Chambers Global Practice Guide 2020: Corporate Tax

Introduction

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Many of the issues that I mentioned in my introduction last year (Brexit, State aid, US tax reform and the general structure of the tax system in a digital age) are still, of course, very current.

The political scene in many countries (not least the UK) continues to be uncertain with multinationals thinking about relocating or restructuring based on what their crystal ball says about possible future legislative changes.

This excellent publication will continue to be helpful to all those facing the challenge of deciding what best to do in planning a restructuring or relocation.

There is no sign of an end to turbulence in the tax arena, it would seem. The wheels of tax reform and/or tax change (extending the scope of tax either to increase yield for its own sake or, as in the digital area, to respond to an actual or perceived need) seem destined to continue to turn for some considerable time.

In particular:

(1) The consequences of Brexit, BEPS (transfer pricing, CFC and anti-hybrid changes in particular) and US tax reform will continue to be felt. The world seems gradually to be accepting that DEMPE (where the people are located who create value out of passive assets) is both highly relevant and likely to provide the answer to the question "where are these profits really generated". In the past, the USA in particular has been too reliant on the notion that returns for managing capital and taking all risks in relation to capital reside in the place where legal ownership of that capital is held (regardless of the fact that active management of those aspects may manifestly be elsewhere). Many restructurings have been driven by the fact that that is now an increasingly questionable position – not least because the jurisdictions where human capital is located are pressing for a greater return to recognise the contribution people make. Improving CFC rules continues to be a priority for many – and substance will also be relevant there. State aid challenges (particularly in Europe) are beginning to mount as some of the worst excesses of jurisdictions anxious to attract inward investment get analysed and the anti-hybrid rules are also beginning to bite (although the imported mismatch rules denying an otherwise entirely justifiable deduction just because the jurisdiction of receipt has not taxed a payment continue to perplex). "Stateless income" is less of a problem than it used to be but it is still obviously causing some practical problems when tax authorities have to think about where income "really belongs".

(2) The last few months have seen extensive discussions taking place about Pillar One. This is not the place for a full discussion but there is no doubt that there is an increasing acceptance by the digital industry and by commentators that some form of global solution would help avoid the disaster of uncoordinated unilateral action with the very likely result of double taxation. Having a principled basis for collecting tax helps a lot because it gives you a context against which you

can test whether or not the tax is doing what it should do. Discussions about creating a "deemed PE" to which sales revenue, some expenses and, therefore, a notional in-country profit and tax charge can be attributed have been going on for many years. Anyone who argues that a company making significant sales in another state (with a corresponding customer base) has no presence or assets there should simply reflect on the commercial certainty that selling that business without giving a non-compete in relation to the markets you are exiting would almost invariably produce a lower sales price. There is, therefore, a form of customer goodwill presence from which value is being derived. At present, it is not clear where the balance of the argument lies. But for fears of unilateral action, the proposals to levy a relatively low tax on turnover (ideally with an ability to elect for deemed PE treatment if a sensible basis for determining profitability in the jurisdiction concerned) might well falter. It is even money on whether anything gets agreed here.

(3) Meanwhile, the OECD (and perhaps the EU) are quietly going along with their objective (Pillar Two) of imposing on the world a minimum tax rate for corporate activities. This has long been seen as the magic solution to profit shifting – but there is a genuine question as to whether or not it is the right answer. If a host jurisdiction (where profits are really being generated) is failing to pick that up so that stateless income is arising in a low tax jurisdiction, then that is really a failure of BEPS 1 and existing legislation in that particular country. Host countries should not be imposing burdens on lesser-developed countries just because they have not been able to do their own job properly. Consider also whether or not this proposal is fair when the profits really do belong in the low tax jurisdiction because considerable assets are held there and significant activities are being carried on there. That might well be the result of a "competitive tax policy" in the past. Such a policy will have been introduced to try to level the playing field with jurisdictions that have geographic or economic advantages or a history and infrastructure that make getting inward investment easier. A case study of Ireland, for example, might well show that competitive tax policies can bring in their train significant inward investment and a growth in local employment numbers and skill-sets. When you see that being matched by changes in the quality and focus of the local education system, you can justifiably feel sorry for countries that are being denied the opportunity to create those benefits by counterbalancing other advantages elsewhere. Pillar Two looks likely to be even more controversial than Pillar One – it is more of an admission of defeat than a real answer to the problem.

So an interesting year awaits us – and I don't expect the answers will be any easier this time next year.

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