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Global Tax Alert

The Latest on BEPS and Beyond

November 2022

EY Tax News Update: Global Edition

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Highlights

The last few weeks have been relatively quiet in terms of Pillar Two developments, with the exception of the Netherlands releasing a public consultation on its Pillar Two draft legislation. However, this period of calm activity will probably change in the following weeks when the OECD/Inclusive Framework on BEPS releases the Implementation Framework on Pillar Two by the end of this year as scheduled. This document will focus on administrative, compliance, and coordination issues in relation to Pillar Two, including the design of different safe harbors. Also, the document may include some additional interpretation guidance of the Model Rules.

Meanwhile, in the European Union (EU), tax developments continue to occur, including developments with relevance outside the EU. First, the Court of Justice of the European Union (CJEU) decided on a State aid case, somehow trying to close the EU Commission's attempt to apply its own version of the arm's-length principle. Instead, the CJEU is of the opinion that the arm's-length principle is a matter of national law.

Second, during the last ECOFIN meeting held on (date(s)), the EU Finance Ministers agreed to revise the mandate of the Code of Conduct for Business Taxation. In this update, the scope of the Code of Conduct was broadened to also include "general features of a tax system" leading to non-taxation. This means that EU Member States will now be subject to assessments under this new criteria that can be expected to trigger more changes and impose greater constraints on the policy options of Member States.

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Further, the European Parliament recently approved the Foreign Subsidies Regulation which could impact Merger & Acquisition activity and procurement processes in the EU. With this new tool, the EU will have the power to investigate financial contributions by non-EU governments which benefit companies engaging in an economic activity in the EU, including tax incentives. This new regulation should be considered in the context of growing attention for the EU trading relationship and the incentives regime included in the United States (US) *Inflation Reduction Act*.

Finally, the activity on public Country-by-Country reporting (CbCR) has been very dynamic during the past few weeks. Some EU Member States have already prepared draft legislation, generally in line with the EU Directive, to be discussed and approved under domestic law. To this end, Romania went above and beyond by implementing public CbCR legislation into domestic law with an earlier date of entry into effect. As a result, in-scope MNE groups should start thinking about their tax reporting strategy in the EU earlier than anticipated. In addition, it seems that Australia has been inspired by the EU since it has proposed to report publicly the CbCR, not only for Australian Multinational Enterprises (MNE) but also for MNEs headquartered outside Australia.

BEPS 2.0

Country developments

Netherlands launches consultation on BEPS 2.0 – Pillar Two implementation

On 24 October 2022, the Dutch Government released a draft legislative proposal as part of a public consultation process on how to implement the Pillar Two rules in its domestic legislation. The proposal is structured as a separate tax law not intended to be embedded into the existing Dutch Corporate Income Tax Code.

The draft legislative proposal is based on the compromise text of the EU Directive dated 16 June 2022 to implement the OECD Pillar Two agreement within the EU. In line with the compromise text, the Dutch Government proposes that the Income Inclusion Rule (IIR) and the Undertaxed Payment Rule (UTPR) become effective for financial reporting years starting on or after 31 December 2023 and 31 December 2024 (respectively). The Dutch Government also makes use of the possibility provided by the draft EU Directive to introduce a Qualified Domestic Minimum Top-up Tax (QDMTT) for fiscal years starting on or after 31 December 2023. Also, in line with the draft EU Directive, the draft legislation extends the scope to purely domestic groups (in addition to multinational groups) with consolidated group revenue of at least €750 million.

Interested parties and stakeholders have until 5 December 2022 to submit input to the public consultation.

See EY Global Tax Alert, *Netherlands launches consultation on BEPS 2.0 – Pillar Two implementation*, dated 24 October 2022.

Germany issues clarifications on the implementation of Pillar Two

On 17 October 2022, the Federal Government of Germany released a parliamentary document including the German Government's answers to recent parliamentary questions on the unilateral implementation of Pillar Two in Germany.

The Government responds to 24 questions of the Parliament and discusses, among others, the feasibility of unilateral implementation, scope exceptions, threshold requirements, substance-based income exclusion, safe harbors, GILTI (Global Intangible Low-Taxed Income) coexistence and interaction of the GloBE Global Anti-Base Erosion) rules with the double tax treaties. The Government also states that it contemplates the introduction of a QDMTT and EU-specific provisions such as the extension of the scope to large-scale purely domestic groups.

Finally, the Government also mentions that the German Controlled Foreign Company (CFC) regime could be modified (especially in what concerns the low-tax thresholds for CFC) after the ongoing negotiations on the concrete design of the Pillar Two global minimum tax are concluded.

BEPS and other developments

OECD

OECD/G20 Inclusive Framework holds 14th plenary meeting

On 6-7 October 2022, the Inclusive Framework held its 14th plenary meeting, including discussions on climate change and tax policy, tax transparency, digitalization of tax administration, and tax and development.

The public part of the Inclusive Framework meeting ended with concluding remarks from the OECD Secretariat-General. The Secretariat described the political agreement on the BEPS 2.0 project reached in October 2021 as the most significant development in international taxation in a very long time. However, he cautioned that the Inclusive Framework cannot relax yet, as there is still more work to be done to achieve an international tax system that is efficient, sustainable and fair. He also stressed the need to make Pillar One and Pillar Two a reality, warning that if this does not happen, there will be a resurgence of uncoordinated measures creating disputes and controversy at a difficult time in the global economy. Furthermore, he noted the need to do more to ensure that developing countries can reap the benefits of the two pillars. Finally, beyond BEPS 2.0, he called for continued focus on ensuring that all the international tax standards remain up to date and fit for purpose, noting that ongoing cooperation on tax transparency is essential.

See EY Global Tax Alert, *OECD/G20 Inclusive Framework holds 14th plenary meeting and publishes 6th annual progress report*, dated 24 October 2022.

European Union

EU Finance Ministers agree on a Code of Conduct mandate reform

On 8 November 2022, EU Finance Ministers agreed on revisions of the mandate of the Code of Conduct for Business Taxation (the Code) during the Economic and Financial Affairs (ECOFIN) Council meeting. As of 1 January 2023, the revised Code will replace the one established in 1997, expanding the scope of the Code from preferential measures (such as special regimes or exemptions from the general taxation system) to cover tax features of general application. The revision will bring greater clarity as to the scope of the Code by expanding it to cover tax features of general application which create opportunities for double non-taxation or that can lead to the double or multiple use of tax benefits for the same amount of income.

The revised Code will apply as of 1 January 2023. The expanded scope will apply from 1 January 2024 and will only cover general features introduced/amended after 1 January 2023.

See EY Global Tax Alert, *EU Finance Ministers agree on Code of Conduct mandate reform*, dated 10 November 2022.

The European Economic and Social Committee issues an opinion for the European Commission to Reconsider the DEBRA Proposal

On 27 October 2022, the European Economic and Social Committee (EESC) unanimously adopted an opinion on the draft debt-equity bias reduction allowance (DEBRA) Directive, raising concerns about its structure and content.

The EESC opinion states that limiting the deductibility of the interest on debt may impact European businesses negatively and place them at a competitive disadvantage in the global market. The interest limitation on debt is also expected to weaken Small and Medium-sized Enterprises (SMEs) and micro-enterprises financially, considering their limited access to capital markets. According to the EESC, as far as SMEs and micro-businesses are concerned, the favor of equity should be encouraged via tax allowances on equity without limiting the deductibility of interest on debt.

To this end, the EESC suggests a substantial reconsideration of the Commission proposal, including a total or at least partial exemption from the DEBRA rules for SMEs and micro-enterprises.

Country developments

Argentine Tax Authority extends suspension of mandatory disclosure regime

On 1 November 2022, the Argentine Tax Authority (AFIP) published in the *Official Gazette* General Resolution No. 5278/2022 extending the suspension of the mandatory reporting regime for an additional 60 calendar days beginning on 31 October 2022.

This suspension is the second one made this year (previous one made in September 2022) and it is motivated by several cases by courts in Argentina where a final judgment is still pending.

See EY Global Tax Alert, *Argentine Tax Authority extends suspension of mandatory disclosure regime*, dated 2 November 2022.

Australia issues 2022-23 October Federal Budget

On 25 October 2022, the Australian Federal Treasurer handed down the second 2022-23 Federal Budget, outlining the new Labor Government's priorities. Among other items, the Budget includes a Multinational tax integrity package comprising details of three measures: (i) changes to Australia's interest deduction limitation rules; (ii) a new rule denying tax deductions for certain intangible and royalty payments; and (iii) tax transparency measures.

Interest deduction limitation rules

The current interest deduction limitation (thin cap) rules provide three tests for MNEs, being (i) the safe harbor test (which broadly disallows debt deductions to the extent that debt exceeds 60% of an entity's Australian assets less non-debt liabilities); (ii) the arm's-length debt test (ALDT); and (iii) the worldwide gearing test. The Budget indicated the safe harbor test will be replaced with an earnings-based test that will apply to limit an entity's debt deductions to 30% of EBITDA (earnings before interest, taxes, depreciation and amortization). Debt deductions exceeding this threshold will be disallowed and carried forward (up to 15 years). The worldwide gearing test will be replaced with an earnings-based group ratio test allowing an entity in a group to claim debt deductions up to the level of the worldwide group's net interest expense as a share of earnings. In addition, while it will be retained as a substitute test, the ALDT will apply only to an entity's external (third-party) debt, resulting in debt deductions for related-party debt being denied under this test.

The amended rules will apply to income years commencing on or after 1 July 2023. The Budget confirms that financial entities will not be subject to the amended rules.

Denying tax deductions for certain intangible and royalty payments

The Budget provides further guidance with respect to a proposed measure to deny deductions for certain payments related to intangibles in low- or no-tax jurisdictions. The anti-avoidance measure will apply to organizations in Australia that are "significant global entities" (i.e., entities with global revenue of at least AU$1 billion (approximately US$646 million)) that make payments, directly or indirectly, to jurisdictions where they are taxed at a rate of 15% or less; or jurisdictions with a tax preferential patent box regime without sufficient economic substance. The measure is proposed to apply to payments made on or after 1 July 2023.

Tax transparency

The Budget confirms the Improved Tax Transparency measures that will require certain companies to disclose information to the public for income years beginning on or after 1 July 2023. The Improved Tax Transparency measures will require: (i) significant global entities to prepare for public release of certain tax information on a country-by-country basis and a statement on their approach to tax; (ii) listed and unlisted Australian public companies to disclose information on the number of subsidiaries and their country of tax domicile; and (iii) tenderers for Australian government contracts worth more than AU$200,000 to disclose their country of tax domicile by supplying their ultimate head entity's country of tax residence. Other details (such as format and detailed content of reporting) are yet to be released.

See EY Global Tax Alert, *Australia issues 2022-23 October Federal Budget*, dated 26 October 2022.

Colombia's modified tax reform bill approved by both houses

The economic commissions of Colombia's Senate and the House of Representatives approved the tax reform bill. Among other items, the bill includes a domestic minimum tax. This minimum tax would establish a new rule under which income taxpayers' effective tax rate should be at least 15% considering a specific formula included in the same law. However, this rule will not apply to companies incorporated under the special economic and social development zones regime during a specific number of years since these companies' corporate income tax rate would be 0% for some years.

The bill also introduces changes to the taxation of nonresident entities with a significant economic presence (SEP) in Colombia as from 1 January 2024. According to the new proposal, a nonresident entity with a SEP in Colombia would be subject to a 10% income tax withholding on its gross income, unless it decides to file an income tax return in which case the applicable rate is 3% on its gross income. A SEP exists in the case of the transfer of goods and the rendering of digital services if a number of specific criteria are met.

The modified bill is being subject to a final formal debate before it can become law.

Cyprus Tax Authority issues clarification regarding Competent Authority Agreement with United States for exchange of CbC reports

On 13 October 2022, the Cypriot Tax Department issued a clarification on the bilateral Competent Authority Agreement (CAA) for the exchange of Country-by-Country (CbC) reports between Cyprus and the US. The CAA is still under negotiations and expected to be effective for reporting fiscal years (RFYs) starting on or after 1 January 2022.

For a Cypriot constituent entity (CE) of an MNE group with a US tax resident ultimate parent entity (UPE), the secondary filing mechanism will be triggered for RFYs starting on or after 1 January 2021 but before 1 January 2022, and the Cypriot CE should still file the CbC report locally in Cyprus for its RFY ending on 31 December 2021, regardless of whether a CbC report has been or will be submitted in the US.

The Cypriot Tax Department has further noted that notifications already filed in Cyprus by Cypriot CEs for RFYs starting on or after 1 January 2021, and before 1 January 2022 must be revised if they are affected by the announcement. No penalties will be imposed if such notifications are revised before 31 December 2022.

See EY Global Tax Alert, *Cyprus Tax Authority issues clarification regarding Competent Authority Agreement with United States for exchange of CbC reports*, dated 20 October 2022.

Czech Republic releases list of non-cooperative jurisdictions for CFC purposes

On 14 October 2022, the Czech Republic issued as part of its Financial Bulletin 13/2022 an updated list of the jurisdictions to be considered as non-cooperatives for the purpose of the application of the national CFC legislation.

The Czech list has been updated to reflect the EU list of non-cooperative jurisdictions for tax purposes. As of 12 October 2022, the Czech list includes the following jurisdictions: American Samoa, Anguilla, Bahamas, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, Turks and Caicos Islands, US Virgin Islands, and Vanuatu.

Ecuadorian Tax Authority reforms definitions and tax treatment for "Tax Havens"

On 3 October 2022, the Ecuadorian Tax Authority published Administrative Resolution Nr. NAC-DGERCGC22-00000049 modifying the list of regimes and jurisdictions considered "Tax Havens."

According to the Administrative Resolution, the following jurisdictions and regimes have been removed from the list of tax havens: Svalbard – Spitsbergen, Gibraltar, Grand Duchy of Luxembourg, Isle Of Man – Mann, Channel Islands, Principality Of Liechtenstein, Republic Of Albania, Republic Of Cyprus, Republic Of Malta, Republic of San Marino, Ostrava, and Ireland.

In addition, the Tax Administration eliminated the concepts applicable to differentiate a Minor Tax Jurisdiction and Special Tax Regimes as other countries or jurisdictions not included on the Tax Haven list but still treated as it. Accordingly, the following concepts were eliminated: (i) minor tax jurisdiction; (ii) special tax regime; (iii) special tax regimes specifically in Costa Rica, Netherlands, New Zealand, and the United Kingdom.

These changes are effective as of 3 October 2022.

See EY Global Tax Alert, *Ecuadorian Tax Authority reforms definitions and tax treatment for Tax Havens, Minor Tax Jurisdictions and Special Tax Regimes*, dated 6 October 2022.

Germany updates the list of non-cooperative states and territories, adding Anguilla, Bahamas and Turks and Caicos Islands

On 11 October 2022, the Ministry of Finance of Germany issued a draft order decree law modifying the Decree on combatting tax avoidance and unfair tax competition released in June 2021 in response to the latest update (October 2022) of the EU list of non-cooperative jurisdiction for tax purposes.

The jurisdictions added to the list are Anguilla, Bahamas and Turks and Caicos Islands. Hence, the updated list includes the following jurisdictions: American Samoa, Anguilla, Bahamas, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, Turks and Caicos Islands, US Virgin Islands and Vanuatu.

Federal Ministry of Justice of Germany releases draft bill on implementing the public CbCR into national law

On 30 September 2022, the German Government published a draft bill to implement the EU Public CbCR Directive. The German implementation of the rules aligns with the EU Directive and creates an obligation for German-based MNEs or standalone corporations operating abroad with revenue exceeding for each of the last two consecutive financial years a total of €750 million as reflected in their financial statement to publish a report on income tax information for financial years starting after 21 June 2024. The publication will take place within one year from the date of the balance sheet of the relevant financial year. The reporting obligation is also triggered for non-EU based MNE groups that have a medium- or large-sized subsidiary in Germany.

Hong Kong refines Foreign-Sourced Income Exemption regime

On 28 October 2022, the Hong Kong Government published the Inland Revenue (Amendment) (Taxation on Specified Foreign-Sourced Income) Bill 2022. There were subsequent committee stage amendments proposed on 10 November 2022 in response to the EU's latest comments (collectively the Bill). The Bill introduces amendments to the tax exemption of certain foreign-sourced passive income which will be subject to additional economic substance, participation and nexus requirements.

This Bill aims to refine the Foreign-sourced Income Exemption (FSIE) regime for the exemption of specified foreign-sourced income items, (i.e., interest, dividends, income from use of intellectual properties (IP) and disposal gain on equity interest), derived by MNE group entities under specific conditions. Under the refined FSIE regime, specified foreign-sourced income will be deemed to be sourced from Hong Kong and chargeable to profits tax if: (i) the income is received in Hong Kong by an MNE entity carrying on a trade, profession or business in Hong Kong irrespective of its revenue or asset size; and (ii) the recipient entity fails to meet the economic substance requirement (for non-IP income) or participation exemption (for dividend and equity disposal gain) or fails to comply with the nexus requirement (for IP income). It will also deem a specified foreign-sourced income as not arising from the sale of capital assets even it is so arises. There are certain exclusions for income derived by a regulated financial entity and an entity benefitting from preferential tax regime or specific tax exemption regime.

The economic substance requirements for non-IP income requires the entity to have adequate employees and to incur adequate operating expense for carrying out the specific economic activities in Hong Kong, such activities include making necessary strategic decisions and managing and assuming principal risks in respect of the assets. Also, there is a reduced substance test applicable to pure equity-holding companies. Further, outsourcing of the relevant activities will be permitted provided that the taxpayer is able to demonstrate adequate monitoring of the outsourced activities and that the relevant activities are conducted in Hong Kong.

As an alternative to satisfying the economic substance requirements, an MNE entity can also rely on the new participation requirement for foreign-sourced dividend or equity disposal gain if the following conditions are met: (i) the MNE entity is a Hong Kong resident person (or has a permanent establishment in Hong Kong to which the income is attributable); and (ii) the MNE entity has continuously held not less than 5% of equity interests in the investee entity concerned for a period of not less than 12 months immediately before the income accrues. The participation requirement is subject to specific anti-abuse rules, including a switch-over rule with subject to tax condition of at least 15%.

The nexus requirement will be applied to determine the extent of the exemption for IP income; it is modelled on the nexus approach adopted by the OECD as the minimum standard under BEPS Action 5.

A number of additional provisions have been included in the Bill in order to address double taxation by extending the foreign tax credit mechanism, treatment of losses and operating expenditures regarding specified foreign-sourced income, and administrative burden.

The Bill is under review by the Bills Committee of the Legislative Council. It is expected to take effect from 1 January 2023.

Israel publishes new TP regulations following adoption of BEPS Action 13 in domestic legislation

On 22 September 2022, the Israel Tax Authority published an amendment to the Israeli Transfer Pricing (TP) regulations following the adoption of the BEPS Action 13 in domestic legislation.

The key changes include: (i) the shortening of the filing deadline of a TP report from 60 to 30 days from demand; (ii) the introduction of a requirement for Israeli taxpayers members of an MNE Group with revenue exceeding ILS150m (approx. US$42.5m) in the preceding year to prepare and file (within 30 days from demand as specified above) a Master File; (iii) enhanced disclosure requirements regarding intercompany transactions as part of the annual tax return; and (iv) introduction of a CbC report filing obligation to apply to ultimate parent entities of MNE groups meeting a consolidated revenue threshold of ILS3.4 billion (approximately US$965 million) within 12 months following the end of the reporting fiscal year.

The new regulations will generally apply to fiscal year 2022.

See EY Global Tax Alert, *Israel publishes new TP regulations following adoption of BEPS Action 13 principles in domestic legislation*, dated 21 October 2022.

Luxembourg Draft Budget Law 2023 clarifies Reverse Hybrid Entity Rule

On 12 October 2022, the Minister of Finance of Luxembourg submitted the 2023 Draft Budget Law, including clarifications on the application of the Reverse Hybrid Entity Rule, to the Parliament. The suggested amendment extends the wording of the reverse hybrid rule provision stating that the Reverse Hybrid Entity Rule will not apply if the nonresident investor in a reverse hybrid entity benefits from a subjective tax exemption in its jurisdiction of residence.

The intention of the suggested amendment is to remove this uncertainty by completing the Reverse Hybrid Entity Rule with a wording that the non-taxation of the net income of the associated enterprises must result from a difference of classification of the Luxembourg tax transparent entity or arrangement.

If adopted, this clarification will take effect from the tax year 2022, when the Reverse Hybrid Entity Rule is applied for the first time.

See EY Global Tax Alert, *Luxembourg Draft Budget Law 2023 clarifies Reverse Hybrid Entity Rule*, dated 17 October 2022.

Mexico ratifies MLI | Timeline for entry into force will be triggered once instrument of ratification is deposited in the OECD

On 12 October 2022, the Mexican Senate approved the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS* (MLI). In June 2017, Mexico submitted its MLI positions, listing its reservations and notifications as well as the 61 tax treaties it wishes to be covered by the MLI as CTAs. A definitive list of reservations and notifications will also need to be provided upon depositing the instrument of ratification.

Following Senate approval, the MLI has now been sent to the President for signature and publication in the Federal *Official Gazette* and subsequent deposit with the OECD.

See EY Global Tax Alert, *Mexico ratifies MLI | Timeline for entry into force will be triggered once instrument of ratification is deposited in the OECD*, dated 14 October 2022.

Netherlands releases updated Decree on national anti-hybrid mismatch legislation

On 3 November 2022, the Dutch State Secretary of Finance published an updated Decree with (new) guidance on the application of the Dutch anti-hybrid mismatch legislation as mandated by the EU Anti-Tax Avoidance Directive II (ATAD II).

Newly provided guidance addresses situations whereby a Dutch taxpayer is treated as a disregarded entity (for US federal income tax purposes) and performs activities for its parent entity (a US corporation) for which it is remunerated on a cost-plus basis with respect to its (third-party) operational expenses.

As the Dutch taxpayer is disregarded (i.e., transparent) for US federal income tax purposes, its expenses are typically (also) deductible at the level of the US parent. This scenario creates a double deduction covered by the ATAD II rules. Therefore, the (third party operational) expenses are, in principle, non-deductible at the level of the Dutch taxpayer, unless offset against dual inclusion income, i.e., income included in the tax base of both the (Dutch) payer and (its) investor jurisdictions.

The updated Decree confirms (in line with the outcome of earlier consultation with the European Commission) that in this case the operational income reported in the US federal income tax return of the US parent qualifies as dual inclusion income under the ATAD II rules to the extent it relates to the cost-plus remuneration reported at the level of the Dutch taxpayer. In such case, the relevant (double deducted third party operational) expenses incurred by the Dutch taxpayer are not disallowed on the basis of the Dutch ATAD II double deduction rule.

See EY Global Tax Alert, *Netherlands issues updated ATAD 2 Decree that will benefit certain cost-plus situations for US corporations with disregarded Dutch taxpayers*, dated 3 November 2022.

Romania implements EU CbCR Directive with early application as of 1 January 2023

On 7 September 2022, the Romanian Government published in the *Official Gazette* legislation to implement the EU Public CbCR Directive. Romania has elected for an earlier adoption date as the rules will apply for financial years starting on or after 1 January 2023.

The legislation requires both Romanian-based MNEs and non-EU-based MNEs doing business in Romania through a branch or subsidiary with total consolidated revenue of more than LEI3,700 million (equivalent to approx. €747 million) in each of the last two consecutive financial years to disclose publicly the income taxes paid and other tax-related information such as a breakdown of profits, revenues and employees per country.

In addition, according to the current wording of the Romanian legislation, MNE groups that have a medium-sized or large subsidiary in Romania are subject to public CbCR in Romania, irrespective whether these are non-EU- or EU-headquartered groups. This represents an expansion of the scope with respect to the Directive.

Romania also chose to allow in-scope groups to defer the disclosure of commercially sensitive information in certain conditions for up to five years. Furthermore, Romania opted to exempt companies from the requirement to publish the CbC reports on their website, provided that they are made available free of charge on the website of the relevant Chamber of Commerce.

See EY Global Tax Alert, *Romania implements EU Country-by-Country Reporting Directive with early application as of 1 January 2023*, dated 3 November 2022.

Inland Revenue Authority of Singapore releases fourth edition e-Tax Guide on CbCR

On 31 October 2022, the Inland Revenue Authority of Singapore (IRAS) published the fourth edition e-Tax Guide on CbCR. The main amendments include a requirement for an ultimate parent entity of a Singapore MNE group to notify IRAS of its obligation to file a CbC Report from financial year beginning on or after 1 January 2022, within three months from the end of the relevant financial year. Also, there is a requirement to prepare CbC reports in CbCR XML Schema format and submit the CbC reports based on instructions on the IRAS CbC report webpage. The updated e-Tax Guide also includes a new section on penalties for non-compliance in case of: (i) failure to provide a notification of filing obligation; (ii) non-filing, late filing or incorrect filing of a CbC report; (iii) failure to retain all documents or information used to prepare a CbC Report; and (v) submitting false or misleading information.

Slovenian Government submits Bill implementing DAC7 Directive into national law to the Parliament

On 27 September 2022, the Slovenian Government submitted the Bill transposing the rules revising the EU Directive on Administrative Cooperation in the Field of Taxation to extend its scope to reporting obligations of digital platform operators (DAC7) to the Parliament via amendments of the Slovenian Tax Procedure Law.

Under DAC7, digital platforms are obliged to collect, verify and report information on sellers who use their platform to sell defined goods or to provide services. DAC7 also aims to enforce the exchange of information and cooperation between the EU Member States' tax authorities, for example, through a joint audit framework or data breach procedures.

Once the Parliament adopts the amendments, the Bill will apply as of the 15th day after being published in the *Official Gazette*.

Spanish tax authorities deny interest deductions on a transaction declared as abusive

On 1 September 2022, in the context of a tax audit procedure, the Spanish tax authorities (STA) challenged, in a binding report, the tax deductibility of financial expenses derived from debt used to fund a share premium distribution.

The challenge was based on the application of the General Anti-Avoidance Rule (GAAR), on the grounds that by using several "intermediary" entities and carrying out a series of consecutive intra-group transactions, the taxpayer achieved an anticipated distribution of future profits and generated financial expenses which reduced the tax burden in Spain.

According to Spanish law, when the GAAR could be applicable, the STA should consult the Advisory Committee composed of members of the Tax Agency and the General Directorate of Taxation.

The GAAR Advisory Committee found that the incorporation of the intermediary entities in the chain and the different transactions carried out were unnatural and improper for the intended transaction and concluded that the true purpose of the actual steps taken was to anticipate a future profit (unrealized profit) for the Spanish operating company's shareholders by generating a financial expense at the level of the Spanish tax unity, thereby reducing the tax burden in Spain. In the absence of the generation of the share premium and the debt borrowed by the Spanish holding company, the Spanish operating company would not have been able to carry out the corresponding profit distribution.

See EY Global Tax Alert, *Spanish tax authorities deny interest deductions on debt to fund a share premium distribution, overall transaction declared as abusive in binding Report*, dated 1 November 2022.

Spain implements reverse hybrid mismatches rule under EU ATAD 2

On 19 October 2022, the Royal-Decree Law (RDL) implementing the reverse hybrid rules outlined in the EU Anti-Tax Avoidance Directive (Council Directive 2017/952 of 29 May 2017, the so-called "ATAD 2") into the Spanish legislation, was published in the Spanish *Official Gazette*.

For a reverse hybrid mismatch to exist and the rules to apply, an entity incorporated or established in Spain should be treated as fiscally transparent in Spain, while one or more associated non-Spanish entities should hold or participate directly or indirectly 50% or more of the share capital, profits or voting rights in the Spanish entity, and be resident in one or more jurisdictions that view the Spanish entity as a taxable person.

Where the conditions above are met, the reverse hybrid entity will become a Spanish Corporate Income Tax taxpayer for specific income items. The remaining items of income obtained by the reverse hybrid entity will be allocated to its owners and will be taxed in line with the Spanish Personal Income Tax Law.

In addition, a carve-out is introduced for Collective Investment Vehicles.

The Spanish Congress must ratify the RDL within 30 days following its publication, and the rules would be effective as of 1 January 2022.

See EY Global Tax Alert, *Spain implements reverse hybrid mismatches rule under EU ATAD 2*, dated 3 November 2022.

Spanish Supreme Court rules on dynamic interpretation of tax treaties and characterizes the transfer of client data as royalty

Recently, the Spanish Supreme Court decided case 840/2022 on the dynamic interpretation of tax treaties and characterization of payments derived from transfer of data. In this case, a Spanish and German entity (both related parties) entered into an agreement in 2009 whereby the German company "transferred" its customer data and operational data (financial information and relevant data to provide distribution services in Portugal) to the Spanish company. The transaction was deemed a transfer, giving rise to a capital gain, which it is not subject to Spanish withholding taxes.

During a tax audit, the Spanish Tax Authorities challenged the tax treatment of payments made under this agreement, finding that the transaction did not trigger a capital gain but rather fell within the definition of royalty, which it is subject to a withholding tax in Spain. The Spanish tax authorities and lower judicial courts confirmed the Spanish tax audit's position, and the case was appealed to the Spanish Supreme Court.

According to the Supreme Court, the remuneration agreed upon in consideration for the "transfer" of customer and "operational" data should be characterized as royalty within the meaning of article 12 of the Germany - Spain tax treaty. The Supreme Court considers that the object of the

agreement does not refer to a mere list of client data that may be extracted from a public database but rather the assignment of operational data referred from commercial experience (i.e., know-how). This notion is included in the royalty definition under Spanish domestic tax law and the Germany-Spain tax treaty. As a result, the Spanish domestic provisions related to royalties (including withholding taxes) are applicable, subject to the reduced tax treaty rates set forth in the tax treaty.

The Judgment, in line with previous case law, adopts a restrictive position regarding the recognition of transactions that determine a "full transfer" of certain rights over intangibles such as know-how or the transfer of technology, for the purposes of applying the tax treaties.

The Supreme Court holds the view that the fact that the tax authorities use the Commentaries to article 12 (royalties) of the 2008 OECD Model Tax Convention to interpret the Germany-Spain tax treaty signed in 1966 does not involve a prohibited "dynamic interpretation" of the tax treaty, since such Commentaries existed before the transaction. This conclusion lies on the fact that the tax treaty definition of royalties did include payments in consideration for know-how and that none of the parties have contended, verified or questioned that the evolution of the Commentaries entails a substantial or material change.

See EY Global Tax Alert, *Spanish Supreme Court rules on dynamic interpretation of tax treaties and "substance-over-form" characterization of cross-border transfer of client and operational data*, dated 11 October 2022.

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