Selected global tax developments of 1999

Jan Kooi of Omnicom Europe picks out the tax developments of note from around the world in the final year of the first millennium.

The final year of this millennium has given us fewer major tax changes than in 1998. Nevertheless, there were developments of note in various countries around the world, some of which are discussed below.

On a pan-European scale, the VAT regime for certain labour-intensive services has been changed. Services relating to the repair of bicycles, footware and clothing, the renovation and repair of private homes (excluding parts that are essential to services), window cleaning of private homes, hairdressing and home healthcare services for children, the elderly and the ill will henceforth be subject to the reduced rate.

France

In 1998, France re-introduced the partial add-back of exempt dividends, a system that had been abolished in the early 1990s. For fiscal years ending on or after 1 January 1998, 2.5% of dividends received (where applicable, increased with ‘avoir fiscal’ and creditable withholding taxes) had to be added back if the dividends were exempt under the so-called ‘mere fille’ regime. The 2.5% add-back is always limited to the actual costs related to the holding of subsidiaries, if lower. For fiscal years ending on or after 1 January 1999, the amount to be added back is 5%, the maximum allowed under the EU parent-subsidiary directive.

From 15 September, the five-year holding period in the case of tax-free rollover contributions has been reduced to three years. Effectively, this measure already affects all transfers of this kind that took place after 15 September 1996.

Furthermore, France finally reduced the registration duty on the transfer of the ‘fonds de commerce’ of a business. A fond de commerce includes goodwill, client lists and basically the intangible assets, other than tradenames and licences, which constitute the core of a business. As from 15 September the transfer of a fond de commerce is no longer subject to 11.4% on amounts in excess of Ffr700,000 (6% for amounts between Ffr150,000 and Ffr700,00) but to 4.8% on transfers with a value exceeding Ffr150,000.

Germany

Last year, I reported on the major tax changes introduced in Germany. This year, there have been fewer substantial changes. Those changes that have been made were predominantly technical corrections. It has been announced, however, that there will be a very important tax overhaul on 1 January 2001. The proposals include the abolition of the current two-rate structure for corporations. At the moment, non-distributed profits are taxed at a rate of 40% while distributed profits are taxed at 30%. Under the proposed regime, the corporate income tax would be levied at a flat rate of 28%. It is also proposed that in future trade tax would be levied in the form of a surcharge on the corporate income tax (and therefore likely on the same basis). The tax overhaul will almost certainly also address the thin capitalisation rules. Most authors fear that the maximum debt : equity ratio will be reduced from 9 : 1 for qualifying holding companies to 3 : 1. It is even suggested that the debt : equity ratios would be reduced in general to 1 : 1. More clarity on this point should be available in the course of next year.


Jan Kooi

As far as personal income tax is concerned, the German proposals include the abolition of the imputation credit, which would be replaced by a taxation of only half of (domestic) dividends received. Furthermore, there have been rumours that the ownership percentage of shares above which capital gains would become taxable will be reduced from 10% or more to 1% or more.

Another important change in Germany will be the reduction of the amount to add back with respect to exempt foreign dividends. Under the current rules, which took effect on 1 January 1999, 15% of foreign dividends received, which are exempt under domestic law and tax treaties, has to be added back to income, representing costs related to the foreign subsidiaries. This percentage is in conflict with the EU parent-subsidiary directive and will be reduced to the maximum permitted of 5% in relation to all foreign subsidiaries.

The Netherlands

Another important development on the continent is the publication of Tax Plan 2001 in the Netherlands. It is virtually certain that this regime will become law.

The plan is a complete overhaul of the Dutch personal income tax act of 1964. The plan introduces a scheduling system, called boxes. There will be three boxes.

Box one will include earned income, income from an enterprise and income and expenses related to the owner occupied primary residence. The maximum rate will be 52% instead of the current 60%. Box two will deal with income from substantial shareholdings

(5% or more). The current proposal would subject such income to a flat tax of 30%. It is likely that this rate will be reduced slightly to avoid the fact that the cumulative tax rate of corporate income tax (35%) plus the 30%, would exceed the maximum rate in box one. The third box will include income from investments. The taxpayer will have to impute a forfeit income of 4% on the total amount of net wealth (other than the items included in box one or two), which imputed amount will be taxed at a flat rate of 30%. Actual income and gains will not be taxed in box three any more. The net wealth tax will be abolished. Tax Plan 2001 will take effect from 1 January 2001.

Changes that will have immediate effect in the Netherlands will be the gradual reduction by 0.1% per annum of the capital tax (stamp duty on capital contributions to legal entities) to 0.7% and the reduction of corporate income tax from 35% to 30% for the first Dfl50,000 of taxable income.

The United Kingdom

Changes in the UK are predominantly in the area of tax rates for individuals and in the introduction from 1 April, 2000 of a new 10% corporate income tax rate for profits up to £10,000 and a marginal rate for profits between £10,000 and £50,000. Furthermore, the Inland Revenue confirmed the ruling by the European Court in Luxembourg (ICI case) which held that group relief is also possible if two (or more) UK companies are held by a foreign parent, which would have been able to apply group relief had it been a UK resident company.

Finally, the Inland Revenue has acknowledged that there is no longer a difference between tax accounting and commercial accounting with respect to provisions, provided that the provisions are made in accordance with the new rules under Financial Reporting Standard 12 (effective 22 March 1999) and also providing that there is no specific tax legislation denying relief for certain provisions.

Denmark

A less publicised but potentially interesting change that became effective on 1 January 1999, is the modification of the Danish holding regime. As per that date, Denmark no longer levies withholding tax on dividend distributions out of dividends received by a Danish parent from qualifying foreign subsidiaries. The latter qualify for the participation exemption in Denmark provided that the Danish company owns at least 25% and has done so for a period of 12 months.

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Sweden

Sweden has also just amended its withholding tax on dividends by exempting dividend payments to 25% or more for non-resident corporate shareholders that are subject to a similar tax as the Swedish corporate income tax.

The United States

As usual, the US has issued a substantial number of rulings and (draft) regulations on a variety of subjects, including detailed regulations on the tax treatment of foreign branches. These 'regs' are highly technical and will have relevance predominantly for US groups. It may be, however, that some of the regulations will necessitate changes in foreign tax structures set up by such US groups.

Canada

Canada has changed the tax treatment of income received from US LLCs to stop perceived abuse. As from 1 January 2000, income that is received from a US LLC, which is transparent for US tax purposes, will no longer be treated as exempt foreign dividends but will now be taxable in Canada as business income. Canadian-owned LLCs have, in the past, been used as financing vehicles.

Australia

Turning to Australia, the following can be noted. During this year the so-called Ralph report (named after the committee chairman) was published and discussed. Some of the changes that will be implemented based on the recommendations of the report will include a reduction of corporation tax from the current 36% to 34% for fiscal year 2000/2001. A further reduction will take place for 2001/2002 and onwards, when the rate will become 30%.

On the personal income tax front, as from 1 October 1999, only half of capital gains is taxed, leading to an effective maximum tax on capital gains of 24.25%. Other changes in the capital gains tax regime include, as from 21 September 1999, a replacement of the 50% goodwill exemption by a general 50% exemption for all active assets. From 20 September, all business assets that have been held by an individual who is at least 55 years old and continuously for 15 years, will be exempt from capital gains tax. A rollover exemption will be introduced for scrip for scrip takeovers.

What the future holds

Looking towards the future, I believe that we can expect increasing legislation when dealing with the tax aspects of internet and e-commerce. Discussion papers have already appeared in many countries. As far as Europe is concerned, agreement might be reached concerning the controversial directive on interest withholding tax for individuals, now that there seems to be some opening to accommodate the UK objections in connection with the City's importance in the bond market. In view of the substantial differences in the various corporate and personal income tax systems in the European Community, it is, however, unlikely that we will experience a real harmonisation on this front in the early years of the second millennium.

It should be noted that the European Commission has recently commissioned a study on the effective corporate income tax rates in the various EU countries. This study is related to an evaluation of the European Code of Conduct, which aims to combat fiscal discrimination between EU countries. ■

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