International Taxation: Opportunities and Risks

Offshore transfers of assets – Update on analysis

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Introduction

- Taxation of indirect transfers important in TA missions
- Is not covered in G20/OECD BEPS project
- G20 Development Working Group has asked IMF OECD (and WB, UN) to report indirect transfers
- This presentation:
  - Illustrates taxation of direct vs. indirect transfers of assets
    - Domestic only transactions
    - Cross-border transactions, with no DDTs
    - Cross-border transactions, with DDTs based on UN or OECD Model Conventions
  - What should a Source Country do if it wants to tax indirect transfers?

Example Facts

- Each Company is a shell that either owns an Asset, or another Company.
- The only value is the Asset. In the first examples, the Asset is a Film Library
    - Physical films
    - Right to exhibit those films
    - No Immovable Property
- Tax basis of Asset = 10
- Sale price of Asset = 50
- Capital gain is 40 = (50 – 10)
- Tax Rate = 20%
- Capital Gains (CG) Tax is 8 = 20% * (50 – 10)

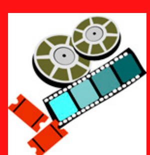
Direct Sale of Asset (Domestic Transfer)

Before Sale

Co. A Sells Asset to Co. B

After Sale

Company A



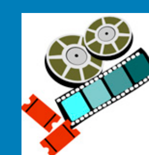
Company B

Cash: 50

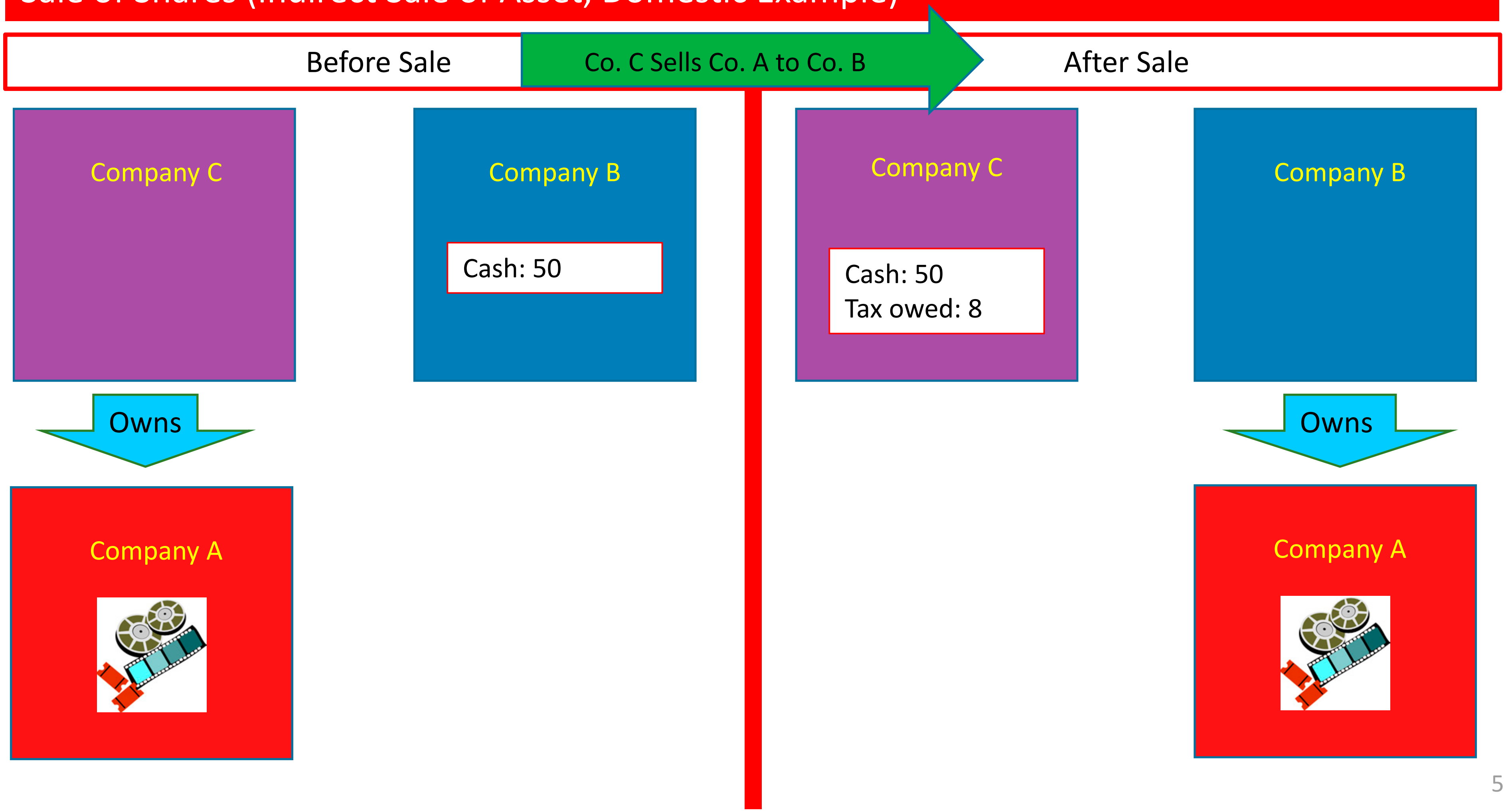
Company A

Cash: 50
Tax owed: 8

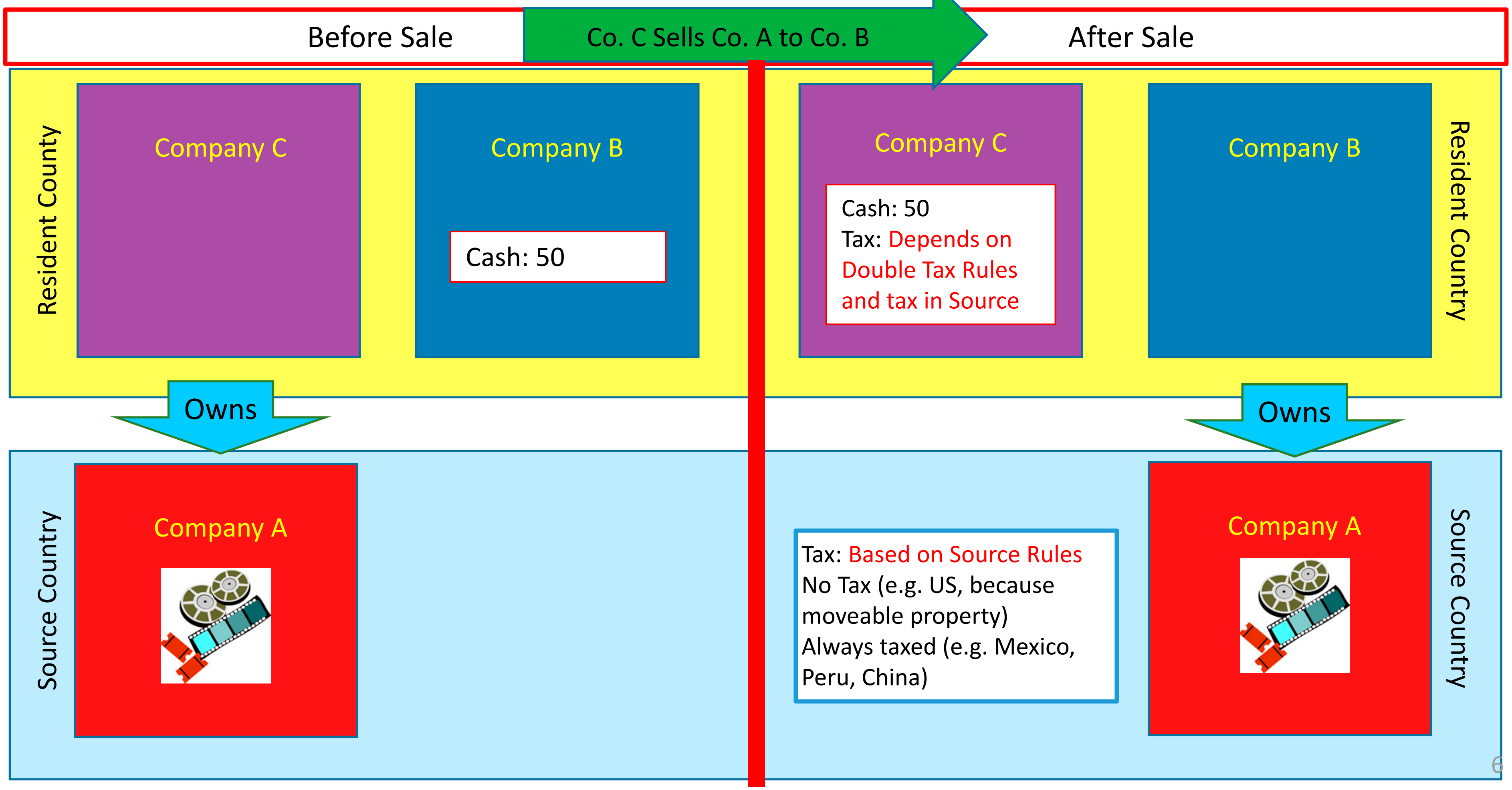
Company B



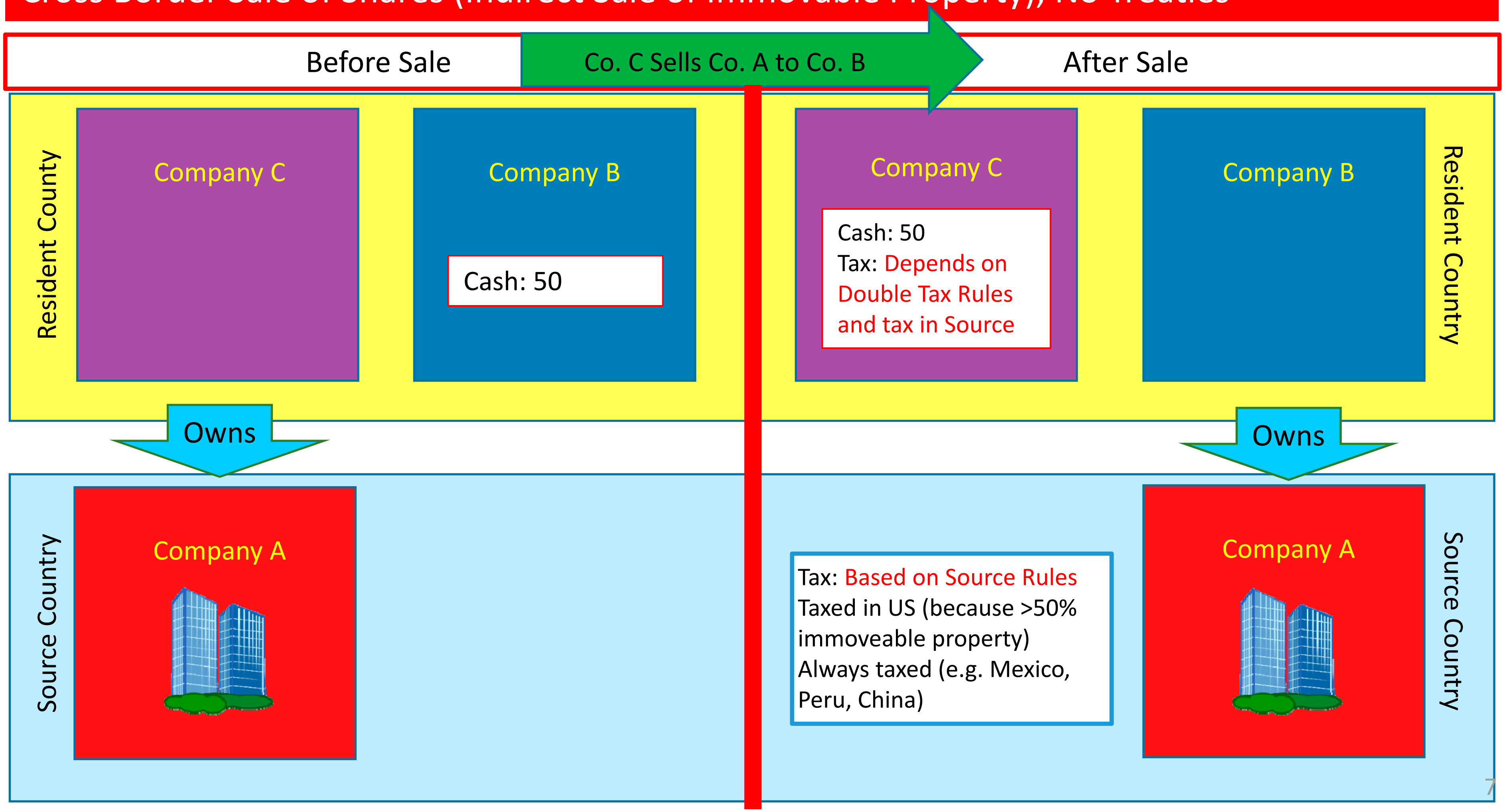
Sale of Shares (Indirect Sale of Asset, Domestic Example)



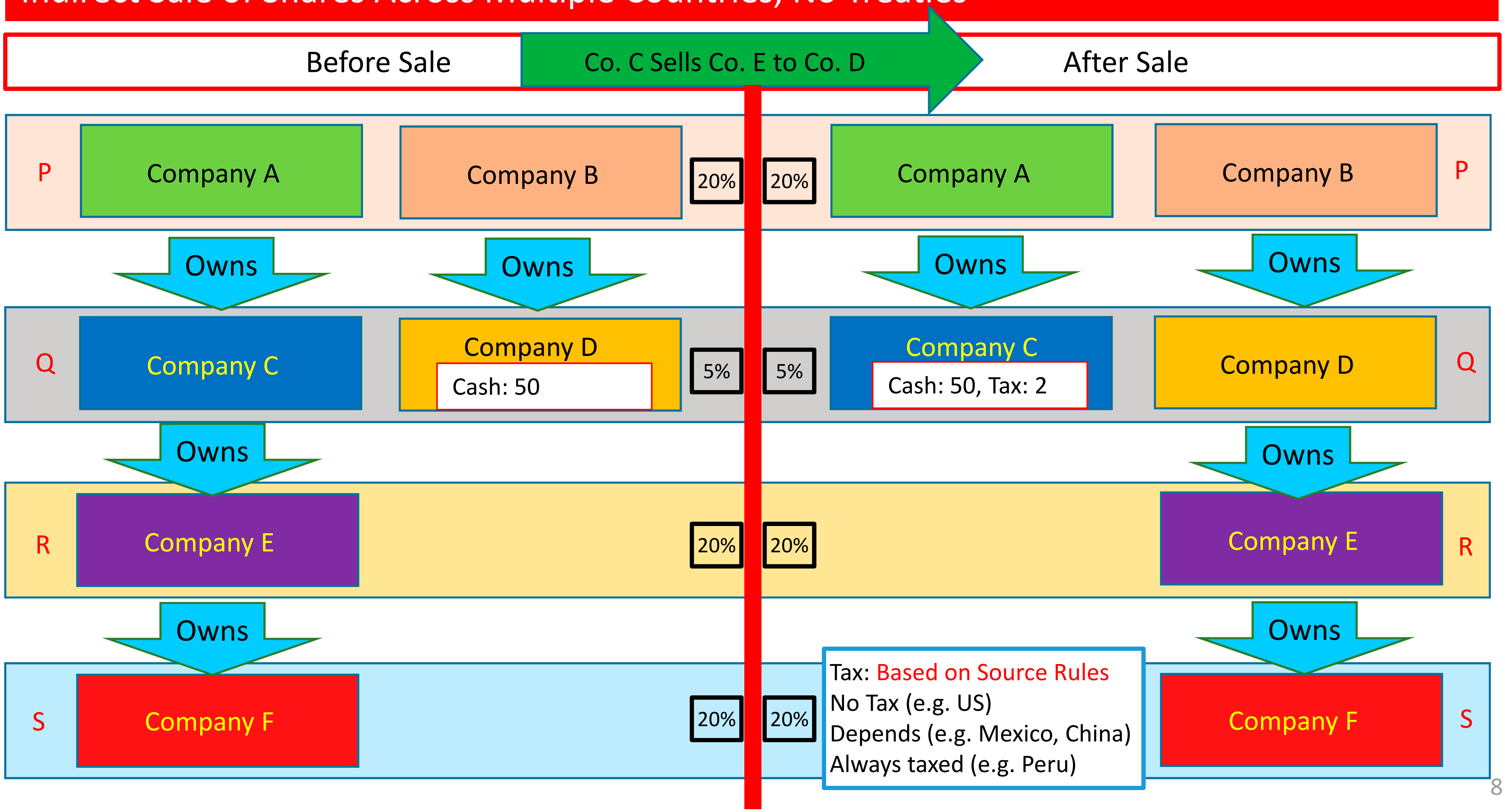
Cross Border Sale of Shares (Indirect Sale of Asset), No Treaties



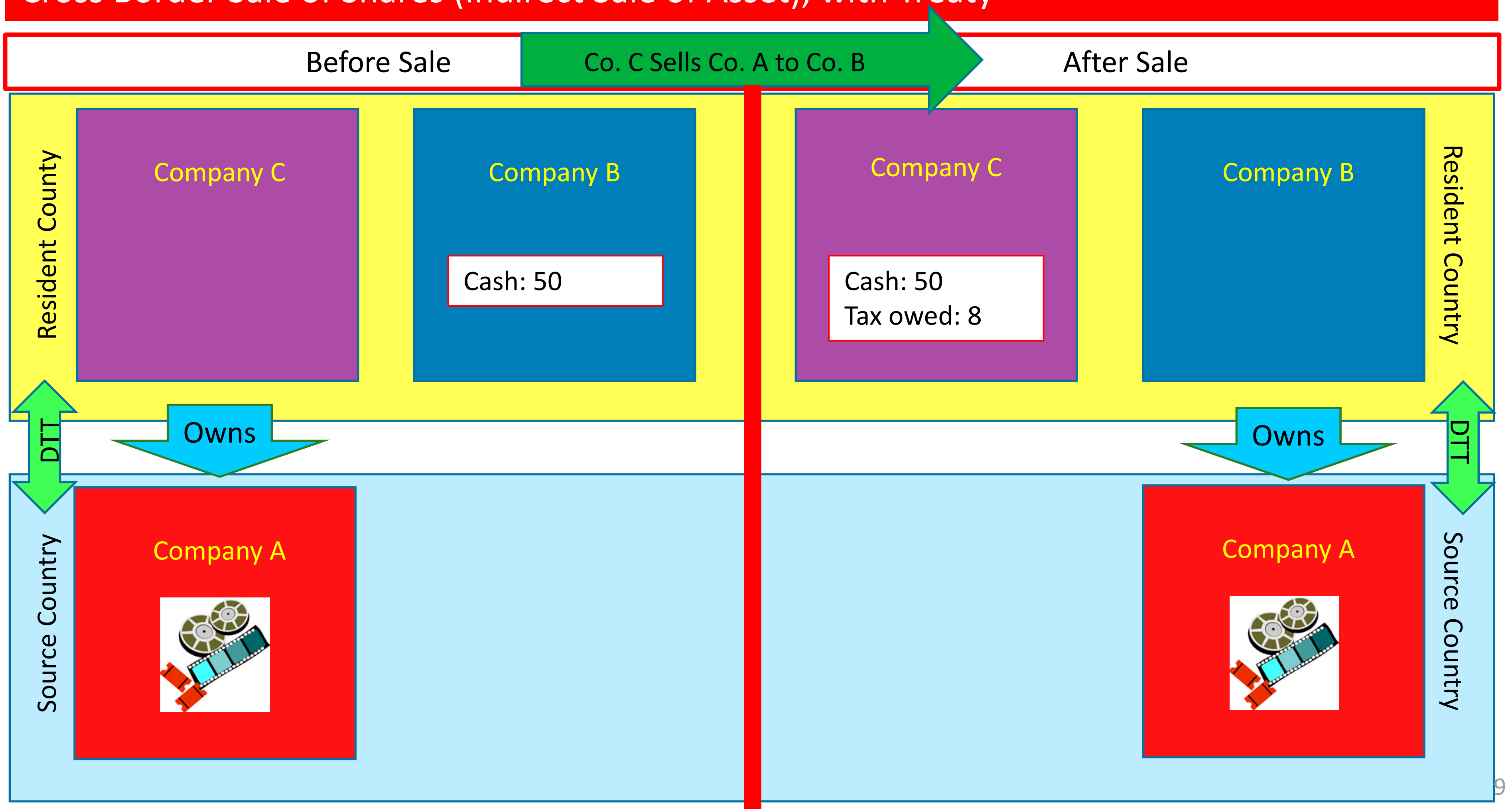
Cross Border Sale of Shares (Indirect Sale of Immovable Property), No Treaties

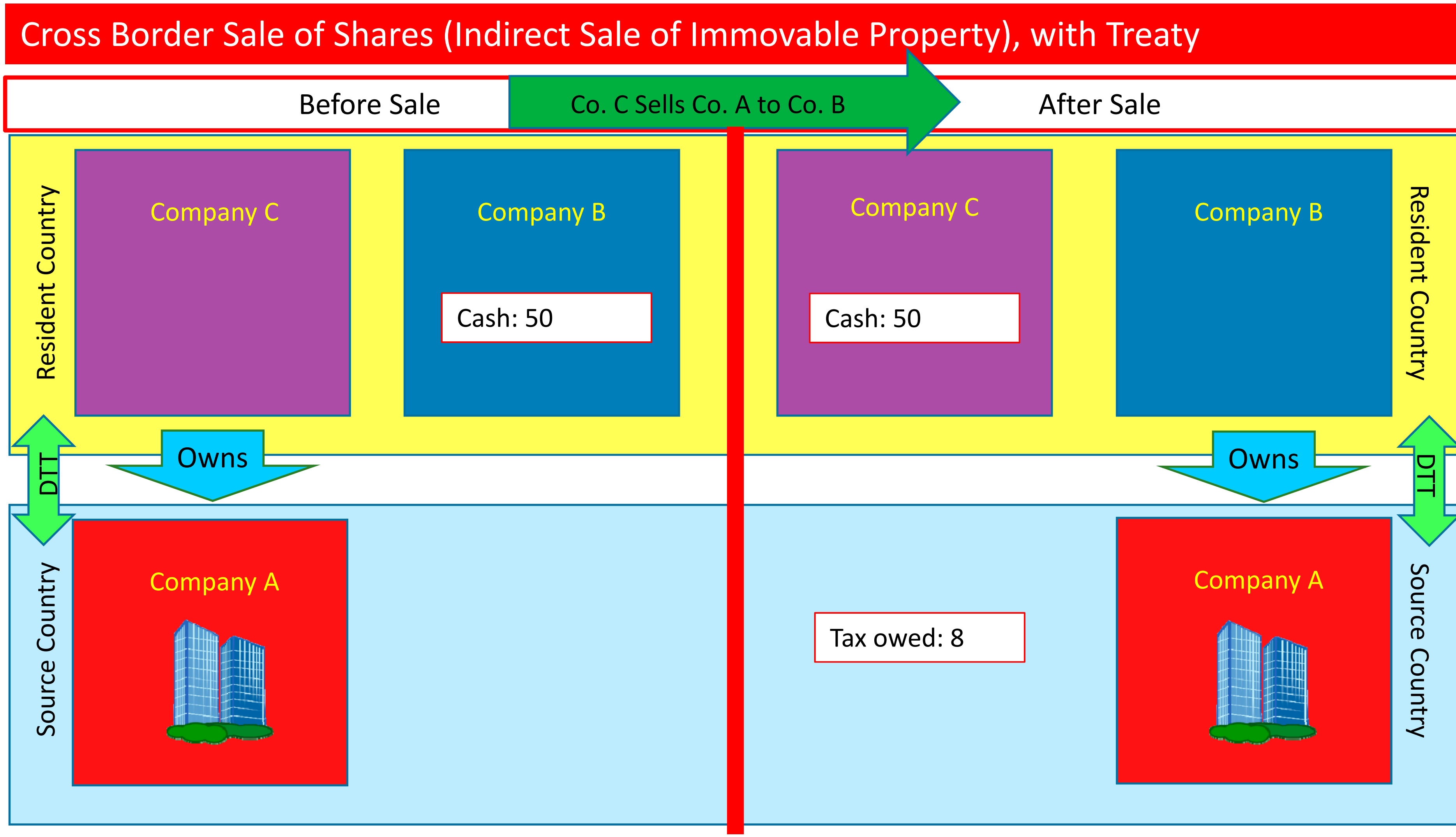


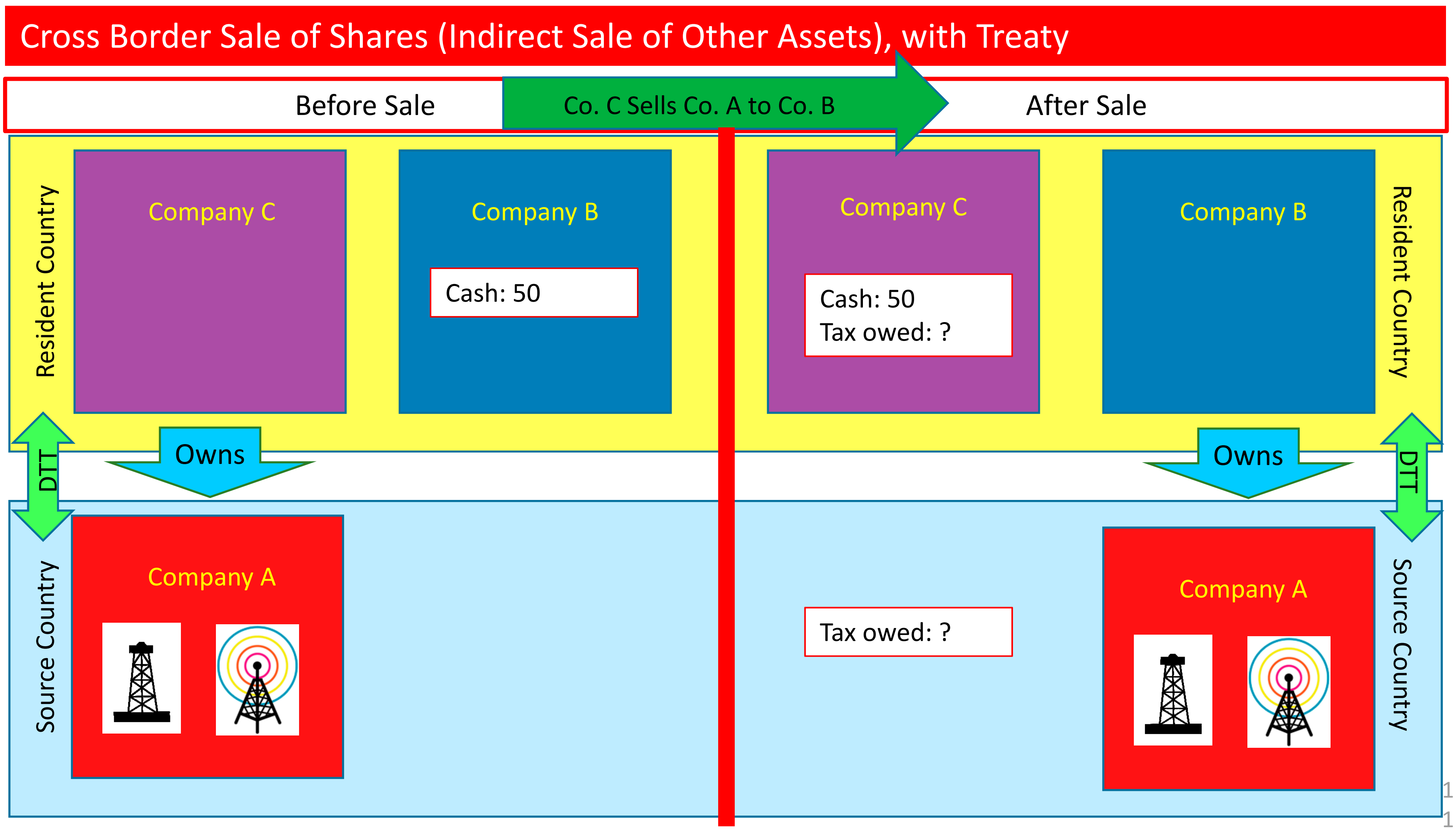
Indirect Sale of Shares Across Multiple Countries, No Treaties



Cross Border Sale of Shares (Indirect Sale of Asset), with Treaty

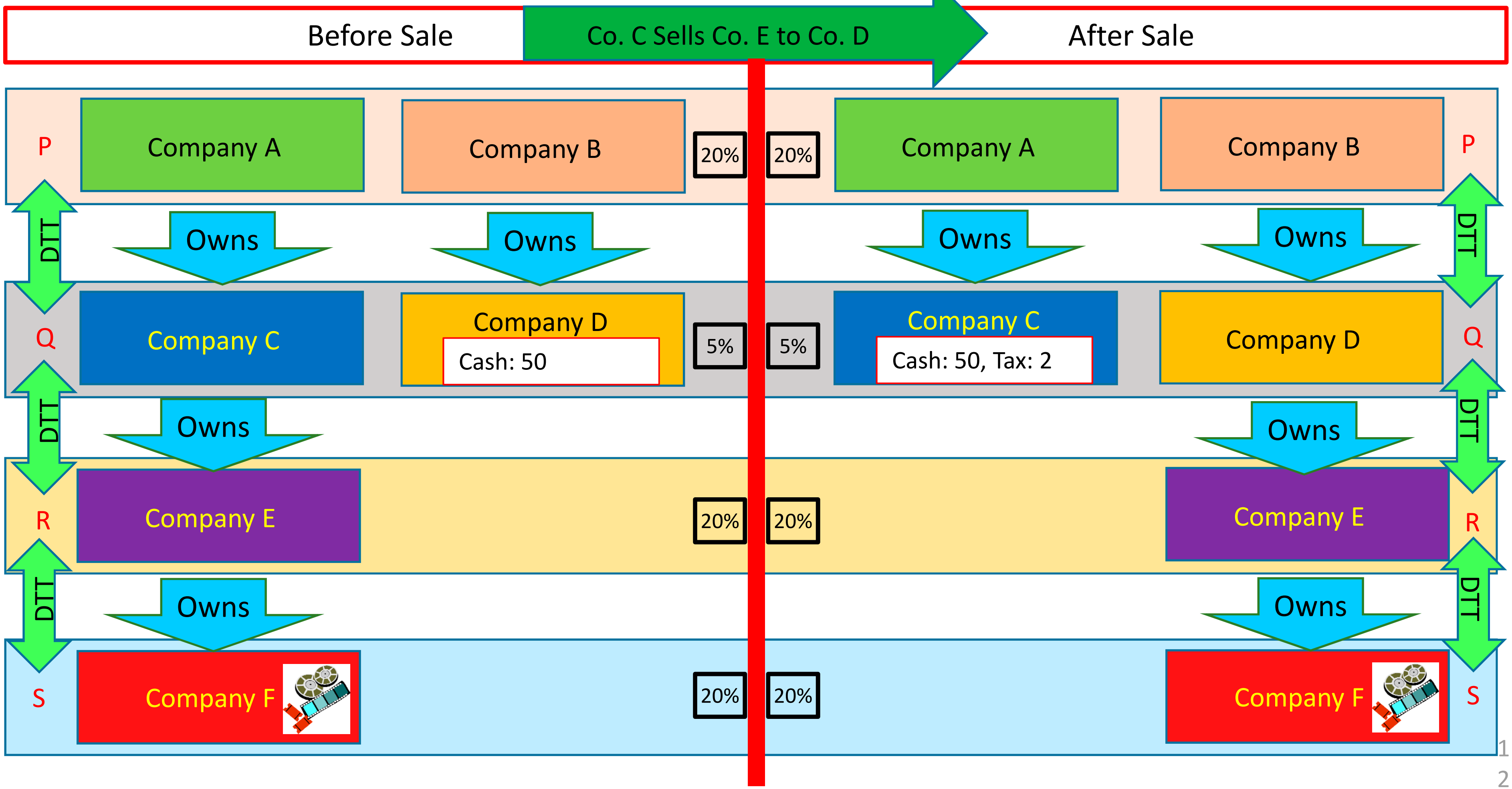



Cross Border Sale of Shares (Indirect Sale of Immovable Property), with Treaty
Before Sale
Co. C Sells Co. A to Co. B
After Sale
Resident Country
Company C
Company B
Cash: 50
Company C
Cash: 50
Company B
Resident Country
DTT
Owns
Owns
DTT
Source Country
Company A
Tax owed: 8
Company A
Source Country

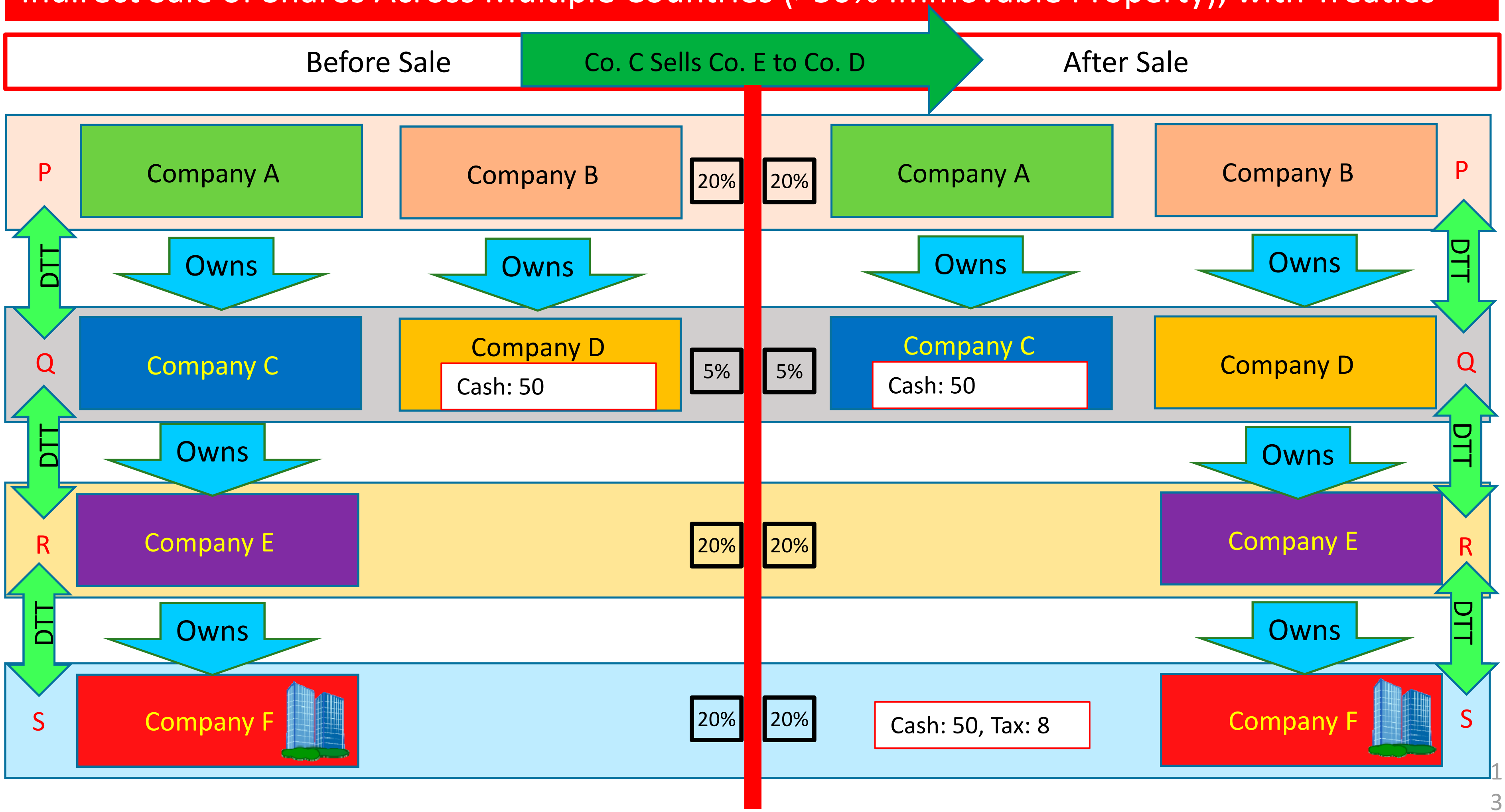


Cross Border Sale of Shares (Indirect Sale of Other Assets), with Treaty
Before Sale
Co. C Sells Co. A to Co. B
After Sale
Resident Country
Company C
Company B
Cash: 50
Company C
Cash: 50
Tax owed: ?
Company B
Resident Country
Owns
DTT
Owns
DTT
Source Country
Company A
Tax owed: ?
Company A
Source Country

Indirect Sale of Shares Across Multiple Countries (<50% Immovable Property), with Treaties



Indirect Sale of Shares Across Multiple Countries (>50% Immovable Property), with Treaties



Key Points and Questions

- Where capital gains tax is paid depends on Domestic Source Rules and Treaties
- How much tax is paid depends on where tax is paid
- Under the UN/OECD Models, tax on cross border sale of shares based on value of underlying asset:
    - Taxed in Source Country: if >50% Immovable Property
    - Taxed in Residence Country: all other sales
- Definition of Immovable vs. Moveable Property
    - Licenses for mining or petroleum?
    - Licenses for telecommunications or other regulated businesses?
    - Other?

How Can Source Country Tax Indirect Sales?

- Decide which types of assets should be taxed at source
- Domestic Source Rules must:
  - Require indirect sales of those assets taxable at source
  - Explicitly define “grey areas” as assets taxable at source
- Treaties must protect domestic source rules
- Require notification if ultimate (indirect) ownership changes (by more than some fixed percentage)
- Invalidate deed of property ownership (or license) when ultimate (indirect) ownership changes, *until capital gains taxes are paid in source country*
  - Otherwise, difficult to get money out of residence country