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Australia

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The **Australia's Future Tax System Review** was established by the Rudd Government in 2008 to examine Australia's tax and transfer system, including state taxes, and make recommendations to position Australia to deal with the demographic, social, economic and environmental challenges of the 21st century.

The review was undertaken by a panel chaired by Dr Ken Henry, Secretary to the Treasurer, and also included other representatives from government and academia. Since inception the review has become known as "The Henry Review".

The terms of reference were broad and the objective was to provide recommendations and a final report to the Treasurer by the end of 2009. The review took a 'root and branch' approach as part of its process and the panel was supported by a working group from within treasury.

During the process they also called for public submissions guided by four broad consultation questions. Around 1,500 formal submissions were received as well as over 4,700 letters. In addition a two-day conference was held in June 2009 which provided a forum for various experts to debate leading edge tax and transfer policy.

As part of the review, the Minister for Families, Housing, Community Services and Indigenous Affairs commissioned Dr Jeff Harmer to under-

take a review of the pension system. The Pension Review investigated measures to strengthen the financial security of seniors, carers and people with a disability.

The report was handed to the Treasurer on 23rd December 2009. In a media release on that date the Treasurer said "the report will provide the foundations for a long-term plan, to make our tax and transfer system fairer, simpler and more competitive".

It is expected that the Australian Government will release its initial response to the report later this month.

Belgium

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Notional Interest Deduction (NID), although recently restricted to 3,8%, still an attractive planning tool in international taxation

Principles

The NID, valid as of accounting year 2006, allows companies subjected to Belgian corporate tax to deduct a percentage of their shareholders equity from their taxable income. The motivation in 2006 was to reduce the tax discrimination between debt-financing (interest is in principle fully deductible in Belgium) and equity-financing (dividends are not deductible).

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Example

Assets	Liabilities	
Group Financing 20.000	Share capital	20.000
	Book year 2009	Book year 2010
Profit before tax	1.000,00	1.000,00
- Notionele interest deduction (share capital x NID %)	-894,60	-760,00
Taxable	105,40	240,00
Corporate tax (33,99%)	35,83	81,58
Effective tax rate	3,58%	8,16%

Restriction 2010 and 2011

Due to the worldwide economic crisis the government has decided to restrict the maximum rate for the NID to 3,8% for accounting year 2010 and 2011. Small and medium companies are still entitled to an upgrade of 0,5% which results in a maximum rate of 4,3%.

The rate of the NID is normally calculated based on the monthly published interest rates for 10-year linear Belgian government bonds. The rate of the NID for accounting year 2009 was 4,473% and for small and medium enterprises it has been increased by 0,5% to a percentage of 4,973%. The expected rate based on the Belgian government bonds for accounting year 2010 (3,9%) was only slightly higher than the new maximum rate of 3,8%.

Conclusion

Although the maximum rate of the NID has been restricted to 3,8%, the NID still is an attractive planning tool in international taxation. For example, international groups can easily lower the effective tax rate in Belgium by raising the capital of the Belgian daughter company.

Brazil

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On December 29, 2009, the Brazilian Official Gazette brought into force Provisory Measure (PM) 478 with changes in different areas of the federal legislation. In the tax area, PM 478

changed some rules in the transfer pricing legislation, the main of which are discussed below:

1. Comparable Independent Price method

In the calculation of a standard import price according to the Comparable Independent Price (PIC) method, PM 478 clarified that taxpayers may include transactions carried out by themselves (as interested parties) or by unrelated third parties.

2. Resale Price Less Profit method

The Resale Price less Profit (PRL) method was replaced by the Sale Price less Profit (PVL) method. The latter is calculated based on the sale of assets, rights and services and, instead of the gross margins of 20% (sale) and 60% (resale) used in the PRL method, the PVL calculation will accept a single 35% gross margin for any transaction. The calculation criterion of the new method will be similar to the PRL methodology currently provided for in Normative Instruction 243/02. The acquisition cost considered in the new method will include both the costs with transportation to the establishment of the taxpayer and insurance – assuming that that burden is borne by the importer of the good – and non-recoverable taxes and customs clearance expenses.

3. General Provisions

In addition to the rules above, PM 478 established the following orientations:

The Ministry of Treasury may fix gross margins to different industries or types of economic activities destined to determine the standard price according to the transfer pricing methods of Law 9,430. This authorization has only existed under Normative Instruction 243/02.

The taxpayer will face restrictions on the choice of a method after the beginning of the federal tax audit, and the option for a transfer pricing method declared in the Income Tax Return will be conditioned to such indication prior to (i) the beginning of the federal tax audit and (ii) the presentation of documents necessary to the appropriate demonstration of the transfer pricing calculation.

4. Validity

For transfer pricing calculations on

December 31, 2009, taxpayers may calculate the PRL method in accordance with the legislation in force until that date. PM 478 provides that taxable events as of January 1, 2010 will be calculated based on the PVL method, in addition to the already existing methods.

Cyprus

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• Tax implications on interest received by Cyprus resident companies

Legislation amending the Cyprus Income Tax Law as well as the Special Contribution for Defence Tax was passed by the Parliament and published in the Official Gazette of the Republic on 6th November 2009.

The new amendments have retroactive effect as from 1st January 2009 and therefore will refer to the accounts of the year ended 31 December 2009.

Interest received by Cyprus tax resident companies is taxable according to the nature of the said interest as follows:

1) Interest derived in the ordinary course of business or closely connected to the ordinary course of business, will not be considered as interest, but as profit subject to 10% Income Tax after deducting allowable expenses.

2) Other interest will only be subject to Special Contribution for Defence at the rate of 10% on gross amount with full exemption from the scope of Income Tax. Up to the year 2008, 50% of passive interest was also subject to Income Tax.

• Double Tax Treaty between Cyprus and Czech Republic

The Double Tax Agreement between Cyprus and Czech Republic was published in the Official Gazette on November 13, 2009 and entered into force on January 1, 2010

The treaty is based on the OECD model convention, and the main provisions are:

- Dividends (Article 10) may be taxed in the source state at a rate not exceeding 5% if the shareholding participation is less than 10%.
- Interest (Article 11) is taxed only in the state of

residency of the recipient.

- Royalties (Article 12) may be taxed at source at a rate not exceeding 10%.

- Capital Gains (Article 13) deriving from the disposal of shares, whereby more than 50% of their value is immovable property, may be taxed in the country in which the property is situated.

- A tax credit is allowed (Article 21) at the level of the receiving state in respect to any taxes paid at the level of the source state.

- The provision for exchange of information (Article 24) is based on the old article of the OECD model convention and does not include paragraphs 4 and 5 added in 2005.

• Changes in the VAT rate of restaurant services and related catering services

Following the decision of the High Court of the Republic of Cyprus, the Parliament reduced the VAT rate from 8% to 5% for restaurant services and other services offered in the course of catering.

The law published in the Official Gazette on December 11, 2009 and is effective for the period from 1 May 2009 to 30 April 2010.

The supplies of alcoholic drinks, beer and wines continue to be taxed at the standard VAT rate of 15%.

• New VAT Package 2010

The European Council has approved VAT changes which came into effect from 1 January 2010 which affect also Cyprus.

The changes are in relation to the following items:

- 1) Changes to the country of taxation of services provided between businesses (B2B)
- 2) Compliance obligations for persons who supply services and goods – new VIES declaration for services
- 3) Changes in the time of supply of services for which VAT is due by the recipient – reverse charge mechanism
- 4) Procedures for refund of VAT paid in

Another Member State for business purposes

Changes to the country of taxation of services supplied to consumers (B2C)

Ireland

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Finance Bill 2010 – Key Changes

The Finance Bill 2010 has recently been passed in Ireland. This Bill brings into law the changes announced in the 2010 Budget. Some of these changes are as follows:

Tax Relief for Start Up Companies

The three year exemption from Corporation Tax will apply to profits and gains of start up companies with a tax liability of less than €40,000 per annum. Marginal relief will apply where the tax liability is between €40,000 and €60,000 per annum. Effectively this enables start up companies to make profits of up to €320,000 per year for the first three years of trading without incurring a tax liability. The relief was initially only available to companies which commenced trading in 2009. The Finance Bill 2010 has extended the relief to apply to companies which commence trading in 2010.

Carbon Tax

A carbon tax at a rate of €15 per tonne is being introduced on fossil fuels. The tax was applied to petrol and auto diesel with effect from 10th December 2009. It will also be applied to kerosene, marked gas oil, liquid petroleum gas, fuel oil and natural gas.

Capital Allowances for Energy Efficient Equipment

This tax incentive was originally introduced in the Finance Act 2008. It provides for accelerated capital allowances of 100% on expenditures incurred by companies in the year of purchase on certain types of energy efficient equipment. The Finance Bill 2010 extended the types of assets to which this provision applies. The new categories to be included in this scheme are:

- Refrigeration and cooling systems
- Electro mechanical systems
- Hospitality equipment

Domicile Levy

This levy is designed to ensure Irish individuals who are Irish citizens and Irish domiciled who would normally not have any liability to Irish tax as a result of their residence and/or ordinarily resident status to be brought into the tax net. It will affect any Individual who is an Irish citizen and Irish domiciled who have Irish located capital assets in excess of €5,000,000 and worldwide income in excess of €1,000,000 and who has a tax liability of less than €200,000. Any such individual will have to be a levy of €200,000 regardless of where they live or where they are tax resident.

Singapore

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INTERPRETING TAX TREATIES

Tax Treaty:

A tax treaty originates as a contract between two sovereign states providing for the taxation rights of the source state and the relief of taxation for the source state by the resident state.

Interpretation

A tax treaty becomes part of the statute law once it is passed by Parliament. As such, should a tax treaty be interpreted by applying the ordinary rules of statutory interpretation or should it be interpreted by applying the rules applicable to interpreting contracts or the generally accepted rules of international law ?

A.D. McNair in “The Law of Treaties”¹ viewed that treaties, where ambiguous, should generally be given a liberal construction. Jean van Houtte in “Principles of Interpretation in Internal and International Tax Law”² held the view that tax treaties should be interpreted similarly as those used in interpreting private contracts.

The courts in the United Kingdom generally lean towards the liberal rather than the literal approach. For example, Lord Denning in *Bulmer Ltd v Bollinger S.A* [1972] 2 ALL E.R. [1226], said –

“The treaty (i.e the EEC Treaty) is quite unlike any of the enactments to which we have been accustomed. The draftsmen of our statutes

have striven to express themselves with utmost exactness. They have tried to foresee all possible circumstances that may arise and to provide for them. They have sacrificed style and simplicity. They have forgone brevity. They have become long and involved. In consequence, the judges have followed suit. They interpret a statute as apply to the circumstances covered by the very words. They give them a literal interpretation

How different is this treaty. It lays down general principles. It expresses its aims and purposes. All in sentences of moderate length and commendable style. But it lacks precision....

Seeing these differences, what are English Courts to do when they are faced with a problem of interpretation? They must follow the European pattern. No longer must they examine the words in meticulous detail. No longer must they argue about the precise grammatical sense. They must look to the purpose or intent.....”

¹ The Law of Treaties (Oxford University Press, 1938). ² Principles of Interpretation in Internal & International Tax Law (International Bureau of fiscal Documentation, 1968), 42

Also, in *Stag Lines Ltd v Foscolo, Mango & Co* [1932] A.C. [328], Lord MacMillan said:

It is important to remember that the Act of 1924 was the outcome of an international Convention and that the rules in the Schedule have an international currency.

As the rules come under consideration in foreign courts, it is desirable in the interest of uniformity that their interpretation should not be not be rigidly controlled by domestic precedents of antecedent date, but rather the language of the rules should be construed on broad principles of general acceptance.”

The Canadian courts also advocated the liberal approach as can be seen in *Saunders v M.N.R* 54 D.T.C 524:

“The accepted principle is to be that a Taxing Act must be construed either against the Crown or against the person sought to be charged, with perfect strictness, so far as the intention of the

Parliament is discernible. When a tax convention is involved, however, the situation is different and the liberal interpretation is usual in the interest of the comity of nations. Tax conventions are negotiated primarily to remedy a subject’s tax position by the avoidance of double taxation rather than to make it more burdensome. This fact is indicated in the preamble to the Convention. Accordingly, it is undesirable to look beyond the four corners of the Convention and Protocol in seeking to ascertain the exact meaning of a particular phrase or word therein”

The weight of authority appears to be against the strict interpretation and the justification appears to do more with the contractual nature of a tax treaty than in its formal ratification by Parliament as legislation.

General Canons of Interpretation

In an article “The Law and Procedure of the International Court of Justice – Treaty Interpretation.”,³ G.G. Fitzmaurice highlighted three main schools of thought on treaty interpretation –

- a. intentions of the parties;
- b. ordinary meaning of the words;
- c. aims and objects

- ³ The law & Procedure of the International Court of Justice (1951): Treaty Interpretation and certain other Treaty Points (1951), 28 British Year Book of International Law 1.

He felt that in interpreting bilateral treaties, the “intentions of the parties” should be paramount since this is the judicial view derived from the principles of private contract law.

It is generally held that a tax treaty should be read as a whole, and particular phrases are not to be read in isolation or out of context. The more conservative view stresses that the natural meaning of the words is to be followed, unless the result gives an unreasonable result, the court should seek what the parties intended.

Articles 31 and 32 of the Vienna Convention on the Law of Treaties (1969)⁴ provide that-

Article 31 - General Rule of Interpretation

a. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purposes;

b. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text including its preamble and annexes:

- i. any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
- ii. any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

c. There shall be taken into account together with the context:

- i. any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
- ii. any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
- iii. any relevant rules of international law application in the relations between the parties.

d. A special meaning shall be given to a term if it is established that the parties so intended.

Article 32 - Supplementary Means of Interpretation

It may be necessary to resort to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of Article 31, or to determine the meaning when the interpretation according to Article 31:

- a. leaves the meaning ambiguous or obscure, or
- b. leads to a result which is manifestly absurd or unreasonable.

A related issue is whether the Commentary to the OECD Model Convention can be admitted as an evidence of the intent of the parties when interpreting a text which follows that of the Model Treaty. As interpretation of treaties is more akin to the interpretation of agreements than that of statutes, evidence of the Commentary should be admitted as an assistance to interpretation, especially in cases where ambiguity exists.

The ensuing question is whether the OECD Commentaries can be used to ascertain the meaning of the terms and expressions used in tax treaties ?

As the OECD Commentaries do not form part of the text of any tax treaty, the Commentaries must first qualify as “travaux préparatoires” (i.e. which designates those extrinsic materials which had a formative effect on the final draft of a treaty, and which assist in disclosing the aims and intentions of the parties) before it could be used for interpreting the treaty.

The leading decision that the OECD Commentaries qualify as “travaux préparatoires” is in *Fothergill v Monarch Airlines Ltd* [1981] AC 251 where Lord Diplock said -

“So far as domestic legislation is concerned it is well established as a principle of interpretation that, even where the words of a statute are ambiguous or obscure, the proceedings in Parliament during the course of the passage of the Bill may not be resorted to for the purpose of ascertaining what ambiguities or obscure provisions mean. The reasons why the nature of the parliamentary process at Westminster would make this an unreliable and inappropriate guide to the interpretation of a statute have been often stated by this House and need no repeating . So Hansard can never form part of the travaux préparatoires of any Act of Parliament whether it deals with purely domestic legislation or not

It is, however, otherwise with that growing body of written law in force in the United Kingdom which, although it owes its enforceability within the United Kingdom to its embodiment in or authorization by an Act of Parliament, nevertheless owes its origin and actual wording to some prior law-preparing process in which Parliament has not participated, such as the negotiation and preparation of a multilateral international convention designed to achieve uniformity of national laws in some particular field of private public law, which Her Majesty's government wants to ratify on behalf of the United Kingdom but can only do so when the provisions of the convention have been incorporated into our domestic law ...

The language of an international convention It is addressed to a much wider and more varied judicial audience than is an Act of Parliament that deals with purely domestic law. It should be interpreted, as Lord Wilberforce put it in *James Buchanan & Co Ltd v Babco Forwarding and Shipping (UK) Ltd* (1077) 3 ALL ER 1048 AT 1052 “unconstrained by technical rules of English Law, or by English legal precedent, but on broad principles of general acceptance”

..... it would seem that courts charged with the duty of interpreting legislation in all the major countries ... have recourse in greater or less degree to travaux préparatoires .. in order to resolve ambiguities or obscurities in the enacting words As Lord Wilberforce has already pointed out , international courts and tribunals do refer to travaux préparatoires as an aid to interpretation of treaties

In *Thiel v FCT*, 89 ATC 4015, Sheppard J said -

“If there be the need to resolve an ambiguity, the Court is entitled to look at the OECD Model Convention, the OECD Commentary thereonthey ought to be accorded as much if not more weight than travaux préparatoires.”

This may be so as the United Kingdom is a signatory to the Vienna Convention on the Law of Treaties and is therefore bound by Articles 31 and 32 of that Convention. However, Singapore is not a signatory to the Vienna Convention and may therefore not be so bound.

The OECD Model Convention is a basic document of reference for negotiations not only between OECD member states but also between member and non-member states, and even between non-member states.

The purpose of the OECD Commentaries is highlighted in the report prepared by the OECD Committee on Fiscal Affairs. The following extracts illustrate – Paragraph 9 “..... the existence of the Commentaries has facilitated the interpretation and the enforcement of bilateral conventions along common lines

Paragraph 25 “..... For each of the Articles in the Convention, there is a detailed

Commentary which is designed to illustrate or interpret the provisions ...”

Paragraph 26 “.... As these Commentaries have been drafted and agreed upon by the experts appointed to the Committee on Fiscal Affairs by the Governments of Member countries, they are of special importance in the development of international fiscal law. Although the Commentaries are not designed to be annexed in any manner to the conventions to be signed by Member countries, which alone constitute legally binding international instruments, they can nevertheless be of great assistance in the application of the conventions and, in particular, in the settlement of any disputes.” It would appear that where the text of a tax treaty concluded conforms with the corresponding test of the OECD Model Convention, the OECD Commentaries could be used as an interpretative guide when reading the tax treaty.

Interpretation by reference to the Law of the Forum: A tax treaty may use terms which have a special meaning in tax law or they may mean different things in the two Contracting States. The issue arises as to which of the two possible meanings is to govern the interpretation ? The OECD Model states that any term not otherwise defined in the treaty shall , unless the context otherwise requires, have the meaning which it has under the laws of the Contracting State relating to the taxes which are the subject of the Convention. This gives the court of the forum the power to interpret undefined terms in accordance with the domestic law.

Where there is an important difference between the meaning in the domestic law and that given to it in the context of the treaty, it would appear that priority be accorded to the meaning given to it in the context of the tax treaty.

It has been suggested, however, that where a problem of interpretation arises, other than one of definition, the application of the domestic law should be avoided and the rules of interpretation which apply under public international law should be followed.