PE under the tax treaty. As no PE of US Co was found to exist, no profits could be taxed in India and no income of I Co could be attributed to or taxed in the hands of US Co.

Globalisation has led many multinational enterprises to outsource business process and information technology services to affiliates in India. This decision provides guidance on issues as well as factors relevant for making a determination of PE in India in such business arrangements.

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Italy

Italy extends International Standard Ruling procedure


Giuliano Foglia and Giovanni d'Ayala Valva, Tremonti Vitali Romagnoli Piccardi e Associati

With the conversion into law of the *Destinazione Italia* Decree (Law Decree December 23 2013, No. 145 converted into Law February 21 2014, No. 9) certain significant and welcomed amendments to the Italian International Standard Ruling procedure become definitive.

The Italian International Standard Ruling was introduced in Italy in 2005 with the aim of preventing and minimising tax litigations with the Italian tax authority and to reduce the risk of international double taxation: it is, in fact, addressed to companies carrying out international activities that intend to reach an advance agreement with the Italian tax administration regarding the taxation of income derived from certain cross-border transactions.

In particular, the matters covered by the Italian International Standard Ruling were originally: (i) the transfer pricing methodology applicable to transactions carried on with related parties in the form of unilateral, bilateral and multilateral APAs; (ii) the tax treatment of dividends, interest and royalties; (iii) the attribution of profits or losses to permanent establishment of non-resident companies and to foreign permanent establishment of resident companies.

In this situation, and as part of a package of provisions aimed at encouraging and attracting foreign investment in Italy through a more certain legal environment, the Decree has now extended the scope of application of the above mentioned procedure.

More specifically, it is now introduced the possibility for a non-resident taxpayer to address in advance whether its presence in Italy amounts to a permanent establishment or not. In other words, non-resident entities operating in Italy might now request a ruling from the tax authority on whether their activities create a permanent establishment in Italy under Italian domestic law or tax treaty provisions.

Furthermore, the Italian International Standard Ruling becomes more attractive for foreign investors as the Decree extends also the legal validity of the ruling to five fiscal years (while before the amendment the agreement was binding for a period of three years including the year in which the agreement was reached). As a result, it is now provided that the agreement is binding on both the taxpayer and the tax administration for the tax year in which it is reached and for the following four years, provided that the relevant facts and circumstances do not change.

In addition, the Decree centralised into a single office of the Italian tax authority the management of the Italian International Standard Ruling applications filed by the taxpayers.

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Luxembourg

VAT Update


Christophe Plainchamp and Nicolas Devillers, ATOZ – Taxand

VAT rates increase

As expected, all Luxembourg VAT rates will be increased by two percentage points in the coming months with the exception of the super-reduced rate which will remain at 3%. In any case, the new Luxembourg standard VAT rate (17%) will remain the lowest within the EU. Even if initially planned for January 1 2015, the implementation date has not been yet confirmed: Finance Minister Gramegna mentioned recently that the increase would either take place this summer (most likely) or in January 2015.

2015 VAT changes for electronic, telecommunication and broadcasting services

By the end of 2013, the Council of the EU published its Implementing Regulation (1042/2013) dealing notably with new rules applicable to the place of supply of telecommunication services, television and radio broadcasting services and electronically supplied services (ICT services) supplied by EU businesses to EU private customers.

Until now, when supplied by an EU service provider, the place of taxation of ICT services was the place of establishment of the service provider. From January 1 2015, the place of taxation will become the member state where the customer is established, his permanent address or his habitual residence. In Luxembourg, the Bill No. 6642 implementing these rules is in the course of approval and should be adopted in the coming months.

Businesses concerned are European providers of telecommunication services, television and radio broadcasting services and electronically supplied services.

Businesses affected by these new rules will be required to charge the respective VAT rate in effect in the member state where their customers are established. As the VAT rates vary from 3% to 27% within the EU, IT systems will have to be adapted to apply the correct rate based on the country of establishment of the customer. Invoices will also have to comply with local requirements.

Fortunately, businesses will not suffer an important administrative burden in all EU member states (for example VAT registration, VAT returns, VAT payments) as a specific scheme, the mini one-stop shop, has been designed to allow ICT service providers to file one single VAT return per quarter, including the VAT due in each respective member state.

These changes raise however issues, such as:

- Defining accurately the place of establishment of the customer and the related VAT liability;
- The pricing effect on the final customer;
- Privacy issues about data collected on customer and the storage of such information; and
- Invoicing requirements.

More member states to apply reduced VAT rates to e-books

In 2013, the European Commission referred France and Luxembourg to the European Court of Justice (ECJ) for applying a reduced VAT rate to e-books.

The battle may however not be lost as another case implicating Finland is pending at the ECJ to clarify the difference in treatment regarding the VAT rates applicable on books, depending on whether they have been supplied under an electronic-format or a hard-format. Besides, in a recent press release, the German Ministry of Culture has notified his intention to also apply a

reduced rate on e-books. We will update you on future developments on this topic.

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FYR Macedonia

Reinstatement of withholding tax on dividends distributed to resident companies

Elena Kostovska, Eurofast Global

Effective from July 2010 and up until February 2014, the tax treatment of dividends in FYR Macedonia depended on the residency of the dividend-receiving entity/individual. This was because of the fact that in July 2010, the government had introduced an anti-crisis taxation exemption principle, whereby all forms of profit distribution made to resident legal entities were exempt from corporate income tax, effectively eliminating the tax burden on the transfer of profits between resident companies. Profit distributions to non-resident entities and individuals were taxed with a 10% withholding tax rate.

However, on January 21 2014 the FYR Macedonian Parliament adopted the proposed amendments to the Law on Profit Tax (published in the Official Gazette no.13 on January 23 2014 and effective as of January 31 2014) which reinstate the final withholding tax of 10% on dividends paid to resident companies. The law effectively levels the field for taxation of all dividend distributions, regardless of the tax residency of the receiving entity or individual.

FYR Macedonian entities paying out dividends are obliged to pay a withholding tax on the dividends distributed to entities or personal income tax on dividends paid to individuals. The same obligation is applied to non-resident entities with a permanent establishment in FYR Macedonia who choose to distribute dividends to other entities.

The tax on dividends is withheld concurrently with the dividend payment (be it monetary or in shares), at a flat rate of 10% regardless of the year for which dividends are distributed. It should be noted that for companies distributing dividends to non-residents, the rate may be reduced under the conditions of a valid double tax treaty, provided that the resident entity distributing dividends explicitly requests a written approval from the Revenue Office which would grant it the right to use the lower or nil tax rate defined in the treaty. If this procedure is not followed, tax will be withheld at the legally prescribed rate, which is 10% and a tax refund would be subsequently requested.

Failure to withhold tax for the payment of dividends is penalised with a fine of €1,500 – €2,500 ($2,000 – $3,500) to the company and a penalty amounting to €500 – €1,000 to the general manager (physical person) of the company.

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Mexico

New mining and environmental royalties

David Cuellar and Caroline Paris, PwC

In the July 2013 issue, we discussed a new 5% mining tax to be introduced to the Mexican tax legislation. This was following a proposal by the Institutional Revolutionary Party (PRI for its initials in Spanish) in March 2013, to establish a tax for the extraction of minerals in favour of the states and municipalities where mining activities are performed. The proposal was approved by the House of Representatives and passed to the Senate for approval.

However, in September 2013, while its analysis and approval by the Senate was still pending, the Federal Government decided to include this proposed tax in the tax reform package for 2014, with several important modifications. The tax reform proposal was approved by the Mexican Congress on October 31 2013 and is applicable as of January 1 2014.

There are two new taxes to consider, which are adding a significant tax burden to multinational mining companies with Mexican projects.

The initially proposed and partly approved 5% royalty is replaced by a 7.5% tax applicable on net revenues arising from the sales related to the mining activities, calculated not including depreciation (except those involved in mining prospecting and exploration), interest and the annual inflation adjustment. This royalty payment is deductible for tax purposes, resulting in an effective tax rate of 5.25%.

In addition, the creation of an annual extraordinary fee aimed to finance the environmental erosion impact of the gold, silver and platinum mining industries was also approved. Hence, a new tax, at a rate of 0.5%, is now applicable to gross income arising from the sales of gold, silver, and platinum. This environmental fee is also deductible for tax purposes so that the effective rate is 0.35%.

It is worth mentioning that the 2014 tax reform maintained the additional fees applicable to idle mining properties. An additional 50% of the highest existing concession fee (based on hectares) will be payable by concession holders not conducting demonstrable exploration and exploitation activities for two consecutive years within the first 11 years of obtaining the mining concession. The fee will reach 100% of the existing concession fee if no exploration or exploitation work is done for two consecutive years after the eleventh year of obtaining the concession title.

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Montenegro

Montenegro regulates taxation of hydrocarbon production activities

Jelena Zivkovic, Eurofast Global

On the February 1 session of the Montenegrin government, the goverment adopted the Draft Law on Taxation of Hydrocarbons, whereby tax policies on profit gained from extracting oil and gas, construction of facilities and related equipment as well as delivery and transport of oil and gas have been defined.

The proposed law, when ratified by the Parliament, will create a special regime for corporate income tax applicable to companies dealing with extracting oil and gas. Per the new law, the corporate income tax rate will be 59%.

The proposed law introduces liability of payment of corporate income tax on profits gained from upstream operation related to hydrocarbons. The law will be applicable to upstream operations undertaken on the Montenegrin Sea and in international waters where Montenegro has the right of exploitation in line with international agreements. Also, the law will be applicable to the transport of hydrocarbons.