

## UPDATES & OTHER TIDBITS

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### Tags

B.E.P.S.  
C.F.C.'s  
Compliance  
Corporate Tax  
Criminal Violations  
Google  
Information Disclosure  
Right to Be Forgotten  
Tax Evasion  
Tax System Administration

### B.E.P.S. PROJECT FACES CHALLENGE IN ADDRESSING C.F.C. RULES

The O.E.C.D.'s pending base erosion and profit shifting action plan is due to face a significant challenge as to how to address controlled foreign corporations. Action 3, which strengthens C.F.C. rules, is set to be released in 2015. Currently, European case law restricts the scope of E.U. members establishing C.F.C. regimes.

Stephen E. Shay of Harvard Law School says the U.S. is encouraging the expansion of the C.F.C. rules as a way to solve several of the issues the B.E.P.S. action plan is trying to address, however, these new rules run the risk of being contrary to E.U. jurisprudence. The E.U.'s ability to adopt stringent C.F.C. rules is limited by the *Cadbury Schweppes* (C-196/04), a 2006 ruling from the Court of Justice of the European Union. The Court held that E.U. freedom of establishment provisions preclude the U.K. C.F.C. regime unless the regime "relates only to wholly artificial arrangements intended to escape the national tax normally payable."

Without resolving the issue among E.U. countries, Action 3 may not be effective in appropriately addressing earnings stripping. However, Shay also added that Action 2, which neutralizes the effects of hybrid mismatch arrangements, so far appears to include an approach that works without C.F.C. rules.

### CHARGES LAID AGAINST U.S. CITIZEN FOR MAINTAINING ALLEGED SECRET SWISS BANK ACCOUNTS

Department of Justice announced that charges have been laid against Peter Canale, a U.S. citizen and resident of Kentucky, for conspiring to defraud the I.R.S., evade taxes, and file a false individual income tax return. It is alleged that Canale conspired with his brother and two Swiss citizens to establish and maintain secret, undeclared bank accounts in Switzerland.

In approximately the year 2000, a relative of Canale died and left a substantial portion of assets which were held in an undeclared Swiss bank account to Canale and his brother, Michael. The brothers met with two Swiss citizens, who agreed to

continue to maintain the assets in the undeclared account for the benefit of the Canales.

In approximately 2005, an account was opened at the Swiss bank Wegelin in the name of a sham foundation under the laws of Lichtenstein to conceal Canale's ownership. By the end of 2009, the assets of the account amounted to approximately \$789,000. For the years 2007 through 2010, the D.O.J. alleges that Canale willfully failed to report on his tax returns the interest and income accrued in the undeclared accounts and also failed to file F.B.A.R.'s with the I.R.S. as required by law. The charges carry a potential statutory maximum sentence of five years in prison.

## **G-20 LEADERS COMMIT TO FINALIZING B.E.P.S. PROJECT IN 2015**

G-20 leaders at the November summit in Brisbane, Australia expressly committed to completing the joint action plan with the O.E.C.D. addressing B.E.P.S. Furthermore, they addressed a strategy to increase beneficial ownership and endorsed a common reporting standard ("C.R.S.") for the automatic exchange of information.

At the conclusion of the summit, the leaders issued a communiqué which promised the completion of all the action items of the B.E.P.S. project and expressed agreement that "profits should be taxed where economic activities deriving the profits are performed and where value is created." They also praised a Germany-U.K. proposal released on November 11 to abolish harmful intellectual property rights regimes. The proposal, which was based on the O.E.C.D.'s modified nexus approach, will ask the O.E.C.D. to formally approve the plan during the O.E.C.D.'s Committee on Fiscal Affairs meeting to be held in January.

Other commitments by the G-20 leaders included improving the transparency of beneficial ownership and both the public and private sectors. However, much to the dismay of non-governmental entities, it did not call for the creation of public beneficial ownership registries. The U.K. and Denmark have already committed to making the registries publicly available. The recommendations included:

- Ensuring that legal persons maintain adequate, accurate, and current beneficial ownership information onshore;
- Requiring financial institutions and designated nonfinancial businesses or professions to verify the beneficial ownership of their customers; and
- Ensuring that trustees of express trusts maintain accurate and current beneficial ownership information.

Each G-20 country will report in writing the steps it will take to implement the beneficial ownership principles and improve the effectiveness of the G-20's legal, regulatory, and institutional framework for making beneficial ownership more transparent.

Finally, the O.E.C.D.'s C.R.S. for the automatic exchange of information was endorsed with G-20 leaders promising that their countries will begin the automatic

exchange of information by 2017 or 2018. This is consistent with the October signing of the competent authority agreement to implement C.R.S.

## CREDIT SUISSE TO PAY \$1.8 BILLION TO I.R.S.

On November 21, Credit Suisse was sentenced to pay \$1.8 billion to the I.R.S. as a result of pleading guilty to conspiracy to aid and assist U.S. taxpayers in filing false income tax returns and other documents with the I.R.S.

The plea agreement, in addition to the agreements made with state and federal agencies, results in Credit Suisse paying approximately \$2.6 billion to the U.S., in addition to the \$196 million to the Securities and Exchange Commission (“S.E.C.”) in disgorgement, interest, and penalties.

Under the plea agreement, Credit Suisse acknowledged that, for decades prior to and including 2009, it operated an illegal cross-border banking business that knowingly and willfully aided and assisted thousands of U.S. clients in opening and maintaining undeclared bank accounts and concealing offshore assets and income from the I.R.S.

Furthermore, Credit Suisse also agreed to make a complete disclosure of its cross-border activities, to cooperate in treaty requests for account information, to close the accounts of clients who fail to come into compliance with U.S. reporting obligations, and to implement programs to ensure compliance with U.S. laws in current and future dealings with U.S. customers.

## U.S. WANTS TO AVOID AN INCREASE IN COMPLIANCE BURDEN AS A RESULT OF B.E.P.S.

At a Washington event in connection with the release of a joint report by the World Bank Group and PwC on November 20, the Treasury Deputy Assistant Secretary (International Affairs), Robert Stack, stated that the O.E.C.D.’s action plan expected to be completed in 2015 should avoid increasing companies’ compliance burdens by creating solutions that are simple to administer and less likely to be prone to dispute. This might include redefining the transfer pricing rules to avoid vagueness.

There has been a general expectation among tax practitioners that disputes will arise when the B.E.P.S. project is implemented. However, in response, Stack says that a focus should then be put on modernizing dispute resolution mechanisms and modernizing tax administrations so disputes are avoided at the bottom level when an audit occurs, or such that the dispute can easily be resolved.

There has also been concern that the information reporting costs will increase the compliance burden, however, some of those concerns have been alleviated because the template has been scaled back to a more achievable set of information requirements. Otherwise, it could have resulted in “phenomenal costs” for country-by-country reporting.

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An emphasis has been placed on improving administrative systems and resources. In an attempt to pave the way for other counties to follow, the I.R.S. outlined four digital initiatives it has been planning, including the creation of online accounts for transactions, customer education to simplify the complexity of tax information, third-party collaboration, and internal tools for I.R.S. employees. No timeline has been given for the completion of the project.

## HOUSE MAY EXTEND LAPSED TAX BREAKS

Two congressional aides indicated that the House of Representatives will revive dozens of lapsed tax breaks and extend them through the end of this year. The proposal comes soon after the collapse of a bipartisan proposal to make some tax breaks permanent. The extension seems to indicate that Congress does not want to disrupt tax filing season in January.

## I.R.S. USES CODE §956 ANTI-ABUSE RULE TO TARGET BACK-TO-BACK LOANS

In a recent memorandum,<sup>28</sup> the I.R.S. re-characterized and collapsed a series of bank-to-bank loans between related controlled foreign corporations and indicated that the deemed inclusion for the parent companies was not limited to the applicable earnings of the intermediaries, but also included the earnings of the parent companies under Code §956.

The I.R.S. based its conclusion on several factors. However, the most salient was the rejection of the taxpayer's business purpose for making the back-to-back loans. Taxpayer tried to argue that the business purpose of the loans stemmed from the parent C.F.C. acting as a shared service center for the cash management of the taxpayer's group in a certain region. The I.R.S. rejected the argument because the taxpayer did not adequately explain why the lower tier C.F.C.'s needed to borrow from the parent companies, other than the need to fund their loans to the taxpayer.

## EMERGING CONSEQUENCES OF E.U.'S RIGHT TO BE FORGOTTEN

In May 2014, the European Court of Justice, the highest court in Europe, ruled against Google Spain SL and its parent company, Google Inc., (collectively "Google"), ordering the companies to comply with Europeans requesting the removal of certain results from its search engine. The court found that Google was responsible for the content of the information it posts and therefore was required to comply with E.U. data privacy laws.<sup>29</sup>

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<sup>28</sup>

CCA 201446020, November 14, 2014.

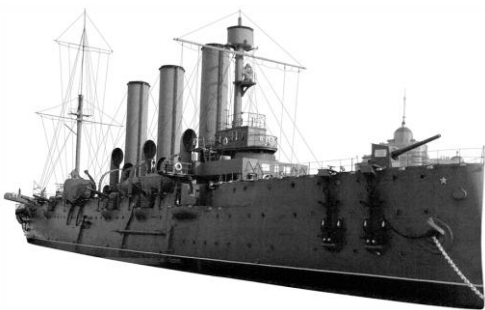
<sup>29</sup>

Case C-131/12.

On the first day of compliance alone (May 30, 2014), Google received 12,000 requests to have personal details removed from its search engine.<sup>30</sup> Since then, figures suggest that Google has received more than 174,000 of these requests, of which it has removed approximately 41.5%, and other search engines, such as Bing and Yahoo are now following suit.<sup>31</sup>

In an age where most research is done online, it is necessary to balance the right to know with the right to protect an individual's privacy. While this ruling provides for the inherent right to the privacy, it also impinges upon freedom of speech, and its implications are now emerging in the international tax sector.

To quote U.K. attorney Sara Mansoori, "90 percent of investigators launch their offshore tax evasion cases by doing a search on Google."<sup>32</sup> This ruling obstructs investigations into offshore tax evasion by allowing for the removal of relevant personal data. At the same time, it is important to note that this ruling only effects European countries. The information that is deleted from search engines in Europe can still be accessed from outside the European Union, and with the help of websites such as HideMyAss.com and Hola.org, it is possible to conduct virtual searches from the country of one's choosing.



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<sup>30</sup> "Removal of Google Personal Information Could Become Work Intensive." EuropeNews.net. June 1, 2014.

<sup>31</sup> Dredge, Stuart. "Microsoft and Yahoo respond to European 'right to be forgotten' requests." *The Guardian*. December 1, 2014.

<sup>32</sup> U.K. Attorney: Offshore Tax Investigators Can Bypass "Right to be forgotten" Ruling by Ali Qassim.