system. The main goal of the system is to spread electronic access and administration within the public administration to make tax procedures faster, to reduce the administration burden for the parties involved in the proceedings and to make the whole tax review more cost-effective. The electronic paperless tax audit system is not mandatory. Taxpayers may request it from the Tax Authority. Performing procedural acts and other obligations can be fulfilled the electronic way instead of by courier or personal appearance.

Prior announcement of the intention of self-revision

According to new regulations that came into force on 1 January 2018 taxpayers may indicate their intention to the Tax Authority for carrying out self-revision. From that announcement onwards the Tax Authority cannot initiate a tax audit related to the taxes which are concerned by the self-revision. The 'protected period' covers 15 days counting from the announcement. This option is available only once for each announced tax type and taxation period.

VAT - The renewed electronic platform of the Online Invoicing System

From 1 July 2018 taxpayers who issue an invoice from a pre-printed block of invoices must report this invoice online and in real time to the Tax Authority within the following deadlines:

- If the VAT amount exceeds HUF 100,000 but does not exceed HUF 500,000 the time limit is five calendar days after the issue.
- If the VAT amount exceeds HUF 500,000 the time limit is one calendar day after the issue.

The new electronic platform of the Tax Authority (https://onlineszamla-test.nav.gov.hu/) provides technical information about test procedures and functioning of the system. Furthermore, taxpayers can find relevant legislation in German as well as English.

PKF Comment

*According to the available information several electronic tax audits have been finished without any problems. Hopefully the administrative burden on taxpayers will decrease significantly as a result of the improvements. For further information or advice concerning Hungarian taxation, please contact Krisztián Vadkerti at **vadkerti.krisztian@pkf.hu** or call **+36 1 391 4220**.*

»BACK

Italy

Introduction of web tax on digital services

As from 2019, a web tax will come into effect. Web tax is an indirect tax levied on Italian and foreign economic operators carrying out more than 3,000 (three thousand) digital transactions per calendar year. Including downloads of software, images, screensavers, books, subscriptions to newspapers or online magazines, the provision of advertising space, the use of search engines on the internet, downloads of music or games, search engines set up to sell objects, or all those "automated" transactions with minimum human intervention carried out between B2B economic operators. Traditional B2C e-commerce will not be targeted.

However, in order to identify exactly which transactions are taxable an implementing decree needs to be issued first, which should be adopted by 30 April 2018. The 2018 Budget Law has come with significant amendments compared to the initial draft law, specifically with regard to the rate and the collection method. The tax rate is fixed at 3% and is to be settled by the buyers of the services (unless the supplier declares in the invoice that it has not reached the threshold of 3,000 transactions in the calendar year), net of Value Added Tax and regardless of where the transaction is concluded.

In addition, collection methods have been modified: direct payment and withholding tax applied by banks have been replaced with a withholding tax applied by the tax withholding agents which is to be paid to the Treasury by the 16th day of the month following the payment of the consideration and cannot be offset against Italian income tax.

PKF Comment

*How will the application of the web tax affect Italian web companies? It is clear that the introduction of the new tax could harm local companies which, for the same implementation, could find themselves forced to increase prices to keep their cash untouched. Moreover, the extra 3% will inevitably affect the profit margins of companies unable to raise prices. For this reason, the legislator has put in place special safeguard rules, which provide for the application of the web tax only if the number of digital services that can be attributed to an operator exceeds three thousand transactions per year. However, it is not easy to prove at the level of web service providers that this limit has not been exceeded as the exemption needs to be indicated on the invoice document and, at the same time, payment and invoicing for subjects working in the digital sector are completely automated. We await further details and fine tuning on this matter. For further information on this matter or any advice on Italian taxation, please contact Fabrizio Moscatelli at **fabrizio.moscatelli@tclsquare.com** or call **+39 010 818 3250**.*

»BACK

VAT exemption regime for vessels used for navigation on the ‘high seas’

One year after issuing Resolution No. 2/E of 12 January 2017 and after several requests for clarification, the Italian tax authorities (Agenzia della Entrate) issued further clarifications on the VAT regime for vessels to be used for navigation at the ‘high seas’ with Resolution No. 6/E of 16 January 2018.

Operations relating to the naval sector fall into the scope of export-related transactions and are therefore not taxable for VAT purposes if the naval unit meets both of the following requirements: (i) it is used for navigation at the high seas and (ii) it is intended for commercial, industrial or fishing activities or is used for transportation of paying passengers, coastal fishing or rescue or sea-going operations (article 8bis letter a of DPR 633/1972).

According to Resolution No. 2/E, in order to benefit from the above mentioned tax benefit the vessel owner must prove that the actual use of the ship at the high seas exceeds 70% of total voyages made in the previous year.

The meaning of ‘high seas’ is that part of the sea exceeding the maximum limit of twelve nautical miles measured from the baselines prescribed by international sea law (article 3 of the Montego Bay Convention on the Law of the Sea). Compliance with this condition must be verified for each year on the basis of the official documentation submitted by the vessel owner or the one who has responsibility over the vessel.

With specific regards to the adequate ‘official documentation’ required to prove the prevalence of voyages carried out at the high seas, Resolution No. 6/E provides the following list of documents that will be considered as official:

- The Log Book, also known as the ship’s log or captain’s log, according to articles 169-173 and 174 of the Italian Navigation Code.
- The maps of voyages as well as the data extracted from the ship’s tracking or identification systems (e.g., with no limitation, the A.I.S., GPS etc.).
- The charter contracts, invoices and relevant payments.

‘Voyage’ will mean any cruise carried out between ports (Italian, EU and/or non-EU ports) where loading or offloading of goods and/or people take place or more generally where said ports are used by the vessel for the purposes of carrying out its commercial activity.

The same Resolution also clarifies that ‘voyage’ will also cover any cruise starting from and coming to the same port (so-called circular cruises or voyages). If during a circular voyage the twelve nautical miles at some point will be crossed by the vessel to sail the high seas then the voyage is qualified as an ‘international voyage’ (voyage at the high seas). Also any voyage entirely carried out outside the Italian territorial waters will be considered an international voyage.

In respect of the calculation of the 70% threshold, any displacement of the vessel to another port of shipyard for technical reasons (even if those reasons are connected to the vessel’s commercial activity cannot be considered as a ‘voyage’ and cannot therefore be included into the calculation of the 70% of voyages.

The high sea cruising condition will be verified each year. In case of a percentage of voyages exceeding 70% during a calendar year, the VAT exemption applies to the subsequent calendar year. In case the threshold does not exceed 70% during the calendar year it will be no longer be possible to benefit from the VAT exemption as from 1 January of the subsequent year, except if:

- The vessel is under construction, or
- The vessel has not yet carried out any voyage at sea.

In the cases only, it is possible to apply the VAT exemption on the basis of a statement declaring the intention to use the vessel on the high seas. In order to issue a VAT exempt invoice the supplier will require the owner or the person responsible for the vessel to provide a statement attesting (i) the declarant’s personal data (ii) the legal status of the declarant in relation to the vessel and (iii) the period for which the statement is provided. In the subsequent year, however, the declarant will verify if the 70% high sea voyages condition is met and in the event of failure he will inform the supplier accordingly. If on the contrary the condition is met the declarant will provide the supplier with the official documentation proving that voyages on the high sea have been carried out.

PKF Comment

*For further information on this matter or any advice on Italian taxation, please contact Fabrizio Moscatelli at **fabrizio.moscatelli@tclsquare.com** or call **+39 010 98 45100**.*

»BACK

Tax amnesty – introduction of the new mini tax shield

Further to article 5septies of Legislative Decree No. 148/2017 related to the 2018 Budget Law, approved by Law 172 of 4 December 2017, a mini tax shield has been introduced for those previously resident abroad and former cross-border workers. The mini tax shield has been improperly referred to as a mini voluntary disclosure as it applies to fewer individuals and items than the Voluntary Disclosure programme (originally made available by Law No. 186/2014).

Scope of subjects and activities

Under article 5*septies* of the converted Law Decree, Italian residents (or their heirs), who (i) previously resided in a foreign country and registered with the Civil Registry of Italian citizens living abroad (*Anagrafe Italiani Residenti all’Estero* or AIRE) or (ii) performed work activities abroad on a continuous basis in frontier zones and neighbouring areas, may commence a voluntary disclosure procedure to regularise their tax positions with respect to undeclared financial assets derived from foreign employment and professional income and held abroad on 6 December 2017.

The following assets can be regularised:

- Sums derived from employment or self-employment abroad, deposited in foreign current accounts and savings books and breaching the rules regarding tax monitoring.
- Sums and assets derived from the sale of real estate held in the country where the individual has worked on a permanent basis.

Payment deadlines

Taxpayers must file a request by 31 July 2018 and pay an amount equal to 3% of the assets’ value on 31 December 2016, covering taxes, interest and penalties due, by 30 September 2018. They may alternatively choose to pay the relevant amount in three equal monthly instalments (whereby the deadline for the first instalment payment would also be 30 September 2018).

Verification process and assessments

- The mini tax shield is not applicable to taxpayers who applied for the previous voluntary disclosure programs.
- By way of derogation from the rules laid down in the Statute of the taxpayers and solely for sums and assets regularised under article 5septies, the time limit for assessments that would normally expire with effect from 1 January 2018 have been extended until

30 June 2020, giving much more latitude to the tax authorities to carry out verifications, controls and investigations

It should be kept in mind that the new provisions on the automatic exchange of information (AEOI) between Italy and many foreign countries represent an important tool to support any assessment actions.

PKF Comment

*For further information on this matter or any advice on Italian taxation, please contact Stefano Quaglia at **stefano.quaglia@tclsquare.com** or call **+39 010 81 83250**.*

»BACK

Malaysia

2018 Budget highlights

The Prime Minister and Finance Minister of Malaysia unveiled the 2018 Budget on 27 October 2017 under the theme 'Prospering an Inclusive Economy and Balancing between Worldly and Hereafter, for the Wellbeing of Rakyat, Towards TN50 Aspiration'. Below are some of the salient tax highlights of the 2018 Budget.

Participation in the Organisation for Economic Cooperation and Development (OECD) taxation initiatives

Malaysia is committed to fulfil the Organisation for Economic Co-operation and Development (OECD) Base Erosion and Profit Shifting (BEPS) Plan Initiative as well as the Automatic Exchange of Information commencing in September 2018.

Implementation of Earning Stripping Rules (ESR) to replace Thin Capitalisation Rules (TCR)

TCR were first introduced in the Malaysia 2009 Budget but their implementation has been deferred a few times up to 1 January 2018. ESR were introduced by the OECD because interest is one of the simplest profit-shifting techniques available in international tax planning where the mix of debt and equity ratio of an entity can be easily adjusted within multinational companies (MNCs). The 2018 Budget has announced that ESR would replace TCR, whereby interest deductibility on loans between related companies within the same group will be subject to a restriction based on a ratio to be determined by the Malaysia Inland Revenue Board (MIRB). The ratio that is likely to be adopted will range between 10% to 30% of the company's profit before tax either using the Earnings before Interest and Taxes (EBIT) or the Earnings before Interest, Tax, Depreciation and Amortisation (EBITDA) approach. The afore mentioned Rules will be effective as from 1 January 2019.

Tax Incentive Automation Incentive/Trans-formation to Industry 4.0

Currently, a manufacturer in high labour intensive industries (rubber products, plastics, wood, furniture and textiles) is eligible for Accelerated Capital Allowance (ACA) and Automation Equipment Allowance (AEA) of 200% on the first MYR 4 million incurred on the acquisition of automation equipment in the basis period for the year of assessment 2015 to the year of assessment 2017.

However, in an effort to further promote automation in labour intensive industries, the Malaysia government has proposed to extend the incentive period up to the year of assessment 2020.

A similar tax incentive is also proposed in the 2018 Budget to encourage the transformation to Industry 4.0 (the 4th Industrial Revolution) which involves the adoption of technology drivers such as big data analytics, autonomous robots, industrial internet of things, etc. by the manufacturing sector and its related services. It is proposed that ACA and AEA be provided on the first MYR 10 million qualifying expenditure incurred in the years of assessment 2018 to 2020 and be fully claimable within 2 years of assessments.

Reduction of personal income tax rates

The tax rates for resident individuals on three chargeable income bands between MYR 20,001 to MYR 70,000 will be reduced by two percentage points as follows, with effect from YA 2018:

Chargeable income	Existing rates	Proposed rates	Reduction
(MYR)	(%)	(%)	(%)
1 – 5,000	0	0	-
5,001 – 20,000	1	1	-
20,001 – 35,000	5	3	2
35,001 – 50,000	10	8	2
50,001 – 70,000	16	14	2
70,001 – 100,000	21	21	-
100,001- 250,000	24	24	-
250,001 – 400,000	24.5	24.5	-
400,001 – 600,000	25	25	-
600,001 – 1,000,000	26	26	-
Exceeding 1,000,000	28	28	-

PKF Comment

Based on the announcement made in the 2018 Budget, the Malaysia Inland Revenue Board (MIRB) will likely adopt more BEPS initiatives in the coming years. Therefore, MNCs and local groups of companies must be pro-active in reviewing their existing financing structure in Malaysia to be in line with the latest developments around BEPS initiatives in order to manage any of the associated tax risks. We believe this to be an area of focus by the MIRB in the coming years with more tax audit activities focusing on the BEPS initiatives and more tax legislation to be progressively introduced.

The ESR is also one of the BEPS initiatives that has been introduced in the 2018 Budget. The MIRB has yet to issue the relevant guidelines to clarify which method (i.e. the fixed ratio rule and/or the Group ratio rule, and any carry-back or carry-forward provision for unused interest) will be adopted as both methods have their own advantages and disadvantages.

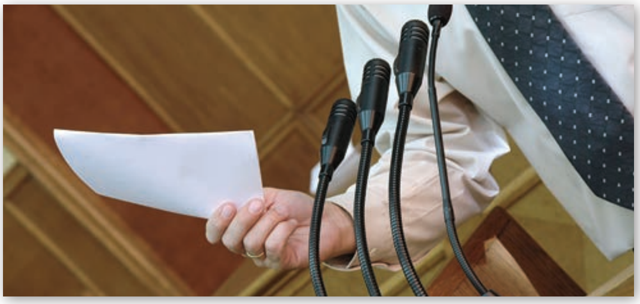
Taking into account that the relevant tax legislation to implement the above is still pending, MNCs are advised to arrange any of their new and existing financing with a view towards flexibility and the possibility to reserve or alter such transactions before upcoming maturity.

For further information or advice concerning Malaysia taxation, please contact Ai Chen, Lim at ***aichen@pkfmalaysia.com*** *or call* ***+603 6203 1888****.*

»BACK

Mexico

Introduction of the National Anti-Corruption System



The year 2018 will see the implementation in Mexico of the National Anti-Corruption System (the NAS) that has been brewing for three years with different reforms to the existing regulations like the Political Constitution as well as to various laws.

The NAS consists of four new laws and several amendments to existing regulations:

- National Anti-Corruption System Law - Ley General del Sistema Nacional Anticorrupción. (new),
- General Law on Administrative Responsibilities - Ley General de Responsabilidades Administrativas (new).
- Organic Law of the Administrative Justice Federal Court - Ley Orgánica del Tribunal Federal de Justicia Administrativa (new).
- Audit and Accounting for Federal Government Agencies Law - Ley de Fiscalización y Rendición de Cuentas de la Federación (new).
- Organic Law of the Attorney General's Office - Ley Orgánica de la Procuraduría General de la República (amended).
- Federal Criminal Code - Código Penal Federal (amended).
- Organic Law of the Federal Public Administration - Ley Orgánica de la Administración Pública Federal (amended).

Many U.S. companies active in Mexico may assume that their processes designed to comply with the Foreign Corrupt Practices Act (FCPA) are sufficient to comply with the new NAS laws. However, that is not necessarily the case. To some extent, the two laws overlap, but some significant differences also exist. Some of the most important variances include the handling of facilitation payments, books and records, and sanctions.

Companies must take a fresh look at NAS and make sure that employees, compliance teams, procedures and internal regulations are prepared to cover both laws. Mexican companies and U.S. businesses active in Mexico must understand that the new NAS regulations are more restrictive overall than previous anti-corruption laws, which were more lenient, resulting in widespread corruption and mistrust in the business environment.

PKF Comment

The enactment of the NAS regulations confirms the Mexican government's commitment to prevent and fight corruption, transparency and accountability. The NAS represents an important and noteworthy development in the fight against corruption in Mexico. For further information related to the NAS or any advice on Mexican taxation, please contact Mario Camposllera at ***mcamposllera@pkfmexico.com*** *or call* ***+52 33 3634 7162****.*

»BACK

Portugal

New rules for capital gains on share sales by non-residents

The 2018 Government Budget introduced a new rule that subjects capital gains realised by non-resident taxpayers on the sale of shares issued by a non-resident company to Portuguese income tax, when the value of such shares is significantly attributable to real estate property located in Portugal.

The new legislation is applicable to both non-resident individuals and non-resident corporations, who have now become liable for Portuguese tax on the sale of shares held in a non-resident company. Whenever the value of such shares, at any moment during the previous 365 days is attributable, directly or indirectly, for more than 50% to real estate assets located on Portuguese territory, except for real estate attributable to an agricultural, industrial or commercial activity which does not consist in the acquisition and disposal of real estate.

According to this new rule, a non-resident individual or corporation realising capital gains on the sale of shares in a foreign company whose assets are mostly derived from real estate located in Portugal will be subject to Portuguese income tax in Portugal. The tax rate levied on capital gains realised by non-residents is 28% for individuals and 25% for corporations.

PKF Comment

In case the seller of the shares is a tax resident in a country that has signed a double tax treaty (DTT) with Portugal, this rule must be analysed in light of the provisions of the DTT while also taking into consideration the Multilateral Instrument signed by that other country and its effects on the respective DTT (Portugal chose to apply article 9(4) of the MLI). For further information or advice concerning Portuguese taxation, please contact José Parada Ramos at ***paradaramos@pkf.pt*** *or call* ***+351 213 182 720****.*

»BACK

Romania

Amendments to the VAT split payment system

A VAT split payment mechanism has entered into force since the begining of October 2017. VAT taxable persons have to use a distinct bank account for cashing and payments representing VAT. With effect from 1 January 2018 the VAT split payment system has been amended. The split system is mandatory only for public and private companies under insolvency or that have VAT liabilities to pay. VAT-registered persons that meet one of the following criteria are required to open and use at least one VAT account:

- As of 31 December 2017, taxpayers with outstanding VAT liabilities exceeding RON 15,000 (large taxpayers), RON 10,000 (mid-sized taxpayers), or RON 5,000 (small-sized companies and individuals), if they are not paid by 31 January 2018.

  As a result, operators having registered liabilities exceeding the above mentioned thresholds as per 31 December 2017 and not paying VAT due by 31 January 2018 will fall under the scope of the split system with effect from 1 March 2018.

- With effect from 1 January 2018 taxpayers with outstanding VAT liabilities exceeding 60 working days as of the due date of more than RON 15,000 (large taxpayers), RON 10,000 (mid-sized taxpayers), RON 5,000 (small companies and individuals).

The VAT split system can be applied optionally by other companies (not covered by the afore mentioned criteria). Taxable persons who opt for the application of the VAT split payment system after 1 January 2018 will be granted a 5% reduction on the tax on profit/income of micro enterprises for the entire period in which they apply the scheme.

The new VAT method does not change any existing VAT rules. Companies that apply the VAT system will have to use a different bank account in respect of receipts and payments of VAT. VAT accounts will be opened, by default, with the various treasury units within the tax offices where taxpayers are registered. However, any taxpayer can opt to open an account with a commercial bank.

The system can cease to apply in the following situations:

- For taxpayers that opted to apply the system but are not required to: by the end of the tax year but no sooner than one year after they opted to apply the system.

- For taxpayers that apply for the system mandatorily:
  - Those with outstanding tax obligations: after a minimum period of six months.
  - Those subject to insolvency or insolvency prevention procedure legislation: once they cease being subject to it, provided that they are not liable to apply the system due to accruing outstanding liabilities.

PKF Comment

Although these amendments significantly restrict the scope of the VAT split system, the Romanian business environment that applies this system will be facing major difficulties regarding cash flow. Moreover, these changes will generate additional costs related to changing IT systems. For further information or advice concerning Romanian taxation, please contact Maria Popa at ***maria.popa@pkffinconta.ro*** *or call* ***+40 21 317 31 96****.*

»BACK

Russian Federation

A new round of tax amnesty

On 7 February 2018, the State Duma adopted in the first and the second reading legislation on the tax amnesty of repatriated funds and continuation of de-offshoring measures. On 19 February 2018, President Putin signed the legislation. This is actually a renewal of the tax amnesty held between 1 July 2015 and 30 June 2016, which did not meet lawmakers' expectations as the number of people who filed respective declarations did not exceed 7,000. However, the tax climate has significantly changed since then. The introduction of CFC (Controlled Foreign Companies) legislation and the imminent AEOI (Automatic Exchange of Information) between Russia and many other countries have forced Russian tax residents to restructure their foreign assets.

Assets covered and deadlines

The tax amnesty timeline applies from 1 March 2018 until 28 February 2019. The terms of participation in the tax amnesty program are the same as under the 2015-2016 program. Individuals (regardless of citizenship or tax residency) are allowed to declare the following assets to the Russsian tax authorities:

- Land, immovable property, vehicles and securites, including shares and equity participations in Russian and foreign companies legally or beneficially owned by the declarant at the time of filing the declaration.
- CFCs controlled by the declarant at the time of filing the declaration.
- Bank accounts and deposits with foreign banks which the declarant should have notified to the competent Russian tax authorities.
- Bank accounts beneficially owned by the declarant.

The bill expressly states that filing a declaration during the first stage of tax amnesty (2015-2016) does not prevent the declarant from filing another declaration during this round of tax amnesty.

Guarantees

- The declarant will be exempt from criminal liability for violations of currency control and tax laws regarding disclosed assets and CFCs. Tax fines do not apply.
- Facts and documents disclosed cannot be used to initiate criminal or administrative proceedings nor can they be used as evidence in such proceedings (except by the declarant himself).
- All facts that occurred before 1 January 2018 are covered, provided no criminal or administrative proceedings or tax audits were inititated at the time of submitting the declaration.
- Relief from administrative liability for violations related to the unlawful use of foreign accounts listed in the declaration. Possibility of extending the amnesty to accounts that were already closed at the date of filing of the declaration (this is of specific importance to current law offences as the fines range from 75 to 100% of illegal operations).

PKF Comment

This new round of tax amnesty will provide a second chance to those who wanted to declare their foreign assets but failed to do so in due time. For further information on this matter or any advice on Russian taxation, please contact Yulia Ponomarenko at ***y.ponomarenko@mef-consult.ru*** *or call* ***+7 495 988 15 15****.*

»BACK

Slovakia

New exit tax could make transfers of business assets more expensive

An amendment to the Income Tax Act effective 1 January 2018 (Act No. 344/2017) introduces a so-called 'exit tax' to be levied on both resident entities and permanent establishments of non-resident entities that shift assets outside the country, unless there has been a change in beneficial owner. The tax is levied when the shifted assets are declared as a line item on a corporate or personal income tax return.

Starting in 2018, tax of 21% will be charged on the difference between the fair value of the shifted asset (i.e. the value of the asset recognized on the balance sheet) at the time when the asset left Slovakia and the tax that would have been charged on the income earned if the asset had been sold along with its ownership rights to a new owner.

An example of where the exit tax would be charged is a company with its corporate seat or place of business in Slovakia which has transferred plant equipment to a branch office outside of the country. In this case, the difference between the fair value of the equipment and the sales price, which the company would have charged if it had sold the equipment instead to a customer, would be subject to tax at a rate of 21%.

PKF Comment

*This amendment was passed virtually at the very end of 2017 and is still being digested by tax advisers. Companies either headquartered or operating in Slovakia could be significantly affected by this change in tax law when they shift intangible and tangible assets between subsidiaries and branches within its organisation. For further information or advice concerning Slovak taxation, please contact Vladimir Pastierik at **pastierik@pkf.sk** or call **+421 46 518 3811**.*

»BACK

Definition of permanent establishment expanded to include online service providers

In an effort to stem the outflow of profits from Slovakia by foreign online companies, such as Uber and Airbnb, which operate digital platforms to provide services in the country, an amendment to the Income Tax Law (Act No. 344/2017) effective from 1 January 2018 specifically defines a digital platform. According to the amendment, "digital platforms" are hardware or software platforms that develop and manage applications.

Such digital platforms would be required to register in Slovakia for income tax as a permanent establishment if they provide services on a recurring basis as an intermediary.

The amendment involves an expansion of the definition of a permanent establishment in Slovakia to include the repeated provision of transportation and accommodation services at a permanent location within the territory of the country through a digital platform.

Under the amendment, the definition of a permanent establishment is also expanded to cover entities either representing a non-resident entity in negotiating, concluding and/or brokering the conclusion of contracts, or playing a major role in concluding contracts to be subsequently entered by a taxpayer with no change in the essential elements. This covers cases where a contract is concluded in the taxpayer's name or the subject-matter of the contract is either the transfer of ownership rights or the granting of rights for the use of assets owned by the taxable entity or of assets which the taxable entity has the right to use or to provide services to the taxable entity.

If such service providers fail to register for income tax as a permanent establishment, withholding tax will be charged on the transactions between entities in Slovakia and non-residential entities for the services. The withholding tax rate would range between 19% (the standard tax rate) and 35% if the ultimate beneficiary has its seat in countries with which Slovakia does not have a double taxation treaty or countries that have not signed the Convention on Mutual Administrative Assistance in Tax Matters.

PKF Comment

*Online marketers and service providers both inside and outside Slovakia should be aware of the impact this expansion of a permanent establishment in Slovak tax law will have on the tax treatment of transactions and profits flowing to them from Slovakia. For further information or advice concerning Slovak taxation, please contact Vladimir Pastierik at **pastierik@pkf.sk** or call **+421 46 518 3811**.*

»BACK

South Africa

Extending the application of CFC legislation to foreign companies held by foreign trusts and foundations

South African legislation has for many years contained anti-avoidance provisions in the form of controlled foreign company (CFC) rules which effectively tax South African residents on their percentage of income of a CFC. A CFC is defined as any foreign company where more than 50% of the participation rights (equity and voting rights) are held by one or more South African residents.

However, prior to the change detailed below, foreign companies which are held by foreign discretionary trusts or foundations did not fall into these CFC provisions resulting in the income of such foreign companies remaining outside of the SA tax net but still be included in consolidated financial statements for accounting reporting purposes in terms of International Financial Reporting Standards (IFRS) 10.

In terms of the G20/OECD base erosion and profit shifting (BEPS) report, Action 3 it was recommended that the scope of CFC rules be extended to include foreign companies that are consolidated into the accounts of a resident company in terms of IFRS.

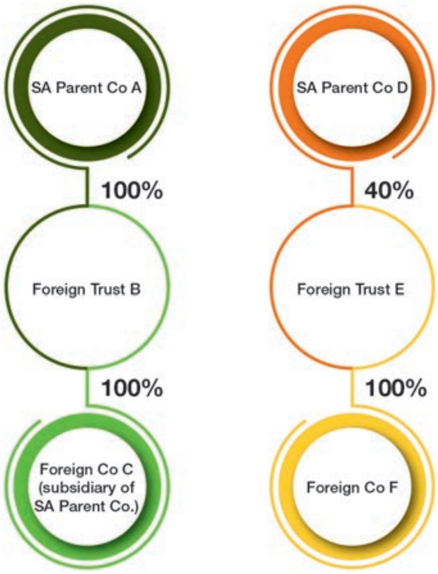
In order to affect this change, the definition of a CFC has been extended to include any foreign company that is consolidated in the financial statements of a South African resident company in terms of IFRS 10 and an additional proviso was inserted to allow for an inclusion of net income equal to the proportion of profits of the foreign company that is included for the purposes of the consolidated financial statements.

This will result in the net profit of that foreign company being included in the South African resident company's taxable income in proportion with the percentage of participation rights held in that company.

This change is demonstrated in these 2 examples as contained in the Explanatory Memorandum to the Amendment Act.

Example 1:
SA Parent Co A owns all the shares in Foreign Co C via a foreign trust B. SA Parent Co A includes in its consolidated financial statements the assets, liabilities, income, expenses and cash flows of foreign trust B and Foreign Co C effectively presenting the 3 entities as a single economic entity.

Example 2:
SA Parent Co D owns 40% of the shares in Foreign Co F via a foreign trust E. Although, SA Parent Co D has an indirect interest of 40% in Foreign Co F, it controls Foreign Co F. In terms of IFRS 10, a company that controls another is required to present consolidated financial statements. Therefore, SA Parent Co D includes in its consolidated financial statements a net percentage of 40% of the financial results of Foreign Co F determined after subtracting the non-controlling interest that is equal to 60%.



This change is effective for years of assessment commencing 1 January 2018.

PKF Comment

For further information or advice concerning South African taxation please contact Kubashni Moodley at ***kubashni.moodley@pkf.co.za*** *or call* ***+27 31 573 5000****.*

»BACK

Taiwan

Standard dividend withholding tax rate for non-resident shareholders increased

As from 1 January 2018 the standard dividend withholding tax rate for non-resident shareholders has been increased from 20% to 21%. The change is effective for dividends received on or after 1 January 2018.

PKF Comment

*This increase of the withholding tax rate for dividends and earnings distributed to foreign investments is one of the government's measures to improve the tax system in Taiwan. Prior to the amendment, dividends received by a non-resident shareholder were subject to a 20% withholding tax rate leading to a disparity between the tax burden on dividends distributed to foreign or domestic investors and resulting in a lower Taiwanese tax burden than the one suffered by a resident investor. For further information or advice concerning Taiwan taxation please feel free to contact Wisdom Lee at **wl@pkf.com.tw** or call **+886 2 8792 2628**.*

»BACK

Amendments to the Income Tax Act

On 7 February 2018, a number of amendments to the Income Tax Act were announced. They will be effective as from 1 January 2018 and the highlights can be summarised as follows:

- The corporate income tax rate will be increased from 17% to 20%.
- The surtax imposed on undistributed corporate earnings is lowered from 10% to 5%.
- The maximum personal income tax rate is lowered from 45% to 40%.
- Personal income tax deductions are significantly enlarged: among others standard deduction of 120,000 TWD (240,000 TWD for a married couple filing jointly) and salary deduction of 200,000 TWD.
- Regarding dividend income for domestic shareholders, the imputation tax system is abolished and dividend income is taxed based on the two following two alternatives, whichever is more advantageous: (i) dividend income is subject to the progressive personal income tax rate with 8.5% of dividend income available as tax credits, capped at 80,000 TWD or (ii) taxed separately at a 28% flat rate. For foreign shareholders, the standard withholding tax rate will be 21% (see also the previous article in this newsletter under the Taiwan section) while the surtax on undistributed earnings can no longer be offset against dividend withholding tax, with the exception of 2018, i.e. dividends distributed in 2018 can still make use of the tax credit.

PKF Comment

*These amendments aim to simplify the income tax system as well as to ease the tax burden on child-raising, individual salary income and low and middle-income families. The corporate income tax increase will be used to compensate for related tax losses. For further information or advice concerning Taiwan taxation please feel free to contact Wisdom Lee at **wl@pkf.com.tw** or call **+886 2 8792 2628**.*

»BACK

Turkey

Various tax amendments

A draft law on various tax amendments was published in the Official Gazette on 5 December 2017:

- The corporate income tax rate for all companies will be increased from 20% to 22% for the 2018, 2019 and 2020 tax years. The law also authorises the Council of Ministers to reduce the rate to 20%. The increased rate will apply to earnings to be included in the corporate income tax returns to be submitted after 1 January 2018.
- Effective from 1 January 2018, a tax reduction will be applicable for compliant tax payers subject to certain conditions. Accordingly, 5% of the taxes calculated over annual corporate income tax returns will be deducted from the corporate income tax due. The reduction may not exceed TRY 1 million.
- The exemption from tax of capital gains derived by corporate taxpayers from the sale of immovable property held for at least two years will be reduced from 75% to 50%. This change applies from the publication date of the adopted bill.

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 0122**.*

»BACK

United Arab Emirates

VAT update on designated zones

UAE VAT smoothly kicked off as planned on 1 January 2018. The UAE Federal Tax Authority (FTA) through its website www.tax.gov.ae has been regularly clarifying issues and industry specific matters through teasers and awareness and guidance materials.

The VAT return format has been officially released. To ensure that businesses don't feel rushed and have sufficient time to understand and file the periodic tax returns, the FTA has postponed the first VAT filing period for many entities to either April, May or June 2018.

Designated Zones

The UAE VAT Executive Regulations [ER] also enhanced the relative attraction of certain free trade zones [commonly referred to as free zones] in the UAE. The UAE VAT ER have defined a Designated Zone [DZ] as follows:

a. Having a specific fenced geographic area and security measures and customs controls in place to monitor entry and exit of individuals and movement of goods to and from the DZ.
b. Having internal procedures regarding the method of keeping, storing and processing of goods.
c. The operator of the DZ complies with the procedures set by the FTA.

Certain benefits/issues have been created by distinguishing DZs from the regular free zones:

- A DZ that meets the conditions specified in the VAT ER shall be treated as being outside the State.
- No VAT is chargeable for transfer of goods between DZs, subject to certain conditions.
- Transfer of goods from one entity to another within the same DZ, as long as it is part of a supply chain and not meant for final consumption by the receiving entity, will not be subject to VAT.
- Regarding the provision of services, being in a DZ offers no locational advantages, as VAT is chargeable at the standard rate.

The FTA released a list of 20 areas as DZs in the first week of January 2018. The Emirate-wise list is given below :

Abu Dhabi
1. Free Trade Zone of Khalifa Port
2. Abu Dhabi Airport Free Zone [ADAFZ]
3. Khalifa Industrial Zone [KIZAD]

Dubai
4. Jebel Ali Free Zone (North-South) [JAFZ]
5. Dubai Cars and Automotive Zone (DUCAMZ)
6. Dubai Textile City
7. Free Zone Area in Al Quoz
8. Free Zone Area in Al Qusais
9. Dubai Aviation City
10. Dubai Airport Free Zone [DAFZ]

Sharjah
11. Hamriyah Free Zone [HFZ]
12. Sharjah Airport International Free Zone [SAIFZ]

Ajman
13. Ajman Free Zone [AFZ]

Umm Al Quwain
14. Umm Al Quwain Free Trade Zone in Ahmed Bin Rashid Port
15. Umm Al Quwain Free Trade Zone on Shaikh Mohammad Bin Zayed Road

Ras Al Khaimah
16. RAK Free Trade Zone [RAKFTZ]
17. RAK Maritime City Free Zone
18. RAK Airport Free Zone

Fujairah
19. Fujairah Free Zone [FFZ]
20. Fujairah Oil Industry Zone [FOIZ]

PKF Comment

The issue of the DZ list by the FTA has assisted many businesses in making crucial commercial and structural decisions depending on the nature of business. A few like real estate and automobiles are feeling the initial impact of the new tax, but it is expected that as these and other industries mature over the year and get used to the new VAT regime, VAT compliance should be a smooth ride. More than the percentage of VAT it is compliance and record keeping requirements that are currently proving a challenge in a country where other than the financial and banking sector businesses are not generally used to much scrutiny and inspection.

*It is hoped that the FTA comes out with a mechanism for issuing advance rulings in the future, which should help in creating tax predictability in areas where the law is not clear enough. For further information or advice concerning VAT in the UAE or any advice with respect to UAE taxation, please contact Ms. Sarika Dhameja at **sdhameja@pkfuae.com** or Mr. Chaitanya Kirtikar at **cgk@pkfuae.com** or call **+971 4 38 88 900**.*

»BACK

United Kingdom

Changes from the autumn budget in 2017

There were a number of measures announced by the UK government in the Autumn budget in November 2017. These varied from newly announced legislation, to refinement of existing rules to consultations over potential future rules. We have outlined some of the key internationally relevant developments below:

- **Taxing gains made by non-residents on immovable property**

  From 6 April 2019, all gains on non-resident disposals of UK property will be brought within the scope of UK tax. It is expected certain exemptions will be introduced e.g. for pension funds.

- **Royalties**
  In April 2019, the UK will extend withholding tax obligations in relation to royalty payments, and payments for certain other rights, made to low or no tax jurisdictions in connection with sales to UK customers. The rules are currently under consultation but are likely to apply regardless of where the payer is located.

- **Double taxation relief**
  On 22 November 2017 a restriction was introduced to limit the relief for foreign tax incurred by an overseas branch of a UK company, where the company has already received relief overseas for the losses of the branch against profits other than those of the branch. This ensures the company does not get tax relief twice for the same loss.

- **Anti-hybrid mismatch rules**
  The rules for the anti-hybrid mismatch were introduced 1 January 2017 in line with OECD BEPS Action 2 and are designed to address where there is a tax mismatch resulting in a double deduction or a deduction with no income recognition. Minor amendments have been made which are effective either retrospectively from 1 January 2017 or from 1 January 2018. These amendments seek to clarify how and when the rules apply.

- **Corporate interest restriction**
  The corporate interest restriction rules were enacted in 2017 in order to restrict the deduction of finance costs, broadly to 30% of EBITDA. Revisions will be put in place to address unintended consequences of the legislation. The revisions include:
  - The rules about relevant derivative contracts.
  - The calculation of group earnings before interest, tax, depreciation and amortisation (EBITDA) to align the treatment of the RDEC.
  - The definition of a group to align it with the accounting definition.
  - The administrative rules around submitting a tax return with an interest restriction.

PKF Comment

*Broadly the changes in the Autumn budget seek to address any unintended consequences of measures previously introduced or to bring legislation in line with wider international consensus on taxation. If you believe any of the above measures may impact your business or require any advice with respect to UK taxation, please contact Stephen Bryan at **stephenb@pkfcooperparry.com** or Suki Kaur at **sukik@pkfcooperparry.com** or call **+44 1332 411163**.*

»BACK

Post Spring Statement- Tax-related consultations and calls for evidence

The Chancellor kept his promise on 13 March 2018 during the Spring Statement and spoke for barely 20 minutes. He had promised not to make any tax announcements, and kept his word, although he did release a number of tax-related consultations and calls for evidence. Among these were:

Entrepreneurs' relief - at present, entitlement to the special 10% rate of CGT may be lost when an entrepreneur's company issues new shares and as a result causes their personal stake to fall below 5%. This loss of entitlement to relief is seen as a perverse consequence of the growth and success of the company and it is possible that in some cases the risk of losing ER acts as a disincentive for seeking finance that would allow the company to grow. The Government promised to review the position at the 2017 autumn Budget and have now released a consultation document.

Position paper on tax and the digital economy - this updated paper sets out the Government's view that participation and engagement of users is an important aspect of value creation for certain digital business models, and discusses a tax on the revenues that such businesses generate from the provision of digital services to the UK market.

Using online platforms to promote VAT compliance and potentially deducting VAT 'at source' from online payments – these consultations detail further moves in the Government's quest to deal with the digital economy and ensure that the correct amount of tax is being paid.

Review of the VAT registration threshold - the case in favour of a higher VAT registration threshold is that it helps to encourage growth because it keeps small businesses free from the burden of VAT for longer. While this makes it easier to start up, there is evidence that the VAT threshold may provide a brake on growth, as businesses approach it. In addition, the VAT registration threshold in most other EU member states is either much lower than that in the UK, or nil – no change is expected until 1 April 2020 though.

Other consultations issued yesterday look at the introduction of a new 'approved' fund structure within the enterprise investment scheme, to encourage investment in knowledge-intensive companies, a call for evidence on reducing the use of single-use plastics, exploring how changes to the tax system or charges could be used to reduce the amount of single-use plastics, by reducing unnecessary production, increasing reuse, and improving recycling.

Also announced were plans to extend the existing tax relief available for self-funded work-related training by employees and the self-employed, as part of the Government's focus on creating an environment for individuals to develop their skills and boost productivity in the UK, and a call for evidence to better understand the role of cash and digital payments in the new economy, in order to keep pace with changes in the ways that people pay for goods and services. This could lead to the end of 1p and 2p coins and £50 notes, but the Chancellor remains aware that many people still use cash and has undertaken to ensure that provision remains for them to do so.

PKF Comment

*The spring statement fulfilled its purpose in dealing with broader fiscal issues, leaving tax announcements to be dealt with in the autumn Budget. The new timetable with only one tax statement a year in the autumn gives the opportunity for a far more meaningful debate between accountants, Government and the professional bodies about new policy initiatives, and will lead to much better targeted legislation at the end of a longer consultation period, before the Parliamentary process begins. If you believe any of the above measures may impact your business or require any advice with respect to UK taxation, please contact Lisa Macpherson at **lisa.macpherson@pkf-francisclark.co.uk** or call **+44 1202 663627**.*

»BACK

United States

IRS provides continuity of interest safe harbour for reorganisations

At a glance

The IRS has released a Revenue Procedure (Rev. Proc. 2018-12, 2018-6 IRB) providing a safe harbour that taxpayers may use to value stock in a reorganisation for purposes of determining whether the continuity of interest (COI) requirement under Treas. Reg. §1.368-1(e) is satisfied. The safe harbour is welcome guidance for taxpayers entering into a potential reorganisation given the confusion and potential pitfalls involved when structuring a transaction to meet the COI requirement.

Background

One of the requirements for the nonrecognition of gain or loss in a reorganisation as described in §368 is that there must be a certain level of COI such that a substantial part of the value of the proprietary interests in the target corporation (Target) must be preserved following the transaction. Per Treas. Reg. §1.368-1(e)(i), 'the purpose of the [COI] requirement is to prevent transactions that resemble sales from qualifying for nonrecognition of gain or loss available to corporate reorganizations'.

A proprietary interest in Target is preserved if it is exchanged for issuing corporation (Issuing Corporation) stock. However, if the shareholders' proprietary interests in Target are acquired for cash (or other nonstock property), their proprietary interests are not considered to be preserved. To determine whether the COI requirement is satisfied, one must look at the value of Issuing Corporation's stock that Target shareholders receive vis-à-vis the total value of the consideration that Target shareholders receive.

For a number of years, determining whether the COI requirement was met in a reorganisation was based on the value of Issuing Corporation stock as of the effective date of the reorganisation (the Closing Date Rule). Using the Closing Date value as the measuring stick meant that a decrease in value of Issuing Corporation stock between the signing date of the reorganization and the Closing Date could result in the transaction failing the prescribed COI requirement. Recognising this seemingly inequitable result, in 2011 the IRS and Treasury issued regulations setting forth the so-called Signing Date Rule. Such rule says that if a binding contract to effect a reorganisation provides for fixed consideration to be exchanged for Target shareholders' proprietary interests, then such consideration is valued as of the end of the last business day before the first date there is a binding contract, rather than on the Closing Date. The Signing Date Rule therefore protects against a situation where a decrease in value of Issuing Corporation stock between the signing date and the Closing Date would run afoul of the COI requirement as seen under the Closing Date Rule.

The IRS and Treasury also issued proposed regulations in 2011 allowing taxpayers in certain situations to use an average of the trading prices of Issuing Corporation stock over a number of days, rather than using the actual trading price on the Closing Date, for purposes of determining the COI requirement.

New Safe Harbour

Eligible transactions: The new safe harbour allows taxpayers to rely on methods similar to those in the 2011 proposed regulations when determining whether COI is met, irrespective of whether the taxpayer applies the Signing Date or Closing Date Rule.

If the taxpayer uses the Signing Date Rule, a transaction is eligible for the safe harbour if:

1. The shareholders of Target receive Issuing Corporation stock and either money or other property (or both) in exchange for their Target stock in a transaction that, apart from the COI requirement, would qualify as a reorganisation described in §368(a)(1)(A), (B), or (C), or as a reorganisation described in §368(a)(1)(G) to which §354, or so much of §356 as relates to §354, applies;

2. Shares of one or more class of Issuing Corporation stock that are exchanged for the Target shareholders' stock are traded on an SEC-registered exchange (Exchange-Traded Stock);

3. All parties to the potential reorganisation, as defined in §368(b), treat the transaction in a consistent manner (i.e., as either qualifying or not qualifying as a reorganisation);

4. The transaction is effected pursuant to a binding contract that evidences the parties' agreement as to the following terms:
   a. The contract specifies:
      i. The Safe Harbor Valuation Method (defined below) and an appropriate Measuring Period that will be used to determine the value of each class of Exchange-Traded Stock to be received by the Target shareholders.
      ii. The national securities exchange and the authoritative reporting source that will be used to determine the trading prices of each class of Exchange-Traded Stock throughout the Measuring Period.
   b. Pursuant to the contract, the parties will utilize the value of each class of Exchange-Traded Stock determined under the selected Safe Harbor Valuation Method and Measuring Period in determining the number of shares of each class of Issuing Corporation stock, the amount of money, and any other property (identified by specific value or by specific description) to be exchanged for all of the Target stock, or to be exchanged for each share of Target stock; and

5. The contract terms described in paragraph 4 above are fulfilled at the Closing Date in all material respects. If the taxpayer uses the Closing Date Rule, a transaction is eligible for the safe harbour if:
   i. The requirements in paragraphs 1, 2, and 3 above are satisfied.
   ii. The transaction is effected pursuant to a contract that is binding on the parties no later than the beginning of the first trading day of

the Measuring Period selected by the parties and evidences the parties' agreement as to the matters set forth in paragraph 4 above.

iii. The contract items described in paragraph 2 immediately above are fulfilled at the Closing Date in all material respects.

Measuring Period: A Measuring Period is a number of consecutive trading days, based on the trading days of the specified exchange, used in connection with a Safe Harbour Valuation Method (described below). The Measuring Period used to determine the value of a share of each class of Exchange-Traded Stock must include at least five but not more than 35 consecutive trading days.

If the Signing Date Rule applies to the transaction, the Measuring Period must end no earlier than three trading days before the Pre-Signing Date and no later than the Pre-Signing Date, if the Pre-Signing Date is a trading day on the specified exchange. If the Pre-Signing Date is not a trading day, the Measuring Period must end no later than the last trading day before the Pre-Signing Date.

If the Closing Date Rule applies to the transaction, the Measuring Period must end no earlier than three trading days before the Closing Date and no later than the Closing Date, if the Closing Date is a trading day on the specified exchange. If the Closing Date is not a trading day, the Measuring Period must end no later than the last trading day before the Closing Date.

Valuation Methods: If a transaction is eligible for a safe harbour, taxpayers may use any of the following valuation methods:

1. Average of the Daily Volume Weighted Average Prices. For each class of Exchange-Traded Stock, taxpayers may use the average of the daily volume weighted average prices of a share of that class of Exchange-Traded Stock, on the specified exchange, as determined on each day of the Measuring Period.

2. Average of the Average High-Low Daily Prices. For each class of Exchange-Traded Stock, taxpayers may use the average of the daily average high-low trading prices of a share of that class of Exchange-Traded Stock, on the specified exchange, as determined on each day of the Measuring Period.

3. Average of the Daily Closing Prices. For each class of Exchange-Traded Stock, taxpayers may use the average of the daily closing prices of a share of that class of Exchange-Traded Stock, on the specified exchange, as determined on each day of the Measuring Period.

Ruling Requests: The Revenue Procedure states that the IRS will entertain requests for rulings and determination letters regarding transactions and legal issues to which the safe harbour does not apply and regarding the applicability of the safe harbour set forth in the Revenue Procedure.

Effective Date: The safe harbour is effective for transactions with an effective date on or after 23 January 2018.

PKF Comment

*Public companies that are entering into potential reorganisations should consider taking advantage of the new safe harbour methods. The COI issue can be extremely challenging, especially if contingent consideration or earnouts are part of the deal consideration. Meeting the COI requirement can mean the difference between a tax-free or fully taxable transaction. Therefore, if your transaction is eligible for the safe harbour, it would likely be advisable to formally comply with the requirements. Additionally, IRS has indicated its willingness to consider ruling requests to assist taxpayers in determining applicability of the safe harbour to their specific transactions. Although ruling requests can be expensive and time-consuming, the resources committed will be worth gaining certainty in connection with the federal tax treatment of a potential reorganisation. If you have any questions about your particular tax situation, please contact Michael De Prima at **mdeprima@eksh.com** or call **+1 303 740 9400**.*

»BACK

C Corporations find new life under the Tax Cuts and Jobs Act

Much has been written on the provisions of the tax legislation which was signed by President Trump on 22 December 2017. Individuals will see a different landscape to their taxes starting in 2018 not only with reduced income tax rates but larger standard deductions, expanded child credits, curtailed state and local tax deductions and limited home mortgage interest deductions just to name a few. Businesses operating as partnerships and/or S corporations can generate a new 'pass-through' deduction which may help lower the overall effective tax rate of partners and shareholders.

But what about the C corporation? Often thought of as the entity of choice used by large, publicly-held companies or businesses with an eye toward raising capital, the C corporation might see a rebirth of those choosing to set up a new business or change an existing business to this structure after analysing the generous provisions of the Tax Cuts and Jobs Act (TCJA) geared toward lowering the income tax burden of C corporations. The matter of double taxation will continue to exist for C corporations and their shareholders, albeit at a lesser bite than under prior tax law. There are also a few givebacks as presented later which will help to pay for the other generous provisions included in the legislation.

This article will discuss the major provisions of the new tax law that will impact businesses operating as C corporations.

Income tax rate reduction

The centrepiece of the TCJA is the reduction of the income tax rates applicable to C corporations. Prior to this legislation, C corps were subject to four graduated income tax rates ranging from 15% of the first USD 50,000 of taxable income to 35% of taxable income in excess of USD 10 million.

These income rates placed U.S. corporations at the high end of other developed countries in the world. The average corporate income tax rate of nations in the Organization for Economic Co-operation and Development (OECD) is 22.5%. U.S. corporations were at a competitive disadvantage and many moved their operations overseas to lower their tax burden. Once the profits were earned and received overseas there was also a 'toll' that was required to be paid when those dollars were brought back into the United States thus limiting spending and employment opportunities at home.

Under the new law, C corporations will pay income tax at a flat 21% rate effective for taxable years beginning after 31 December 2017. This should provide a significant boost to the bottom lines of these corporations. In fact, stories have already hit the press about companies awarding unplanned bonuses to all employees or making plans to significantly increase capital spending as a result of this new tax law.

Repeal of corporate Alternative Minimum Tax

The corporate alternative minimum tax (AMT) is repealed for tax years beginning after 2017. As with the AMT for individuals, this tax was meant to ensure that corporations who took advantage of certain deductions in computing their regular tax would pay some amount of tax under the AMT. AMT was computed based on the excess of a corporate taxpayer's tentative minimum tax over their regular tax liability. The tentative minimum tax is 20% of the taxpayer's alternative minimum taxable income (AMTI). An exclusion from corporate AMT was in place for small corporations (average annual gross receipts of USD 7.5 million or less for the previous three tax years.) The AMT will still exist for individuals, estates and trusts after 2017.

Corporations subject to AMT in any year were eligible to claim a "minimum tax credit" against their regular tax liability for AMT paid in previous tax years. Any unused minimum tax credit can be used to offset the regular tax liability for any year. Some of the unused minimum tax credit can be refunded in 2018 through 2021. The amount refundable is 50% of any excess minimum tax for the year over any credit allowable against regular tax for the year. The refund percentage increases to 100% in 2021.

Incentives to Increase Capital Expenditures

In a change that will most certainly spur capital spending, bonus depreciation will increase from 50% to 100% of the cost of property acquired and placed in service after 27 September 2017 and before 1 January 2023. After 2023, the bonus depreciation percentage will decline by 20% each year until it reaches zero (expires) for assets placed in service after 31 December 2027. Used property will now also qualify for bonus depreciation under the new law (prior bonus depreciation was eligible only for new property).

Section 179 expensing of new or used property will get a boost through an increase in the dollar limitation from USD 500,000 to USD 1 million. The investment limitation also rises from USD 2 million to USD 2.5 million. Both changes are effective for tax years beginning after 31 December 2017.

Net operating loss carry-backs and carryovers

The new law makes changes to the rules for net operating loss (NOL) usage. Under prior law, corporations could carry-back an NOL two years and carry-forward any remaining NOL for a period of up to 20 years. Longer carry-back periods were available for NOLs arising from casualty losses and farming businesses.

The new law eliminates the carry-back of NOLs arising in tax years ending after 2017 (other than for farm losses and certain insurance companies) while allowing such NOLs to be carried forward indefinitely. The NOL deduction for those NOLs arising in tax years beginning after 2017 is limited to the lesser of the aggregate of the NOL carry-forwards to the tax year or 80% of taxable income computed without regard to the NOL.

For fiscal year 2017/2018, special attention should be given to these new provisions. An NOL arising in this fiscal year cannot be carried back because it arose in a tax year ending after 2017. That same NOL will NOT be subject to the 80% of taxable income limitation because the NOL did not arise in a tax year ***beginning*** after 2017.

Meals and entertainment deductions reduced and eliminated

Businesses were permitted to deduct 50% of meals and entertainment expenses in prior years. The new tax law puts an end to the deduction of entertainment expenses by eliminating in full any deduction for those expenses paid or incurred after 2017. This will end any business deductions for taking your clients to night clubs, theatres, country clubs, sporting events, hunting/fishing trips and other similar types of client entertainment.

Expenses for meals incurred after 2017 (previously 50% deductible) are also not deductible with some exceptions. The 50% deduction for expenses of food, beverages and related facilities furnished on business premises primarily for employees (such as company cafeterias or executive dining rooms) will continue. Meals provided to employees on the employer's premises for the convenience of the employer (i.e., dinners provided during busy periods) will continue to be deductible at 50% and will become non-deductible after 2025 barring future action by Congress.

Limitation on deduction of business interest expense

For tax years beginning after 2017, the deduction for business interest expense will be subject to an annual computation. This limitation applies to all taxpayers regardless of how the business is organised (partnership, corporation or sole proprietorship). The amount of deductible business interest is limited in any tax year to the sum of:

- Business interest income of the taxpayer for the tax year.
- 30% of the taxpayer's adjusted taxable income for the year, including any increases in adjusted taxable income as a result of a distributive share in a partnership or S corporation, but not below zero.
- Floor plan financing interest for the tax year (applicable to financing vehicles for sale or lease to retail customers).

Adjusted taxable income equals the taxable income of the taxpayer computed without regard to any item of income, gain, deduction or loss not properly allocable to a trade or business, any business interest or business interest income, any NOL deduction, the 20% deduction for pass-through business income under new section 199A, and, for tax years beginning before 1 January 2022, the allowable deduction for depreciation, amortisation or depletion.

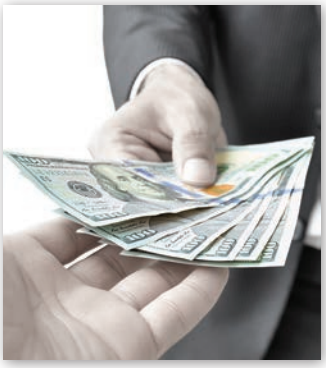
There is a small business exception to this limitation available to any tax payer whose average annual gross receipts for the three tax years ending with the prior year do not exceed USD 25 million (to be adjusted for inflation after 2018). The small business exception is applied to taxpayers who are not corporations or partnerships in the same manner as if they were a corporation or partnership.

Business interest for purposes of this limitation is the amount of interest expense paid or accrued on debt that is properly allocable to a trade or business of the taxpayer. Investment interest expense or investment interest income is not included as business interest expense or in the computation of the amount of the limitation.

Any business interest expense not deducted as a result of these rules may be carried forward indefinitely.

The limitation on the deduction for business interest is applied at the entity level for partnerships and S corporations and the deduction for business interest is taken into account in determining the non-separately stated taxable income or loss of the partnership or S corporation. The partners or shareholders who have business interest expense not from the partnership or S corporation will compute their own adjusted taxable income limitation without regard to the distributive share of income passed through to them.

New definitions expand limitation on public company excessive employee compensation



A publicly-traded corporation cannot deduct employee compensation in excess of USD 1 million paid to any 'covered employee' during the tax year.

Effective for tax years beginning after 31 December 2017:

A covered employee of a corporation:

- is the principal executive officer (PEO) of the corporation (or an individual acting in such capacity) at any time during the tax year.
- is the principal financial officer (PFO) of the corporation (or an individual acting in such capacity) at any time during the tax year.
- is among the three highest compensated officers for the tax year (other than the PEO or the PFO).
- was a covered employee of the corporation (or any predecessor) for any prior tax year beginning on or after 1 January 2017.

Compensation to a covered employee included in the cap:

- taxable wages.
- any cash and noncash benefits paid for services.
- commissions and performance-based compensation.

Compensation to a covered employee excluded from the cap:

- income from specified employee trusts, annuity plans, or pensions.
- any benefit that is reasonably anticipated to be tax free under the Code.
- income payable under a written binding contract which was in effect on 17 February 1993.
- compensation paid before a corporation became publicly held.

The reach of the limitation on the deduction for excess compensation now extends to compensation paid to the employee's estate, a beneficiary of the employee's estate or to a former spouse. Compensation paid pursuant to a written binding contract which was in effect on 2 November 2017 (and not modified in any material respect on or after such date) is not subject to the new provisions discussed herein.

PKF Comment

The significant reduction in the corporate income tax rate, along with the repeal of the corporate Alternative Minimum Tax and greatly enhanced current write-offs for capital expenditures, should for many taxpayers offset any of the impact of the revenue raisers such as the changes to deductibility of meals and entertainment, the limitation on the deduction of business interest and the broadened scope of excessive compensation limitations. Should your business be impacted by one or all of the changes discussed above, we are here to help you navigate and assist you in determining the impact of these major changes to the taxation of C corporations. If you have any questions about your particular tax situation, please contact Daniel Effron at ***deffron@pkfod.com*** *or Leo Parmegiani at* ***lparmegiani@pkfod.com*** *or call* ***+1 551 249 1732*** *or* ***+1 646 699 2848*** *respectively.*

»BACK

IRS Releases Instructions to Examiners on Five Transfer Pricing Issues

During January 2018, the Commissioner of the IRS's Large Business and International ("LB&I") Division[1] ("Commissioner") issued five instruction memoranda for examiners that will affect the IRS's approach to its transfer pricing examinations. These instructions provide examiners with guidance as they engage in the review of taxpayers' transfer pricing positions and are designed to help the IRS manage its transfer pricing examination

[1] *LB&I includes companies with greater than $10 million in assets.*

workload. Each of the memoranda are explored in detail below:

1. **Issue Selection and Scope of Analysis - Best Method Selection[2] (Revised)**
On 29 January 2018, the Commissioner issued guidance where IRS examiners need to "Obtain Treaties and Transfer Pricing Operations Transfer Pricing Review Panel approval before changing the taxpayer's selection of a Treas. Reg. §1.482 method as the best method as supported in contemporaneous transfer pricing documentation or APA submission."[3]

In the past, the IRS has examined each intercompany transaction under any of the specified methods available to it and often did it to increase profitability of the U.S. entity under examination. The new guidance will require that examiners "[start] with the taxpayer's selection of the best method, the examination team should thoroughly analyze the taxpayer's application of their selected method"[4] before determining whether a new method should be considered. In the event that an examiner believes that a different method is required, the examination team would have to develop and document their argument and gain approval before proceeding with the lengthy analysis.

2. **Issue Examination Scope - Appropriate Application of IRC §6662(e) Penalties[5]**

On 12 January 2018, the Commissioner issued guidance to examiners to apply transfer pricing penalties where appropriate. Section 6662(e) allows the IRS to penalize taxpayers that are assessed an adjustment of a magnitude that meets certain thresholds, and transfer pricing penalties can be quite onerous. The penalty regime was put in place to encourage taxpayers to maintain adequate and timely transfer pricing documentation. The Commissioner writes that the failure to apply penalties has led a situation where taxpayers have less incentive

to provide contemporaneous transfer pricing documentation. Further, the Commissioner reiterates that contemporaneous transfer pricing documentation does not provide a taxpayer penalty protection, as it must also be considered adequate and reasonable.

As such, the Commissioner states that penalties should apply in circumstances where a taxpayer relied on the unreasonable selection or application of a specified method and the net adjustment meets the penalty thresholds.

3. **Mandatory Information Document Request (IDR) in LB&I Examinations[6] (Interim)**

On 12 January 2018, the Commissioner issued a procedural change to the IDR process for LB&I examinations. According to the new instructions, the mandatory transfer pricing IDR is no longer required for all new LB&I cases. This memorandum replaces instructions introduced in 2003 that required a mandatory transfer pricing IDR be issued on "all examinations when the taxpayer filed Form 5471 or 5472, or when the taxpayer engaged in cross-border transactions."[7]

The new procedures require the mandatory transfer pricing IDR be issued in the following cases:

1. *For examinations arising under approved LB&I [transfer pricing] campaigns, examination team*

[2] *LB&I-04-0118-006, "Revised Instructions for LB&I on Transfer Pricing Issue Selection and Scope of Analysis - Best Method Selection"; https://www.irs.gov/businesses/corporations/instructions-for-lbi-on-transfer-pricing-selection-and-scope-of-analysis-best-method-selection*

[3] *Ibid.*

[4] *Ibid.*

[5] *LB&I-04-0118-003, "Instructions for Examiners on Transfer Pricing Issue Examination Scope - Appropriate Application of IRC §6662(e) Penalties"; https://www.irs.gov/businesses/corporations/instructions-for-examiners-on-transfer-pricing-issue-examination-scope-appropriate-application-of-irc-ss6662e-penalties*

[6] *LB&I-04-0118-001, "Interim Instructions on Issuance of Mandatory Transfer Pricing Information Document Request (IDR) in LB&I Examinations"; https://www.irs.gov/businesses/corporations/interim-instructions-on-issuance-of-mandatory-transfer-pricing-information-document-request-idr-in-lbi-examinations*

[7] *Ibid.*

members will follow the specific guidance for the Mandatory Transfer Pricing IDR provided for within the campaign. If no such guidance is provided, the procedures under item 2, below, will apply.[8]

2. *For examinations with initial indications of transfer pricing compliance risk (considering the volume and type of transactions), Transfer Pricing Practice (TPP) and/or Cross Border Activities (CBA) Practice Area employees will issue the Mandatory Transfer Pricing IDR if assigned to the case. If TPP or CBA resources are not assigned as a consultant or team member to the case, the Mandatory Transfer Pricing IDR will not be issued.* [9]

This memorandum is currently set to expire on 12 January 2020.

4. Issue Selection - Cost-Sharing Arrangement Stock Based Compensation[10]

On 12 January 2018, the Commissioner issued instructions to stop opening issues related to stock-based compensation ("SBC") included in cost-sharing arrangement ("CSA") intangible development costs. In this memorandum, the Commissioner is abiding by the Tax Court's ruling in Altera Corp. v. Commr, 145 T.C. 91 (2015). The IRS is appealing the Tax Court's ruling to the Ninth Circuit court but will abide by it until the appeals process if exhausted.

5. Issue Selection - Reasonably Anticipated Benefits in Cost Sharing Arrangements[11]

On 12 January 2018, the Commissioner issued instructions to stop adjustments to CSAs based on changing a taxpayer's reasonably anticipated benefits ("RAB") shares to a single RAB share in the event that a taxpayer uses multiple RAB shares. Often, when a party to a CSA makes an acquisition with valuable intangible property ("IP"), it may make the IP available to the foreign participant through a platform contribution transaction ("PCT"). The Commissioner states that, in some cases, the expected share of expected benefits from the new IP may be substantially different than the RAB share of the existing IP and, as such, require the use of a different RAB share. The Commissioner does not have instructions as of the time of publishing and, instead, directed examiners to allow the use of multiple RAB shares in cases where the positions are based on documented valid facts until a Service-wide position is finalized.[12]

PKF Comment

*The Commissioner issued these instructions under the weight of a burdensome transfer pricing caseload with increasingly limited resources. Taken together, the new instructions should reduce the number of new transfer pricing cases, increase the speed of a transfer pricing examination, and encourage taxpayers to proactively maintain adequate and reasonable transfer pricing documentation. We believe that these changes are vital for companies under a transfer pricing examination as the IRS will be more likely to resolve an examination in a timely manner, and we welcome any effort to that end. EKS&H's International Advisory Group helps companies navigate through complex tax issues in the areas of transfer pricing and international tax compliance. To learn more, please contact Kari Thiessen at **kritzthiessen@eksh.com**, or call **+1 303-846-3495**.*

»BACK

[8] Ibid.

[9] Ibid.

[10] LB&I-04-0118-005, "Instructions for Examiners on Transfer Pricing Issue Selection - Cost-Sharing Arrangement Stock Based Compensation"; https://www.irs.gov/businesses/corporations/instructions-for-examiners-on-transfer-pricing-selection-cost-sharing-arrangement-stock-based-compensation

[11] LB&I-04-0118-004, "Instructions for Examiners on Transfer Pricing Issue Selection - Reasonably Anticipated Benefits in Cost Sharing Arrangements"; https://www.irs.gov/businesses/corporations/instructions-for-examiners-on-transfer-pricing-selection-reasonably-anticipated-benefits-in-cost-sharing-arrangements

[12] Ibid.

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