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and International Tax Law

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# Trends and Players in Tax Policy

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European and International  
Tax Law and Policy Series

IBFD



# Trends and Players in Tax Policy

## Why this book?

Tax policy has always been a predominant element of national economic policies and a decisive tool in directing the actions of governments in the economic field. In the past decade, however, as an increasingly globalized economy has presented challenges, tax policy has gained new importance because of its global dimension.

The aim of this book is to provide a comprehensive overview of the tax policy trends that can be seen in various countries since the turn of the century. Thirty-three national reports from countries across the globe have been compiled in this volume. The reports, which were prepared for the conference "Trends and Players in Tax Policy" that took place in Rust (Austria) from 4-6 July 2013, focus on how different countries pursue their tax policy goals in the global economy and try to secure competitiveness and, at the same time, protect the national tax base. Much attention is given to the main factors influencing the formulation of tax policies and tax legislation as well as to the changes in the relationship between tax administrations and taxpayers. In addition to the national aspects, the book also outlines global trends and best practices through which it hopes to set the path to building up a globally consistent exercise of tax sovereignty. The general report extensively discusses issues connected with the Base Erosion and Profit Shifting (BEPS) project, taking into account national reports and other information on additional countries.

The book is of relevance to tax policymakers, tax practitioners, academics and students doing research on tax law, and all those who have an interest in the most current issues in the field of tax policy.

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## Table of Contents

<b>Preface</b>		xliii
	Part One	
<b>Chapter 1: General Report</b>		3
	<i>Pasquale Pistone</i>	
1.0.	Introduction	3
1.1.	Trends in tax policy as from 2000	4
1.1.1.	Personal income taxes	4
1.1.2.	Corporate income taxes	9
1.1.3.	Other business taxes	12
1.1.4.	VAT	12
1.1.5.	Excise duties	15
1.1.6.	Taxes on capital	16
1.1.7.	Compulsory social security contributions paid to government	18
1.1.8.	Environmental taxes	18
1.1.9.	Other taxes	20
1.2.	Main drivers of tax reforms since 2000	21
1.2.1.	Main drivers of tax reforms since 2000	21
1.2.2.	Influence of tax reform commissions	23
1.2.3.	Influence of independent research institutes and universities	26
1.2.4.	Tax expenditure budget	26
1.2.5.	Assessment of the impact of tax reform	27
1.3.	Drafting and reviewing tax legislation and regulations	28
1.3.1.	Drafting of tax legislation	28
1.3.2.	The role of outside stakeholders	30
1.3.3.	Drafting of tax regulations	31
1.3.4.	Influence of tax regulations and secondary sources of law in the design of tax policy	34
1.3.5.	Assessing the consistency of drafting with the constitutional, supranational and treaty law	35

## Table of Contents

---

1.4.	Building up tax expertise	36
1.4.1.	Training of tax professionals	36
1.4.2.	Professional qualifications and their assessment	39
1.4.3.	Ideas for future development	41
1.5.	The changing relationship between tax administrations and taxpayers	42
1.5.1.	General issues	42
1.5.2.	The protection of taxpayers' rights: From theory to practice	42
1.5.3.	The relations between taxpayers' rights and human rights	46
1.5.4.	The consequences of violations in tax matters	48
1.5.5.	Legal remedies in tax matters	49
1.5.6.	The relations between tax authorities, taxpayers and their advisors	52
1.5.7.	The protection of legal certainty in the tax system	53
1.5.8.	The protection of the collection of revenue	55
1.5.9.	The status and remuneration of tax officials	56
1.6.	Major players in tax policy	56
1.6.1.	General issues	56
1.6.2.	The role of the parliament and government in determining the tax policy	57
1.6.3.	Tax policy and regulatory goals	58
1.6.4.	The influence of external players	58
1.6.5.	The influence of international external players	59
1.6.6.	Participation in the debate on international tax policy	61
1.7.	Tax policy in the global economy	62
1.7.1.	Competitiveness	62
1.7.2.	Smart tax competition	63
1.7.3.	Outward and inward investment	65
1.7.4.	The role of tax treaties in attracting inward investment	66
1.7.5.	Tax incentives and tax sparing	68
1.7.6.	Measures against aggressive tax planning	69
1.7.7.	The BEPS project	70
1.8.	Good governance	72
1.8.1.	General issues	72
1.8.2.	Global tax transparency and good governance	72

1.8.3.	The expected and desirable developments in international tax coordination	74
1.8.4.	Good tax compliance and good corporate governance	75
1.9.	Conclusions	75
Part Two		
<b>Chapter 2:</b>	<b>Australia</b> <i>Richard Krever and Peter Mellor</i>	79
2.1.	Trends in tax policy as from 2000	79
2.1.1.	Personal income tax	79
2.1.2.	Corporate income tax	81
2.1.3.	Other business taxes	82
2.1.4.	VAT	83
2.1.5.	Excises	84
2.1.6.	Recurrent taxes on capital	85
2.1.7.	Non-recurrent taxes on capital	85
2.1.8.	Compulsory social security contributions paid to government	86
2.1.9.	Environmental taxes	86
2.1.10.	Other taxes (e.g. natural resources taxes)	86
2.2.	Main drivers of tax reforms since 2000	87
2.2.1.	Main drivers of tax reforms since 2000	87
2.2.2.	Major tax reform commissions	89
2.2.3.	Influence of independent research institutes and universities	91
2.2.4.	Australian tax expenditures budget	91
2.2.5.	Data on tax reforms	92
2.3.	Drafting and reviewing tax legislation and regulations	92
2.3.1.	By whom are tax laws drafted?	92
2.3.2.	Outside stakeholders	93
2.3.3.	Drafting of secondary instruments	94
2.3.4.	Influence of secondary law	94
2.3.5.	Verification of proposals	95
2.4.	Building up tax expertise	95
2.4.1.	Formal training	95
2.4.2.	Professional qualifications	95

## Table of Contents

---

2.4.3.	Verification of qualifications	96
2.4.4.	Teaching of tax law drafting	96
2.4.5.	Role of universities in improving development of tax expertise	96
2.5.	The changing relationship between tax administrations and taxpayers	97
2.5.1.	Enactment of taxpayers' rights	97
2.5.2.	Taxpayers' rights and human rights	98
2.5.3.	Legal sanctions	98
2.5.4.	Avenues of appeal for taxpayers	99
2.5.5.	Reimbursement of taxpayer expenses	99
2.5.6.	Overall relationship between tax administration, taxpayers and advisors	100
2.5.7.	Tax administration measures to provide greater certainty	101
2.5.8.	Measures to protect the corporate tax base	101
2.5.9.	Scope for retroactive tax legislation	102
2.5.10.	Social prestige of tax officials	103
2.5.11.	Official measures of tax administration success	104
2.6.	Major players in tax policy	104
2.6.1.	Formal procedure for changes of tax law	104
2.6.2.	Relative influence of political parties, lobbying groups and public officials	105
2.6.3.	Influence of ministries in use of tax for social engineering	105
2.6.4.	Role of other interest groups	106
2.6.5.	Adoption of measures against long-term interests or in conflict with culture	106
2.6.6.	Role of international and regional organizations	107
2.6.7.	Role of government in influencing organizations	107
2.6.8.	Specialized bodies established by government	108
2.7.	Tax policy in the global economy	108
2.7.1.	Competitive considerations in tax policy	108
2.7.2.	Moves to "smart tax competition"	109
2.7.3.	Tax arrangements and inward and outward investment	110
2.7.4.	Tax treaties and inward investment	110
2.7.5.	Tax incentives, tax sparing arrangements and inward investment	111



2.7.6.	Measures to reduce cross-border aggressive tax planning	111
2.7.7.	Profit shifting and base erosion	112
2.7.8.	Barriers to inward investment	112
2.7.9.	Transition time for reforms	113
2.8.	Good governance	113
2.8.1.	Tax administration access to information	113
2.8.2.	Next steps in improved international cooperation	115
2.8.3.	Other actions to strengthen ties	116
2.8.4.	Strengthening linkage between good tax compliance and good corporate governance	116
<b>Chapter 3:</b>	<b>Austria</b>	119
	<i>Alexander Zeiler</i>	
3.1.	Trends in tax policy as from 2000	119
3.1.1.	Taxation of individuals	119
3.1.1.1.	New taxation scheme for capital gains	119
3.1.1.2.	Taxes on capital	120
3.1.2.	Corporate taxation	120
3.1.3.	Excises	121
3.1.4.	Other taxes	122
3.2.	Main drivers of tax reforms since 2000	122
3.2.1.	Main drivers of tax reforms since 2000	122
3.2.2.	Data on tax expenditures and reforms	123
3.3.	Drafting and reviewing tax legislation and regulations	124
3.3.1.	Formal framework	124
3.3.2.	“Real” tax legislation procedure	124
3.3.3.	Secondary instruments	126
3.3.3.1.	<i>Verordnung</i> (regulation)	126
3.3.3.2.	Richtlinien and <i>Erlässe</i> (directives)	127
3.3.4.	Review procedures	128
3.4.	Building up tax expertise	129
3.4.1.	Formal training	129
3.4.2.	Qualifications	130
3.4.2.1.	Tax consultant	130
3.4.2.2.	Certified accountants	130

3.5.	The changing relationship between tax administrations and taxpayers	130
3.5.1.	Avenue of appeal	132
3.5.1.1.	Complaint to the Federal Tax Court	132
3.5.1.2.	Appeal to the Supreme Administrative Court	133
3.5.1.3.	The role of the Constitutional Court	133
3.5.2.	Legal sanctions	134
3.5.3.	Reimbursement of taxpayer expenses in court proceedings	135
3.5.4.	Measures for legal certainty	136
3.5.5.	Retroactive tax legislation	137
3.6.	Major players in tax policy	138
3.6.1.	Political parties	138
3.6.2.	Government	138
3.6.3.	Administration	139
3.6.4.	Interest groups	140
3.6.5.	International organizations	142
3.7.	Tax policy in the global economy	143
3.7.1.	Domestic tax law	143
3.7.1.1.	Corporations	143
3.7.1.2.	Individuals	143
3.7.2.	Austrian treaty policy	144
3.7.3.	Anti-avoidance rules	145
3.8.	Good governance	146
3.8.1.	Tax transparency	146
3.8.2.	International cooperation	147
3.8.3.	Corporate governance	147
<b>Chapter 4:</b>	<b>Brazil</b>	149
	<i>Luís Eduardo Schoueri and Mateus Calicchio Barbosa</i>	
4.1.	Trends in tax policy as from 2000	149
4.1.0.	Introduction	149
4.1.1.	Individual income tax	149
4.1.2.	Corporate income tax	150
4.1.2.1.	General developments in the corporate income tax system	150
4.1.2.2.	Calculating the tax base	152
4.1.2.3.	Simplified tax base	153

4.1.3.	Value added taxation and harmful tax competition	155
4.1.4.	Alternative to social security contribution on payroll	159
4.1.5.	Environmental taxes	161
4.2.	Main drivers of tax reforms since 2000	163
4.3.	Drafting and reviewing tax legislation and regulations	165
4.4.	Building up tax expertise	168
4.4.1.	Tax advisors	168
4.4.2.	Tax authorities	169
4.4.3.	Training on drafting of tax law	170
4.5.	The changing relationship between tax administrations and taxpayers	171
4.5.1.	The Constitution, taxpayers' and human rights	171
4.5.2.	The administrative review procedure	172
4.5.3.	Reimbursement of expenses in court proceedings	173
4.5.4.	Advance rulings and certainty to taxpayers	174
4.5.5.	Protecting the corporate tax base: Brazilian thin cap rules and the general anti-avoidance rule	176
4.6.	Major players in tax policy	178
4.6.1.	Society and lobbying	178
4.6.2.	Brazil and the OECD	180
4.7.	Tax policy in the global economy	182
4.7.1.	Controlled foreign company rules and Brazilian investments abroad	182
4.7.2.	Brazilian transfer pricing rules	183
4.7.3.	Tax treaties and tax sparing	184
4.8.	Good governance	186
<b>Chapter 5:</b>	<b>Canada</b>	<b>191</b>
	<i>Kim Brooks</i>	
5.1.	Trends in tax policy as from 2000	191
5.1.0.	Introduction	191
5.1.1.	General trends	192
5.1.2.	Tax rates	192
5.1.2.1.	Personal income tax	192

## Table of Contents

---

5.1.2.2.	Corporate income tax	193
5.1.2.3.	Consumption taxes	193
5.1.2.4.	Capital taxes	194
5.1.3.	Tax incentives	194
5.1.3.1.	Personal income tax	194
5.1.3.2.	Corporate income tax	195
5.1.4.	Capital gains tax	196
5.1.5.	Other developments in domestic tax law	196
5.1.5.1.	Personal income tax	196
5.1.5.2.	Corporate income tax	197
5.1.6.	Developments in international taxation	198
5.1.7.	Environmental taxes	198
5.2.	Main drivers of tax reforms since 2000	199
5.2.0.	Introduction – Political and economic background	199
5.2.1.	The role of governmental institutions	200
5.2.2.	Tax reform commissions	201
5.2.3.	Availability of data on tax expenditures	203
5.3.	Drafting and reviewing tax legislation and regulations	203
5.4.	Building up tax expertise	205
5.5.	The changing relationship between tax administrations and taxpayers	206
5.5.1.	The structure of the tax administration	206
5.5.2.	Taxpayers' rights	207
5.5.3.	Avenues of appeal	208
5.5.4.	Voluntary disclosures program	209
5.5.5.	Retroactive legislation	209
5.6.	Major players in tax policy	210
5.6.1.	The role of the courts in Canadian tax law	210
5.6.2.	The influence of foreign tax law developments in Canada	211
5.6.3.	The role of research organizations	212
5.6.4.	The role of professional associations and other interest groups	212
5.7.	Tax policy in the global economy	213
5.8.	Good governance	215

<b>Chapter 6: China</b>	219
<i>Kang Jia and Na Li</i>	
6.1. Trends in tax policy as from 2000	219
6.1.0. Introduction	219
6.1.1. Personal income taxes	219
6.1.2. Corporate income taxes	221
6.1.3. Other business taxes	222
6.1.4. Value added tax	223
6.1.4.1. VAT reform in 2008	223
6.1.4.2. VAT Pilot Programme	224
6.1.5. Excises	225
6.1.6. Recurrent taxes on capital	226
6.1.6.1. Resident property tax pilot projects in Shanghai and Chongqing	226
6.1.7. Compulsory social security contributions paid to government	227
6.1.8. Environmental taxes	227
6.1.9. Other taxes	227
6.1.9.1. Resource tax reform	227
6.1.9.2. Abolition of agriculture tax	228
6.2. Main drivers of tax reforms since 2000	228
6.3. Drafting and reviewing tax legislation and regulations	230
6.4. Building up tax expertise	232
6.5. The changing relationship between tax administrations and taxpayers	233
6.5.1. Rights of taxpayers	233
6.5.2. Legal sanctions	234
6.5.3. Tax review and litigation	235
6.5.4. Relationship between tax authority and taxpayers	235
6.5.5. Major measures to protect the corporate tax base	236
6.5.6. Social prestige of tax officials	238
6.6. Major players in tax policy	238
6.7. Tax policy in the global economy	240
6.8. Good governance	242

<b>Chapter 7: Colombia</b>	245
<i>Natalia Quiñones</i>	
7.1. Trends in tax policy as from 2000	245
7.1.0. Introduction	245
7.1.1. Personal income taxes	245
7.1.2. Corporate income taxes	246
7.1.3. Other business taxes	247
7.1.4. Value added tax	248
7.2. Main drivers of tax reforms since 2000	249
7.2.1. Main drivers and tax reform objectives	249
7.2.2. Tax reform commissions	251
7.2.3. Independent research institutes and universities	252
7.2.4. Measuring tax expenditures	252
7.2.5. Assessment of the impact of tax reforms	253
7.3. Drafting and reviewing tax legislation and regulations	253
7.3.1. Drafting of tax law provisions	253
7.3.2. Outside stakeholders and tax legislation	254
7.3.3. Drafting of secondary instruments of tax policy	255
7.3.4. Verification of constitutional consistency	256
7.4. Building up tax expertise	256
7.5. The changing relationship between tax administrations and taxpayers	257
7.5.1. Taxpayers' rights	257
7.5.2. Taxpayers' rights and human rights	258
7.5.3. Legal sanctions	259
7.5.4. Appeals and tax procedure	259
7.5.5. The taxpayer's expenses in court proceedings	260
7.5.6. Relationship between tax administration, taxpayers and their advisors	261
7.5.7. Tax certainty	261
7.5.8. Protection of the corporate tax base	262
7.5.9. Retroactivity in tax measures	263
7.5.10. Tax officials	264
7.5.11. Measures of the success of tax administrations	265
7.6. Major players in tax policy	265
7.6.1. Procedure for changes of tax law	265

7.6.2.	Influence of political parties, lobbying groups, public officials in the Ministry of Finance and in other ministries	266
7.6.3.	Academia, media, trade unions, associations of employers or other interest groups	266
7.6.4.	Measures that conflict with culture or habits	267
7.6.5.	International organizations	268
7.7.	Tax policy in the global economy	268
7.7.1.	Competition considerations	268
7.7.2.	Outward investment and inward investment	269
7.7.3.	Tax incentives and tax sparing	270
7.7.4.	Cross-border aggressive tax planning	270
7.7.5.	Tax-related barriers to inward investment	271
7.8.	Good governance	272
7.8.1.	Information and transparency initiatives	272
7.8.1.1.	Main barriers to the effective use of information	272
7.8.1.2.	Main risks posed by better transparency	273
7.8.2.	The next steps in improved international cooperation?	273
7.8.3.	Other actions to strengthen ties between countries	274
<b>Chapter 8:</b>	<b>Croatia</b>	275
	<i>Hrvoje Arbutina, Tereza Rogić Lugarić, Sonja Cindori, Jasna Bogovac, Nevia Čičin Šain and Ivan Reiner</i>	
8.1.	Trends in tax policy as from 2000	275
8.1.0.	Introduction	275
8.1.1.	Personal income tax	277
8.1.2.	Corporate income tax	278
8.1.3.	Value added tax	279
8.1.4.	Excises	280
8.1.5.	Recurrent taxes on capital	280
8.1.6.	Non-recurrent taxes on capital	281
8.1.7.	Compulsory social security contributions paid to government	281
8.2.	Main drivers of tax reforms since 2000	281
8.3.	Drafting and reviewing tax legislation and regulations	283
8.4.	Building up tax expertise	284

## Table of Contents

---

8.5.	The changing relationship between tax administrations and taxpayers	286
8.6.	Major players in tax policy	290
8.7.	Tax policy in the global economy	293
8.8.	Good governance	294
<b>Chapter 9:</b>	<b>Czech Republic</b>	299
	<i>D. Nerudová and L. Moravec</i>	
9.1.	Trends in tax policy as from 2000	299
9.1.0.	Introduction	299
9.1.1.	Personal income tax	301
9.1.2.	Corporate income tax	304
9.1.3.	Value added tax	305
9.1.4.	Excises	307
9.1.5.	Recurrent taxes on capital	308
9.1.6.	Non-recurrent taxes on capital	308
9.1.7.	Compulsory social security contributions paid to government	308
9.1.8.	Environmental taxes	309
9.1.9.	Other taxes	309
9.2.	Main drivers of tax reforms since 2000	310
9.2.1.	Main drivers of tax reforms since 2000	310
9.2.2.	The role of independent advisory bodies and research institutes	310
9.2.3.	Data on the impact of the tax reforms	311
9.3.	Drafting and reviewing tax legislation and regulations	311
9.3.1.	The drafting of tax law provisions	311
9.3.2.	Consultation on draft legislation	312
9.3.3.	The drafting of secondary instruments	312
9.3.4.	Verifying compliance with higher-ranking law	312
9.4.	Building up tax expertise	313
9.5.	The changing relationship between tax administrations and taxpayers	314
9.5.1.	Taxpayers' rights	314



9.5.2.	Avenues of appeal	315
9.5.3.	The relationship between tax administration, taxpayers and their advisors	315
9.5.4.	Measures protecting the corporate tax base	319
9.5.5.	Retroactivity in tax legislation	319
9.5.6.	The social prestige of tax officers	320
9.6.	Major players in tax policy	321
9.6.1.	The procedure for changes of tax law	321
9.6.2.	The influence on tax policy formulation of political parties, lobbying groups, other ministries, academia and trade unions	321
9.6.3.	The role of international and regional organizations in influencing tax policy	322
9.7.	Tax policy in the global economy	323
9.7.1.	Tax competition and its impact on tax policy formulation	323
9.7.2.	The role of domestic law measures and tax treaties in attracting inward investment	324
9.7.3.	Measures against cross-border aggressive tax planning	325
9.8.	Good governance	326
9.8.1.	Access of the tax administration to information	326
9.8.2.	The next steps in international cooperation	327
9.8.3.	Tax compliance and good corporate governance	328
<b>Chapter 10: Germany</b>		<b>329</b>
	<i>Gert Müller-Gatermann</i>	
10.0.	Introduction	329
10.1.	Trends in tax policy as from 2000	330
10.1.1.	Personal income tax	330
10.1.1.0.	Introduction	330
10.1.1.1.	Discussion of a flat tax	330
10.1.1.2.	Discussion of dual income tax	331
10.1.1.3.	Broadening the tax base	331
10.1.1.4.	Taxation of retirement income	333
10.1.1.5.	Change in the rate structure	333
10.1.1.6.	From synthetic income tax to scheduler taxation	334
10.1.1.7.	From imputation to the classical system	336

## Table of Contents

---

10.1.1.8.	Taxation of private capital gains	337
10.1.1.9.	Taxable entity	337
10.1.2.	Corporate income tax	338
10.1.2.1.	Broadening of the tax base	338
10.1.2.2.	Discussion of a uniform business tax	339
10.1.2.3.	Changes in rate or structure	342
10.1.2.4.	Adaptation to international accounting standards	342
10.1.2.5.	Taxation of foreign income	343
10.1.2.6.	Option for alternative (simplified) tax base	343
10.1.3.	Trade tax	343
10.1.4.	VAT	345
10.1.4.0.	Introduction	345
10.1.4.1.	Tax rate changes	346
10.1.4.2.	Measures to combat fraud	347
10.1.4.3.	Adaptation to Community law	347
10.1.4.4.	Electronic communication	348
10.1.5.	Taxes on capital	348
10.1.6.	Inheritance and gift tax	349
10.1.7.	Real property transfer tax	349
10.1.8.	Motor vehicle tax	350
10.1.9.	Excises	350
10.1.10.	Environmental taxes	351
10.1.11.	Social security contributions and bank levy	351
10.2.	Main drivers of tax reforms since 2000	352
10.3.	Drafting and reviewing tax legislation and regulations	355
10.4.	Building up tax expertise	356
10.5.	The changing relationship between tax administrations and taxpayers	356
10.6.	Major players in tax policy	360
10.7.	Tax policy in the global economy	362
10.8.	Good governance	363

<b>Chapter 11: Italy</b>	<b>365</b>
<i>Alessandro Turina</i>	
11.1. Trends in tax policy as from 2000	365
11.1.1. Personal income tax	365
11.1.2. Corporate income tax	367
11.1.3. Other business taxes	369
11.1.4. VAT	370
11.1.5. Excises	371
11.1.6. Recurrent taxes on capital	371
11.1.7. Non-recurrent taxes on capital	374
11.1.8. Social security contributions	376
11.1.9. Environmental taxes	376
11.2. Main drivers of tax reforms since 2000	377
11.2.1. Objectives of tax reforms	377
11.2.2. Role of tax reform commissions and academia	378
11.2.3. Monitoring tax expenditures	379
11.3. Drafting and reviewing tax legislation and regulations	380
11.4. Building up tax expertise	382
11.5. The changing relationship between tax administrations and taxpayers	384
11.5.1. Taxpayer's rights	384
11.5.2. Legal sanctions	385
11.5.3. Avenues of appeal	386
11.5.4. Judicial fora for tax disputes	390
11.5.5. Taxpayer's expenses in court proceedings	390
11.5.6. Promoting cooperative relationship between tax administration and large taxpayers	392
11.5.7. Providing certainty for taxpayers	393
11.5.8. Retroactivity of tax legislation	393
11.5.9. Anti-abuse measures	394
11.5.10. Measuring the performance of the tax administration	396
11.6. Major players in tax policy	397
11.7. Tax policy in a global economy	399
11.7.1. Competitiveness of the Italian tax system	399
11.7.2. Measures against aggressive tax planning	401

## Table of Contents

---

11.8.	Good governance	402
11.8.1.	Exchange of information	402
11.8.2.	Cooperation with other law enforcement agencies	405
11.8.3.	Italian tax treaty policy	407
11.8.4.	Tax and corporate governance issues	408
<b>Chapter 12:</b>	<b>Netherlands</b>	411
	<i>Sigrid J.C. Hemels</i>	
12.1.	Trends in tax policy as from 2000	411
12.1.1.	Personal income taxes	411
12.1.2.	Corporate income taxes	413
12.1.3.	Value added tax	414
12.1.4.	Excises	415
12.1.5.	Recurrent taxes on capital	416
12.1.6.	Non-recurrent taxes on capital	416
12.1.7.	Compulsory social security contributions paid to government	417
12.1.8.	Environmental taxes	417
12.2.	Main drivers of tax reforms since 2000	418
12.3.	Drafting and reviewing tax legislation and regulations	421
12.4.	Building up tax expertise	423
12.5.	The changing relationship between tax administrations and taxpayers	424
12.6.	Major players in tax policy	426
12.7.	Tax policy in the global economy	427
12.8.	Good governance	429
<b>Chapter 13:</b>	<b>New Zealand</b>	433
	<i>Adrian J. Sawyer and Andrew M.C. Smith</i>	
13.0.	Introduction	433
13.1.	Trends in tax policy as from 2000	433
13.1.0.	Introduction	433

13.1.1.	Personal income taxes	434
13.1.2.	Corporate income taxes	435
13.1.3.	Value added tax (GST)	436
13.1.4.	Excises	436
13.1.5.	Environmental taxes	436
13.1.6.	Other taxes	436
13.2.	Main drivers of tax reforms since 2000	437
13.2.1.	Main drivers of tax reforms since 2000	437
13.2.2.	Government tax reform commissions	438
13.2.3.	Independent research institutes	439
13.2.4.	Tax expenditure budget	439
13.2.5.	Assessment of tax reform	439
13.3.	Drafting and reviewing tax legislation and regulations	440
13.4.	Building up tax expertise	443
13.5.	The changing relationship between tax administrations and taxpayers	444
13.6.	Major players in tax policy	449
13.7.	Tax policy in the global economy	453
13.8.	Good governance	456
13.9.	Conclusion	458
<b>Chapter 14:</b>	<b>Norway</b>	459
	<i>Frederik Zimmer, Anna B. Scapa Passalacqua and Lars A. Henie</i>	
14.1.	Trends in tax policy as from 2000	459
14.1.1.	Personal income taxes	459
14.1.1.1.	The 1992 tax reform	459
14.1.1.2.	The 2006 tax reform	459
14.1.2.	Corporate income taxes	461
14.1.2.1.	Rate	461
14.1.2.2.	The 2004 tax reform	461
14.1.2.3.	Timing rule	462
14.1.2.4.	Exit taxation rules	463

## Table of Contents

---

14.1.3.	Value added tax	463
14.1.4.	Excises	464
14.1.5.	Recurrent taxes on capital	465
14.1.6.	Non-recurrent taxes on capital	466
14.1.7.	Compulsory social security contributions paid to government	466
14.1.8.	Environmental taxes	467
14.1.9.	Other taxes	468
14.2.	Main drivers of tax reforms since 2000	468
14.2.1.	Main drivers of tax reforms since 2000	468
14.2.1.1.	General remarks	468
14.2.1.2.	Secure public revenue	469
14.2.1.3.	Achieve a fair tax system	469
14.2.1.4.	Redistribute wealth	469
14.2.1.5.	Achieve a better environment	470
14.2.1.6.	Promote employment throughout the entire country	470
14.2.1.7.	Provide a competitive tax system	470
14.2.1.8.	Achieve simplicity	471
14.2.1.9.	Transparency	471
14.2.1.10.	Dealing with external constraints	471
14.2.2.	Major tax reform commissions	472
14.2.3.	Influence of independent research institutes and universities on reforms	472
14.2.4.	Tax expenditures budget	473
14.2.5.	Data available to assess the impact of tax reforms	475
14.3.	Drafting and reviewing tax legislation and regulations	475
14.3.1.	Drafting of tax law provisions	475
14.3.2.	The influence of outside stakeholders	475
14.3.3.	Drafting procedure for secondary instruments	476
14.3.4.	Influence of secondary law in the design of tax policy	477
14.3.5.	Consistency of tax law proposals with higher-ranking law	477
14.4.	Building up tax expertise	477
14.4.1.	Formal training	477
14.4.2.	Professional qualifications	478
14.4.3.	Verification of qualifications	478
14.4.4.	Drafting of tax law	478
14.4.5.	Improvement possibilities by universities	479

14.5.	The changing relationship between tax administrations and taxpayers	479
14.5.1.	Enactment of taxpayers' rights	479
14.5.2.	Connection between taxpayers' rights and human rights	480
14.5.3.	Legal sanctions	480
14.5.4.	Appeals procedures	481
14.5.5.	Reimbursement of expenses	482
14.5.6.	Overall relationship between tax administration, taxpayers and their advisors	482
14.5.7.	Measures to provide greater certainty to taxpayers	482
14.5.8.	Major tax measures to protect the corporate tax base	484
14.5.9.	Retroactive tax legislation	484
14.5.10.	Social prestige of tax officials; corruption	485
14.5.11.	Measures of success of the tax administration	485
14.6.	Major players in tax policy	485
14.6.1.	Formal procedure for changes of tax law	485
14.6.2.	Relative influence on tax policy formulation	486
14.6.3.	Taxes used for social engineering purposes	486
14.6.4.	The role of academia and interest groups	486
14.6.5.	Membership in the EEA and other international organizations	487
14.6.6.	Specialized bodies to provide objective data	487
14.7.	Tax policy in the global economy	488
14.7.1.	Considerations of competition	488
14.7.2.	Policies regarding outward and inward investments	488
14.7.3.	Measures to reduce aggressive cross-border planning	489
14.7.4.	Transition time for tax reforms	489
14.8.	Good governance	490
14.8.1.	Access to information	490
14.8.2.	Good tax compliance and good corporate governance	491
<b>Chapter 15:</b>	<b>Poland</b>	493
	<i>Alicja Brodzka and Krzysztof Biernacki</i>	
15.1.	Trends in tax policy as from 2000	493
15.1.1.	Personal income tax	493
15.1.2.	Corporate income tax	494
15.1.3.	Other business taxes	495
15.1.4.	Value added tax	496

## Table of Contents

---

15.1.5.	Excises	497
15.1.6.	Recurrent taxes on capital	497
15.1.7.	Non-recurrent taxes on capital	498
15.1.8.	Compulsory social security contributions paid to government	498
15.1.9.	Environmental taxes	499
15.1.10.	Other taxes	500
15.2.	Main drivers of tax reforms since 2000	500
15.3.	Drafting and reviewing tax legislation and regulations	501
15.4.	Building up tax expertise	503
15.5.	The changing relationship between tax administrations and taxpayers	504
15.5.1.	Taxpayers' rights	504
15.5.2.	Legal sanctions and tax proceedings	505
15.5.3.	Measures to provide certainty to taxpayers and to protect the corporate tax base	506
15.5.4.	The relations between tax authorities, taxpayers and their advisors	508
15.5.5.	The social prestige of tax officials and the success measures of the tax administration	509
15.6.	Major players in tax policy	510
15.6.1.	Taxes and social engineering	510
15.6.2.	The role of interest groups and their influence on tax policy decisions	511
15.6.3.	The role of international and regional organizations in influencing Poland's tax policy	512
15.7.	Tax policy in the global economy	514
15.7.1.	Competitive considerations in Poland's tax policy	514
15.7.2.	Poland's tax arrangements and tax incentives	515
15.7.3.	Measures to reduce cross-border aggressive tax planning	517
15.8.	Good governance	517
15.8.1.	The result of the G20 tax transparency initiative	517
15.8.2.	Future steps in international cooperation	521
15.8.3.	Strengthening the link between good tax compliance and good corporate governance	523



<b>Chapter 16: Russia</b>	<b>527</b>
<i>Danil V. Vinnitskiy and Evgeniy Pustovalov</i>	
16.1. Trends in tax policy as from 2000	527
16.1.0. Introduction	527
16.1.1. Personal income taxes	527
16.1.2. Corporate income tax	528
16.1.3. Other business taxes	528
16.1.4. Value added tax	528
16.1.5. Excises	529
16.1.6. Recurrent taxes on capital	529
16.1.7. Non-recurrent taxes on capital	530
16.1.8. Compulsory social security contributions paid to government	530
16.1.9. Environmental taxes	531
16.1.10. Other taxes	531
16.2. Main drivers of tax reforms since 2000	532
16.2.1. General background	532
16.2.2. Group of experts	532
16.2.3. Coordination of tax reform	533
16.2.4. Tax expenditures	533
16.2.5. Information about the course of tax reform	533
16.3. Drafting and reviewing tax legislation and regulations	534
16.3.1. Legislative initiative	534
16.3.2. Public discussions	535
16.3.3. Secondary instruments	536
16.3.4. Doctrinal concepts	537
16.3.5. The role of the domestic constitutional law and international treaties	537
16.4. Building up tax expertise	538
16.4.1. Professional training	538
16.4.2. Attestation of the officials	538
16.4.3. Federal educational standards	539
16.4.4. The role of Russian law universities	539
16.5. The changing relationship between tax administrations and taxpayers	540
16.5.1. Taxpayers' rights and practice	540
16.5.2. Taxpayers' rights and human rights	540

16.5.3.	Legal sanctions	541
16.5.4.	Right to appeal	541
16.5.5.	Right to compensation	542
16.5.6.	The development of the relationship between tax administration, taxpayers and their consultants	542
16.5.7.	Measures to provide greater certainty	543
16.5.8.	Measures to protect the corporate tax base	544
16.5.9.	Prohibition of retroactivity	544
16.5.10.	Social prestige and risks of corruption	545
16.5.11.	Official statistics	545
16.6.	Major players in tax policy	545
16.6.1.	Rules and procedures	545
16.6.2.	Major players	546
16.6.3.	The role of the Ministry of Finance	547
16.6.4.	Academia, media and business associations	547
16.6.5.	Principle of tax sovereignty	547
16.6.6.	International and global factors	548
16.6.7.	Efficiency monitoring	548
16.7.	Tax policy in the global economy	549
16.7.1.	Competitive considerations	549
16.7.2.	The concept of neutrality in tax policy	549
16.7.3.	Tax sparing arrangements	550
16.7.4.	Measures to reduce aggressive cross-border tax planning	550
16.7.5.	Tax-related barriers to inward investment	550
16.7.6.	Tax reforms and transition periods	550
16.8.	Good governance	551
16.8.1.	Access to tax information	551
16.8.2.	Good governance and the development of international cooperation	551
<b>Chapter 17:</b>	<b>South Africa</b>	<b>553</b>
	<i>Jennifer Roeleveld, Craig West and Riël Franzsen</i>	
17.1.	Trends in tax policy as from 2000	553
17.1.0.	Introduction	553
17.1.1.	Personal income taxes	553
17.1.2.	Corporate income taxes	554
17.1.3.	Other business taxes	556

17.1.4.	Value added tax	556
17.1.5.	Excises	557
17.1.6.	Recurrent taxes on capital	557
17.1.7.	Non-recurrent taxes on capital	558
17.1.8.	Compulsory social security contributions paid to government	559
17.1.9.	Environmental taxes	559
17.1.10.	Other taxes	560
17.2.	Main drivers of tax reforms since 2000	561
17.2.1.	Main drivers of tax reforms since 2000	561
17.2.1.1.	Addressing the legacies of the past and the dictates of a constitutional state	561
17.2.1.2.	Reducing tax rates of personal and corporate income taxes	561
17.2.1.3.	Improved tax administration and international cooperation	561
17.2.1.4.	Reducing the compliance burden for small and medium-sized enterprises	562
17.2.1.5.	Curbing impermissible tax avoidance and regulating tax practitioners	562
17.2.1.6.	Sub-national taxation	562
17.2.1.7.	Regional tax issues	563
17.2.2.	Major tax reform commissions and their impact	564
17.2.3.	Independent research institutes and universities' impact on tax reforms	564
17.2.4.	Tax expenditures analysis and the impact on tax reform	565
17.2.5.	Assessment of the impact of the tax reforms	565
17.3.	Drafting and reviewing tax legislation and regulations	566
17.3.1.	Drafting of tax law provisions	566
17.3.2.	Consultation and comment on draft legislation	566
17.3.3.	Drafting policy for secondary instruments	567
17.3.4.	Influence of secondary law in the design of tax policy	567
17.3.5.	Testing consistency with constitutional law and international agreements	567
17.4.	Building up tax expertise	568
17.4.1.	Formal training for the tax profession	568
17.4.2.	Professional qualifications of tax practitioners	568
17.4.3.	Verification of the qualifications and continuing education of tax professionals	569

17.4.4.	The drafting of tax legislation	569
17.5.	The changing relationship between tax administrations and taxpayers	570
17.5.1.	Taxpayers' rights and application	570
17.5.2.	Human rights	570
17.5.3.	Legal sanctions	571
17.5.4.	Objection and appeal	571
17.5.5.	Legal costs and awards	574
17.5.6.	The relationship between tax administration, taxpayers and their advisors	574
17.5.7.	Measures to provide greater legal certainty to taxpayers	575
17.5.8.	Protection of the corporate tax base	575
17.5.9.	Retroactive tax legislation	575
17.5.10.	Status of tax officials	576
17.5.11.	Measuring the success of the revenue authority	576
17.6.	Major players in tax policy	576
17.6.1.	Process for legislative amendment	576
17.6.2.	Influence on tax policy formulation by other parties	577
17.6.3.	Taxes and social engineering	577
17.6.4.	The role of academia, media, trade unions, associations of employers or other interest groups	577
17.6.5.	The role of international and regional organizations	578
17.6.6.	The influence of government on the international debates	578
17.6.7.	Specialized bodies for objective data on public finances	578
17.7.	Tax policy in the global economy	579
17.7.1.	Tax competition perspectives	579
17.7.2.	Harmful tax competition versus "smart tax competition"	579
17.7.3.	Policy effects on outward investment versus inward investment	580
17.7.4.	Tax treaties and inward investment	580
17.7.5.	Impact of tax incentives and tax sparing arrangements on inward investment	580
17.7.6.	Measures to reduce cross-border aggressive tax planning	581
17.7.7.	Base erosion and profit shifting	581

17.7.8.	Barriers to inward investment	581
17.7.9.	Transitional rules for major reforms	581
17.8.	Good governance	582
17.8.1.	Access to information	582
17.8.1.1.	Overcoming the main barriers to the effective use of information	582
17.8.1.2.	The main risks posed by information exchange	582
17.8.1.3.	Increased and effective cooperation between tax administrations and third parties	582
17.8.2.	Improving international cooperation	583
17.8.2.1.	The move from bilateral to multilateral treaties	583
17.8.2.2.	Supplementing exchange on request with automatic exchange of information	583
17.8.2.3.	Moving from cooperation to tax coordination	584
17.8.3.	Actions to strengthen ties between countries	584
17.8.3.1.	Selection of treaty partners	584
17.8.3.2.	Regional organizations	584
17.8.4.	Strengthening the linkage between good tax compliance and good corporate governance	584
17.8.4.1.	The corporate governance agenda	584
17.8.4.2.	Tax strategy and its impact on financial and reputation risk for corporations	585
17.8.4.3.	Compliance of multinational enterprises with the spirit and the letter of the law	585
<b>Chapter 18:</b>	<b>Spain</b>	<b>587</b>
	<i>Domingo Jiménez-Valladolid de L'Hotellerie-Fallois, César Martínez Sánchez and Félix Alberto Vega Borrego</i>	
18.1.	Trends in tax policy as from 2000	587
18.1.1.	Personal income taxes	587
18.1.2.	Corporate income tax	588
18.1.3.	Other business taxes	589
18.1.4.	Value added tax	589
18.1.5.	Excises	590
18.1.6.	Recurrent taxes on capital	590
18.1.7.	Non-recurrent taxes on capital	591
18.1.8.	Compulsory social security contributions paid to government	591
18.1.9.	Environmental taxes	591

18.1.10.	Other taxes	591
18.2.	Main drivers of tax reforms since 2000	592
18.2.1.	Main drivers of tax reforms since 2000	592
18.2.2.	Tax reform commissions	592
18.2.3.	Influence of independent research institutes, universities and interest groups on the tax reforms	593
18.2.4.	Measuring tax expenditures	594
18.2.5.	Assessment of the impact of tax reforms	594
18.3.	Drafting and reviewing tax legislation and regulations	595
18.3.1.	Drafting of tax law provisions	595
18.3.2.	Consultation with outside stakeholders	595
18.3.3.	Drafting of secondary instruments of tax policy	596
18.3.4.	Influence of secondary law in the design of tax policy	596
18.3.5.	Verifying the compliance of proposals with higher-ranking laws	596
18.4.	Building up tax expertise	597
18.4.1.	Training for tax professionals	597
18.4.2.	Professional qualifications available	597
18.4.3.	Verification of the qualifications of professionals working in the tax area	598
18.4.4.	Training for the drafting of tax law	599
18.4.5.	The role of universities in training tax professionals	600
18.5.	The changing relationship between tax administrations and taxpayers	600
18.5.1.	Taxpayers' rights	600
18.5.2.	Taxpayers' rights and human rights	601
18.5.3.	Legal sanctions	602
18.5.4.	Appeals	602
18.5.5.	Reimbursement of taxpayer's expenses in court proceedings	602
18.5.6.	Relationship between tax administration, taxpayers and their advisors	603
18.5.7.	Measures to provide greater certainty to taxpayers	604
18.5.8.	Measures to protect the corporate tax base	604
18.5.9.	Retroactive tax legislation	605
18.5.10.	Social prestige of tax officials	606
18.5.11.	Official measures of the success of the tax administration	606

18.6.	Major players in tax policy	607
18.6.1.	Procedure for changes of tax law	607
18.6.2.	Influence of public officials in the Ministry of Finance and in other ministries	607
18.6.3.	Influence of interest groups	608
18.6.4.	Influence of international organizations	608
18.6.5.	Objective data on public finances and the impact of any tax reform	609
18.7.	Tax policy in the global economy	609
18.7.1.	Competitive considerations in tax policy	609
18.7.2.	Outward and inward investment	610
18.7.3.	Tax incentives and tax sparing	611
18.7.4.	Measures against aggressive tax planning and base erosion and profit shifting	612
18.7.5.	Transition time in introducing new tax rules	613
18.8.	Good governance	613
18.8.1.	Exchange of information and limits on the use of information obtained	613
18.8.2.	Next steps in international cooperation	614
18.8.3.	Other actions to strengthen ties between countries	615
18.8.4.	Strengthening the link between good tax compliance and good corporate governance	616
<b>Chapter 19:</b>	<b>Sweden</b>	617
	<i>Björn Westberg</i>	
19.1.	Trends in tax policy as from 2000	617
19.1.1.	Personal income taxes	617
19.1.2.	Corporate income tax	620
19.1.3.	Taxation of shipping	622
19.1.4.	Value added tax	622
19.1.5.	Excises	623
19.1.6.	Recurrent taxes on capital	623
19.1.7.	Non-recurrent taxes on capital	624
19.1.8.	Compulsory social security contributions paid to government	624
19.1.9.	Environmental taxes	624
19.1.10.	Other taxes	625
19.2.	Main drivers of tax reforms since 2000	625

19.2.1.	Main drivers of tax reforms since 2000	625
19.2.2.	Independent research institutes and universities	625
19.2.3.	Measuring tax expenditures	625
19.2.4.	Public evaluations	626
19.3.	Drafting and reviewing tax legislation and regulations	626
19.3.1.	Tax commissions	626
19.3.2.	Availability and circulation of government proposals	626
19.3.3.	Drafting of secondary instruments	627
19.3.4.	Legislation and the issue of binding and non-binding decrees	628
19.3.5.	Law Commission	629
19.4.	Building up tax expertise	629
19.5.	The changing relationship between tax administrations and taxpayers	631
19.5.1.	Taxpayers' rights	631
19.5.2.	Legal sanctions	631
19.5.3.	Appeal of assessments	632
19.5.4.	Reimbursement of costs to taxpayers	633
19.5.5.	Relationship between tax administration and taxpayers	634
19.5.6.	Tax rulings	634
19.5.7.	Protection of the corporate tax base	635
19.5.8.	Constitutional prohibition on retroactivity	636
19.5.9.	The social prestige of tax officials	636
19.6.	Major players in tax policy	637
19.6.1.	The Parliamentary Committee for Fiscal Affairs	637
19.6.2.	The role of the Minister of Finance	637
19.6.3.	Influence of NGOs	638
19.6.4.	Influence of public opinion	638
19.6.5.	International and regional cooperation	638
19.6.6.	Independent expert studies	639
19.7.	Tax policy in the global economy	639
19.7.1.	Competitive considerations	639
19.7.2.	Tax incentives	640
19.7.3.	Measures to reduce aggressive tax planning	640
19.7.4.	The base erosion and profit shifting project	641
19.7.5.	Tax-related barrier to inward investment	642
19.7.6.	Transitional periods for new legislation	642



19.8.	Good governance	642
19.8.1.	The G20 tax transparency initiative	642
19.8.2.	Bilateral or multilateral conventions?	643
19.8.3.	Priorities in respect of treaty negotiations	643
19.8.4.	The importance of good tax compliance	644
<b>Chapter 20:</b>	<b>United Kingdom</b>	<b>645</b>
	<i>Christopher John Wales and Caroline Turnbull-Hall</i>	
20.1.	Trends in tax policy as from 2000	645
20.1.0.	Introduction	645
20.1.1.	Personal income taxes	645
20.1.2.	Corporate income taxes	647
20.1.3.	Other business taxes	647
20.1.4.	Value added tax	648
20.1.5.	Excise duties	648
20.1.6.	Recurrent taxes on capital	648
20.1.7.	Non-recurrent taxes on capital	648
20.1.8.	Compulsory social security contributions paid to government	649
20.1.9.	Environmental taxes	649
20.1.10.	Other measures	649
20.2.	Main drivers of tax reforms since 2000	650
20.2.1.	Main drivers of tax reforms since 2000	650
20.2.2.	Tax reform commissions and their influence	651
20.2.3.	Influence of independent research institutes and universities on reforms	652
20.2.4.	The United Kingdom's tax expenditures budget	653
20.2.5.	Available data to assess the impact of tax reforms	653
20.3.	Drafting and reviewing tax legislation and regulations	654
20.3.1.	Drafting tax law	654
20.3.2.	Opportunities for outside stakeholders to comment on draft legislation	654
20.3.3.	The drafting procedure for secondary instruments	655
20.3.4.	The influence of secondary law in the design of tax policy	656
20.3.5.	The process for verifying that the proposals are consistent with constitutional law, European law (if applicable), etc.	656

20.4.	Building up tax expertise	656
20.4.1.	Formal training for new entrants to the tax profession	656
20.4.2.	Professional qualifications available to tax practitioners	657
20.4.3.	Verification of the qualifications of professionals working in the tax area	658
20.4.4.	Drafting tax law as an academic subject	658
20.4.5.	The impact of universities on the drafting of tax statute	658
20.5.	The changing relationship between tax administrations and taxpayers	659
20.5.1.	Taxpayers' rights in the United Kingdom	659
20.5.2.	The interaction of taxpayers' rights and human rights	660
20.5.3.	Legal sanctions for tax	660
20.5.4.	Avenues of appeal against decisions made by HMRC	663
20.5.5.	Procedure for the reimbursement of the taxpayer's expenses in court proceedings	664
20.5.6.	The overall relationship between tax administration, taxpayers and their advisors	664
20.5.7.	Measures implemented by HMRC to provide greater certainty to taxpayers	665
20.5.8.	Major measures to protect the corporate tax base	666
20.5.9.	Retroactive tax legislation	667
20.5.10.	The social prestige and pay of tax officials	668
20.5.11.	Official measures of the success of tax administrations	669
20.6.	Major players in tax policy	669
20.6.1.	The formal procedure for changes of tax law	669
20.6.2.	The influence on tax policy formulation of political parties, lobbying groups, etc.	670
20.6.3.	The use of taxes for social change	671
20.6.4.	The role of academia, media, trade unions, associations of employers or other interest groups	671
20.6.5.	The adoption of measures which are seen as not being in the long-term interests of the United Kingdom	672
20.6.6.	The role of international and regional organizations in influencing tax policy	672
20.6.7.	The government's role in international debates	672
20.6.8.	Bodies established by government to provide objective data on public finances and the impact of any tax reform	673

20.7.	Tax policy in the global economy	674
20.7.1.	The importance of competitive considerations in influencing the United Kingdom's tax policy	674
20.7.2.	The United Kingdom and "smart tax competition"	674
20.7.3.	The balance between outward investment and inward investment	675
20.7.4.	The importance of tax treaties in attracting inward investment	675
20.7.5.	The role of tax incentives and tax sparing arrangements in attracting inward investment	675
20.7.6.	UK measures to reduce cross-border aggressive tax planning	676
20.7.7.	The top three tax-related barriers to inward investment	676
20.7.8.	Transition time for business to adapt to new tax measures	677
20.8.	Good governance	677
20.8.1.	Unparalleled access to information by tax administrations	677
20.8.2.	What are the next steps in improved international cooperation?	678
20.8.3.	Other actions to strengthen ties between countries	679
20.8.4.	Strengthening the linkage between good tax compliance and good corporate governance	679
Part Three		
<b>Chapter 21:</b>	<b>Burundi</b>	683
	<i>Thomas Dubut</i>	
21.0.	Introduction	683
21.1.	Trends of the recent Burundi tax reform	684
21.1.1.	Main drivers of the tax reform in Burundi	684
21.1.2.	Basic features of the tax reform in Burundi	685
21.1.2.1.	Direct taxation	685
21.1.2.2.	Indirect taxation	687
21.1.2.3.	Tax procedures	688
21.2.	Players in Burundi tax policy	688
21.2.1.	Players in the drafting process	688
21.2.2.	Funding of the global tax reform in Burundi	689
21.3.	Conclusion	690

<b>Chapter 22: Chile</b>	693
<i>Felipe Yañez and Cristián Gárate</i>	
22.0. Introduction – The Chilean tax system	693
22.1. Personal income taxes	695
22.2. Corporate income taxes	696
22.3. VAT	700
22.4. Excises	701
22.5. Recurrent taxes on capital	702
22.6. Compulsory social security contributions paid to government	702
22.7. Natural resources tax	702
22.8. Conclusion	703
<b>Chapter 23: Finland</b>	705
<i>Kristiina Äimä and Kenneth Hellsten</i>	
23.0. Introduction	705
23.1. Taxation of earned income	705
23.2. Household credit	706
23.3. Taxation of corporations and shareholders	706
23.4. Capital gains on fixed assets	707
23.5. Transfer pricing documentation	708
23.6. Interest deduction limitation rules	708
23.7. Tax incentives	709
23.7.1. Additional deduction for research and development	709
23.7.2. Research, development and innovation box	709

---

23.8.	VAT	709
23.9.	Excises	711
23.10.	Recurrent taxes on capital	711
23.11.	Non-recurrent taxes on capital	712
23.12.	Other taxes	712
<b>Chapter 24:</b>	<b>Greece</b>	715
	<i>Katerina Pantazatou</i>	
24.0.	Introduction	715
24.1.	Personal income taxes	716
24.2.	Corporate income taxes	718
24.3.	VAT	718
24.4.	Excises	719
24.5.	Recurrent taxes on capital	719
24.6.	Non-recurrent taxes on capital	720
24.7.	Compulsory social security contributions paid to government	720
24.8.	Environmental taxes	721
24.9.	Conclusion	722
<b>Chapter 25:</b>	<b>Hungary</b>	723
	<i>Borbála Kolozs</i>	
25.0.	Introduction	723
25.1.	Description of Hungarian tax policy	723
25.2.	Personal income tax	726

25.3.	Corporate income tax	728
<b>Chapter 26: Lithuania</b>		731
	<i>Ramūnas Riazanskis and Maryte Somare</i>	
26.0.	Introduction	731
26.1.	Personal income taxes	732
26.2.	Corporate income taxes	733
26.3.	VAT	734
26.4.	Excise duties	735
26.5.	Wealth taxes and taxes on capital	736
26.6.	Social security contributions	737
26.7.	Environmental taxes	738
<b>Chapter 27: Luxembourg</b>		739
	<i>Anne Selbert and Katharina Schiffmann</i>	
27.0.	Introduction	739
27.1.	Personal income tax	739
27.1.1.	Final withholding tax on interest income (for resident and non-resident individuals)	739
27.1.2.	Special expat tax regime	740
27.1.3.	Fund manager's carried interest regime	741
27.1.4.	Crisis contribution	741
27.1.5.	Abolishment of net wealth tax for individuals	742
27.2.	Corporate income tax	742
27.2.1.	Common tax regime	742
27.2.1.1.	Decreasing tax rate and minimum income tax	742
27.2.1.2.	Abolishment of the capital duty	743
27.2.2.	Specific activity regimes	743
27.2.2.1.	Transfer pricing practice	743
27.2.2.2.	Intellectual property regime	744

	27.3. Value added tax	744
	27.3.1. Introduction	744
	27.3.2. E-books	745
	27.3.3. E-services and VAT	745
	27.4. Other taxes	746
	27.4.1. Environmental taxes	746
	27.4.2. Excises	746
	27.4.3. Social security contributions	746
	27.4.4. Inheritance tax and gift tax	746
	<b>Chapter 28: Mexico</b>	749
	<i>Daniel Fuentes</i>	
	28.0. Introduction	749
	28.1. Corporate tax amendments in the period from 2000 to 2006	750
	28.2. Corporate tax amendments in the period from 2006 to 2012	752
	28.3. Corporate tax amendments in the period from 2012 to date	754
	<b>Chapter 29: Peru</b>	757
	<i>Cecilia Delgado Ratto</i>	
	29.0. Introduction	757
	29.1. Personal income tax	758
	29.2. Corporate income tax	758
	29.3. Indirect taxes	759
	29.4. Taxes on capital	759
	29.5. Other taxes	760

29.6.	The changing relationship between tax administrations and taxpayers	760
29.7.	Tax policy in the global economy	761
<b>Chapter 30: Portugal</b>		<b>763</b>
	<i>Miguel Cortez Pimentel</i>	
30.1.	The Portuguese tax system in 2014	763
30.2.	Brief policy analysis (2000-2012)	766
30.3.	Developments and ongoing tax reform	770
30.3.1.	Corporate income tax	770
30.3.2.	Personal income tax	771
30.3.3.	VAT and other taxes	772
30.4.	A note on tax (good) governance	772
<b>Chapter 31: Romania</b>		<b>775</b>
	<i>Ciprian Adrian Păun and Dragoș Păun</i>	
31.1.	Personal income tax	775
31.2.	Corporate income tax	775
31.3.	Value added tax	777
31.4.	Compulsory social security contributions paid to government	779
31.5.	Pension system in Romania	780
<b>Chapter 32: Serbia</b>		<b>781</b>
	<i>Svetislav V. Kostić</i>	
32.0.	Introduction	781
32.1.	Personal income taxes	782
32.2.	Corporate income taxes	784



---

32.3.	Value added tax	785
32.4.	Excises	785
32.5.	Recurrent taxes on capital	786
32.6.	Non-recurrent taxes on capital	786
32.7.	Compulsory social security contributions paid to government	787
32.8.	Conclusion	788
<b>Chapter 33:</b>	<b>Slovenia</b>	789
	<i>Sabina Taškar Beloglavec and Lidija Hauptman</i>	
33.0.	Introduction	789
33.1.	Personal income taxes	790
33.2.	Corporate income taxes	791
33.3.	Other business taxes	792
33.4.	VAT	792
33.5.	Excises	793
33.6.	Recurrent taxes on capital	794
33.7.	Non-recurrent taxes on capital	795
33.8.	Compulsory social security contributions paid to government	796
33.9.	Environmental taxes	797
33.10.	Other taxes	797
33.11.	Conclusions	798

<b>Chapter 34: Turkey</b>	799
<i>Leyla Ateş</i>	
34.0. Introduction	799
34.1. Indirect tax reform	800
34.2. Direct tax reform	800
34.3. Tax incentives reform	802
34.4. Tax administration reform	804
34.5. Conclusion	805
<b>List of Contributors</b>	807

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## Preface

Understanding the major trends in tax policy around the world is of great relevance not only for researchers, but also for tax policy makers, government officials and tax practitioners active in the field of national and international tax law. Accordingly, the main purpose of the research project the final result of which is this book was to analyse various aspects of national tax policies, including the main drivers of tax policy decisions, the players influencing such decisions and the translation of tax policy decisions in the legislative process in the different political and economic systems of the countries included in the project.

Although the focus is on national tax policies, this topic cannot be analysed in isolation from international and global aspects. In the past decade, the globalization of the economy has progressed at an unprecedented pace thereby presenting global challenges, among which has been the financial crisis, to governments around the world. Global issues require global answers. Therefore, the analysis included in this book extends not only to the way governments pursue their national tax policy goals but also to the various answers national tax policy makers give to global challenges.

The comparative analysis in this respect aims at pointing out similarities and differences in national tax policies reacting to common challenges and at identifying global trends. Throughout the book and in particular in the general report we have highlighted best practices that can be implemented by states around the world in the framework of voluntary compliance. The national implementation of global initiatives for coordination of tax policies and tax rules is also examined in a comparative perspective. Great attention is given to the change in the relationship between tax administrations and taxpayers from a strict authority approach to a more cooperative relationship, the role of “major players” in the formulation of tax policy decisions and tax legislation as well as aspects of good governance in international relations in the tax field.

More than a hundred experts, including the national reporters, participated in the Conference “Trends and Players in Tax Policy” from 4 to 6 July 2013 in Rust, Austria, which was hosted by the Institute for Austrian and International Tax Law of WU (Vienna University of Economics and Business) in cooperation with the Research Council of Norway.

We are very grateful for the contributions of all the national reporters and authors who tirelessly worked in order to deliver up-to-date reports. We would also like to thank them for their active participation in the discussions at the Conference.

IBFD agreed to include this book in its new WU Institute for Austrian and International Tax Law – European and International Tax Law and Policy Series. We would like to take the opportunity to express our sincere thanks to IBFD for its cooperation and the smooth carrying-out of the project; in particular we would like to thank Estela Ferreiro Serret, João Nogueira and Alessandro Turina. Ms Margaret Nettinga contributed greatly to the finalization of the book by editing and polishing the reports for the authors, for whom English is – to a great extent – a foreign language.

Our gratitude also goes to the members of the secretariat and the research staff of the Institute for Austrian and International Tax Law, especially Ms Renée Pestuka, Na Li, Alejandro Ruiz Jiménez, Lukas Mechtler, Nikolas Neubauer and Rita Szudoczky, who were responsible for the organization and preparation of the Conference in Rust as well as the publication of this book. Without their efforts and talent for organization, the success of the Conference and the completion of this book could not have been achieved.

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## Luxembourg\*

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### 27.0. Introduction

The Luxembourg tax system has been subject to several important changes in the past 10 years, influenced by the growing importance of European legislation and obviously by the economic crisis affecting Europe recently. However, Luxembourg has remained an attractive financial centre, also due to important changes in its tax system.

Below, the most important changes are outlined on the basis of the kind of tax.

### 27.1. Personal income tax

#### 27.1.1. Final withholding tax on interest income (for resident and non-resident individuals)

In the course of implementing the European Savings Directive (EUSD) in 2005, Luxembourg introduced a final withholding tax (WHT) on interest income accrued from 1 July 2005 and paid after 1 January 2006 for resident individuals by the law of 23 December 2005<sup>1</sup> (the “Relibi-Law”). Any Luxembourg paying agent paying interest to a beneficial owner who is resident in Luxembourg must apply a final WHT tax of 10%. This WHT can be deemed final, as no further tax is due on interest income by the resident. Furthermore, the interest income does not have to be reported in the taxpayer’s tax return and it is not taken into account when calculating the average rates of tax on the income. Interest that is only paid once a year on savings accounts and does not exceed EUR 250 per person and per paying agent is exempt from WHT.

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\* This contribution was finalized in the spring of 2014 and is current through that date.

1. The law of 23 December 2005 introducing a domestic withholding tax on certain interest income on interest payments (*Loi du 23 décembre 2005 portant introduction d’une retenue à la source sur certains intérêts par l’épargne mobilière*).

With the law of 21 June 2005<sup>2</sup> (the “EUSD Law”), Luxembourg implemented the EUSD (Council Directive 2003/48/EC) into domestic law. Under the EUSD Law, which has been in effect since 1 July 2005, Luxembourg levies a WHT on interest payments or other similar income paid by a paying agent within its jurisdiction to or for an individual resident in another EU Member State unless such individual agrees to an exchange of information regarding the interest or similar income it received between the tax authorities of Luxembourg and the relevant EU Member State. The rate of the WHT is equal to 35% from 1 July 2011.

Political announcements in April 2013 by the Luxembourg Prime Minister Jean-Claude Juncker already led to the assumption that the WHT option will be abolished. The Luxembourg draft bill No. 6668, which was submitted to the parliament on 18 March 2014, is purporting to finally abolish the withholding tax principle in order to introduce an automatic exchange of information regarding the payment of interest or similar income. The entry into force of this reform is expected to take place on 1 January 2015.

### 27.1.2. Special expat tax regime

A special regime for highly skilled and dedicated employees who are transferred to the Luxembourg office of a company group or who are directly recruited in a foreign country by a Luxembourg company (“LuxCo”) to work temporarily<sup>3</sup> in Luxembourg came into effect on 1 January 2011 through Circular No. 95/2.<sup>4</sup> On 27 January 2014, the Luxembourg tax authorities issued an update<sup>5</sup> to the original Circular No. 95/2.<sup>6</sup> The main change from 1 January 2014 is the extension of the scope of the tax regime to the benefit

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2. The law of 21 June 2005 on taxation of savings income in the form of interest payments, transposing the European Directive 2003/48/CE of 3 June 2003 into Luxembourg law (*Loi du 21 juin 2005 transposant en droit luxembourgeois la directive 2003/48/CE du 3 juin 2003 du Conseil de l’Union européenne en matière de fiscalité des revenus de l’épargne sous forme de paiement d’intérêts*).

3. The expatriate can benefit from the regime up to 5 calendar years following the year of arrival, provided the conditions mentioned in Circular No. 95/2 are met.

4. Circular of the Director of the tax authorities LITL No. 95/2 of 31 December 2010 (*Circulaire du directeur des contributions L.I.R. – n° 95/2 du 31 décembre 2010*).

5. Circular of the Director of the tax authorities LITL No. 95/2 of 27 January 2014 (*Circulaire du directeur des contributions L.I.R. – n° 95/2 du 27 janvier 2014*).

6. The original Circular was already updated by the Circular of the Director of the tax authorities LITL No. 95/2 of 21 May 2013 (*Circulaire du directeur des contributions L.I.R. – n° 95/2 du 21 mai 2013*), which provides all details and conditions to be fulfilled (e.g. the employee should satisfy a shortage of competent workers in Luxembourg, the employee meets minimum salary requirements (i.e. EUR 50,000 per year as

of the employees directly recruited abroad not only by companies established in Luxembourg but in any member state of the European Economic Area.

Employees falling under this special regime benefit from special tax deductions (e.g. costs of moving to Luxembourg and similar repatriation expenses at the end of the secondment, school fees associated with primary and secondary education) and tax reliefs but this is subject to an overall cap (e.g. home leave, costs associated with the difference in taxes between Luxembourg and the home country).

### 27.1.3. Fund manager's carried interest regime

The expat tax regime can be combined with the special tax regime on the remuneration of fund managers.<sup>7</sup> Usually, the remuneration of fund managers (i.e. carried interest) is governed by the Luxembourg Income Tax Law (LITL) and is in principle taxable as speculative capital gain (and not as income). The intended regime foresees a temporary reduced rate amounting to 25% of the average (i.e. in 2013, a marginal rate of 10.34%) provided that several conditions are fulfilled.

### 27.1.4. Crisis contribution

In the course of the economic crisis of the European Union, Luxembourg introduced a “crisis contribution” in 2010 to make its residents help balance the consequences of the economic and financial crisis.

A non-deductible tax was withheld at a rate of 0.8% on all categories of income of individual persons (also on replacement income like sickness benefits and unemployment benefits) for the tax year 2011 (even though it was originally foreseen to withhold such a tax in 2012 as well).<sup>8</sup>

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at 1 January 2013) and must not replace another non-expatriate employee) for the expat tax regime to apply.

7. The law of 12 July 2013 relating to managers of alternative investment funds transposing Directive 2011/61/EU of the European Parliament and of the Council on Alternative Investment Managers into Luxembourg law provides for a special regime on the remuneration of such fund managers.

8. With the law of 16 December 2011 on the budget of revenues and expenditures of the state for year 2012 (*Loi du 16 décembre 2011 concernant le budget des recettes et des dépenses de l'Etat pour l'exercice 2012*) Luxembourg abolished the crisis contribution for 2012 within the framework of signing an agreement on civil service reforms.

### 27.1.5. Abolishment of net wealth tax for individuals

The net wealth tax for individuals of 0.5% on their net assets was abolished from the tax year 2006 in the course of introducing the above-mentioned 10% WHT on interest income.

## 27.2. Corporate income tax

### 27.2.1. Common tax regime

#### 27.2.1.1. Decreasing tax rate and minimum income tax

Luxembourg's corporate income tax (CIT) rate and municipal business tax (MBT) rate have been constantly decreasing since 1999 from 37.45% down to 28.59% in 2010<sup>9</sup> (for companies situated in Luxembourg City).

Starting in 2011, Luxembourg introduced several measures to balance its national budget and public debt.<sup>10</sup> From 1 January 2011, the solidarity sur-tax<sup>11</sup> was increased from 4% to 5%, which has resulted in a rise of the total effective tax rate from 28.59% to 28.80%.

Furthermore, the above-mentioned measures also included the introduction of a minimum CIT of EUR 1,500 per fiscal year for Luxembourg residents, fully taxable corporate entities whose activity does not require a business licence and for which the sum of fixed financial assets, receivables on related entities, transferable securities and cash at bank exceeds 90% of their balance sheet<sup>12</sup> (i.e. the so-called Soparfi).

With effect from 1 January 2013, the minimum CIT for such corporations was increased to EUR 3,000 per annum and was extended to all other corporations (i.e. corporations other than the above-mentioned collective undertakings falling under the EUR 3,000 minimum CIT) having their registered seat or central administration in Luxembourg. For such other

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9. B. Höfer and C. Alter, *Luxembourg's Minimum Flat Tax for Corporations*, Tax Notes International, Vol. 61, No. 11 (2011), pp. 853-857.

10. Draft law No. 6166 of 30 July 2010 (*Projet de loi n° 6166 du 30 juillet 2010*, p. 2).

11. I.e. contribution to the Employment Fund.

12. Law of 17 December 2010 introducing tax measures relating to the financial and economic crisis (*Loi du 17 décembre 2010 portant introduction des mesures fiscales relatives à la crise financière et économique*, Mémorial A n° 247, 31 décembre 2010, p. 4095, article 2).



corporations the minimum CIT will range from EUR 500 to EUR 20,000 depending on the total balance sheet of the company.<sup>13</sup> Additionally, this was followed by an increase of the contribution made by corporations to the solidarity surtax from 5% to 7%. This increase resulted in a rise of the aggregate CIT payable from a rate of 28.80% to 29.22% (for Luxembourg City), even though the rate itself remained unchanged.

### 27.2.1.2. Abolishment of the capital duty

The law of 19 December 2008<sup>14</sup> abolished the capital duty (which was levied before at a rate of 0.5%<sup>15</sup> on the capital contributed to commercial and civil entities) in Luxembourg and replaced this with a fixed registration duty of EUR 75. This fixed capital duty applies for the incorporation of a LuxCo and for any amendments to the articles of incorporation of a LuxCo.

## 27.2.2. Specific activity regimes

### 27.2.2.1. Transfer pricing practice

In 2011, the tax authorities published two important circulars<sup>16</sup> (together, the “Transfer Pricing Circulars”) relating to the tax treatment of intra-group financing transactions at the level of affiliated companies.

Under Article 56 LITL and according to the transfer pricing guidelines of the Organisation for Economic Co-operation and Development (OECD), any activity carried out between related parties should be remunerated at arm’s length according to the functions performed. Specifically, under the Transfer Pricing Circulars, companies performing a back-to-back financing activity must realize an arm’s length margin on this activity.

13. Law of 21 December 2012 / Circular of the Director of the tax authorities LITL No. 174/1 of 1 August 2013 (*Loi du 21 décembre 2012*, Mémorial A n° 270, 28 décembre 2012, p. 3831, article 2 / *Circulaire du directeur des contributions L.I.R. – n° 174/1 du 1er août 2013*).

14. Law of 19 December 2008 (*Loi du 19 décembre 2008*, Mémorial A n° 207, 24 décembre 2008, p. 3136).

15. Such rate was decreased from 1 January 2008 from 1% to 0.5%.

16. Circular of the Director of the tax authorities LITL No. 164/2 of 28 January 2011 and Circular of the Director of the tax authorities LITL No. 164/2bis of 8 April 2011 (*Circulaire du directeur des contributions L.I.R. – n° 164/2 du 28 janvier 2011 et Circulaire du directeur des contributions L.I.R. – n° 164/2bis du 8 avril 2011*).

An advance pricing agreement (APA) filed with the Luxembourg tax authorities securing this margin<sup>17</sup> may only be issued to intra-group financing companies which have sufficient substance<sup>18</sup> in Luxembourg and which bear the risks linked to the financing activities.<sup>19</sup>

### 27.2.2.2. Intellectual property regime

With the intellectual property (IP) regime, which came into force on 1 January 2008 by the introduction of Article 50bis in the LITL, Luxembourg offers an 80% exemption on the net income arising from the use of or the right to use copyright on software, patents, trademarks, domain names, designs or models (hereinafter intellectual property rights (IPR)) acquired<sup>20</sup> or created by a LuxCo or a Luxembourg permanent establishment after 31 December 2007. Furthermore, the exemption also applies to net capital gains realized on such IPR. Applying this special IP regime, the effective tax rate for such IP income is 5.84% for the tax year 2013.<sup>21</sup>

## 27.3. Value added tax

### 27.3.1. Introduction

The present value added tax (VAT) regime relies mainly on Directive 2006/112/CE of 28 November 2006, which partly rewrote and completely reorganized the old Sixth VAT Directive of 17 May 1977. The Sixth VAT Directive of 17 May 1977 was implemented in Luxembourg by the law of 12 February 1979 on VAT,<sup>22</sup> as amended (the “LTVA”).

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17. Margin is secured for 5 years.

18. A majority of LuxCo’s board members – those able to take binding decisions – should be resident in Luxembourg, LuxCo should not be viewed as being tax resident in another state, LuxCo must have its own bank account at a Luxembourg credit institution or a Luxembourg branch of a foreign credit institution, etc.

19. The company’s equity (share capital and reserves) must be appropriate with regard to the functions it carries out, the assets being invested and the risks it assumes, i.e. at least 1% of the nominal value of the loan being granted, but without exceeding EUR 2 million.

20. IP should not be acquired from a related party according to the definition mentioned in the Circular of 5 March 2009 on Article 50bis LITL.

21. On 5 March 2009, the Luxembourg tax authorities published a circular (*Circulaire du directeur des contributions L.I.R. – n° 50bis/1 du 5 mars 2009*) on the Luxembourg IP regime, which aimed to provide some guidance regarding the interpretation of this partial exemption regime pursuant to Article 50bis LITL.

22. Law on Value Added Tax (*Loi concernant la taxe sur la valeur ajoutée*).

Since the implementation of the “VAT package” on 1 January 2010,<sup>23</sup> new rules on the place of taxation of services<sup>24</sup> apply in Luxembourg.

### 27.3.2. E-books

A super-reduced VAT rate of 3% applies in Luxembourg to physical books, journals, newspapers, etc. In December 2011, the Luxembourg government issued a circular<sup>25</sup> stating that the reference to books in the LTVA should be understood as including e-books. Before this Circular, the supply of digitized products fell within the meaning of electronically supplied services, subject to the normal VAT rate. The European Commission has decided to refer Luxembourg (and France) to the Court of Justice of the European Union (ECJ) regarding the application of reduced rates of VAT to e-books (Case C-502/13). The decision of the ECJ is still pending.

### 27.3.3. E-services and VAT

Luxembourg is currently home to many e-service providers as Luxembourg has an attractive way of applying VAT to these services. For services supplied to European customers, e-businesses duly established in the European Union are required to charge VAT on their services at the rate applicable in their country of establishment. With a rate of 15%,<sup>26</sup> Luxembourg has the lowest standard VAT rate in the European Union, which provides the opportunity to save costs, thus leading to more competitive sales prices. From 2015, Luxembourg will establish mandatory rules<sup>27</sup> for e-business under the VAT package. The new VAT rules will abolish the distinction between European and non-European companies providing their e-services to European customers because the VAT will be due at the place of the customer from 2015.

23. Implemented into Luxembourg domestic law by the law of 10 November 2009 (*Loi du 10 novembre 2009 “Paquet TVA”*).

24. In this respect, most business-to-business supplies of services are taxed where the customer is situated rather than where the supplier is located. For business-to-consumer supplies of services, the place of taxation continued to be where the supplier is established.

25. Circular No. 756 of 12 December 2011 (*Circulaire n° 756 du 12 décembre 2011*).

26. Luxembourg’s Prime Minister Xavier Bettel has recently confirmed the government’s decision to increase Luxembourg’s VAT rate by 2% to 17% from 1 January 2015.

27. As soon as a company provides e-services to a non-VAT-registered EU customer, regardless of whether a legal or natural person, it is bound to these rules.

## 27.4. Other taxes

### 27.4.1. Environmental taxes

Energy taxes are levied within the framework of the 2003/96/EC Energy Taxation Directive.<sup>28</sup>

### 27.4.2. Excises

Luxembourg levies excise duties on specific goods such as electricity, gas, oils, manufactured tobacco and alcohol.

### 27.4.3. Social security contributions

In Luxembourg, social security contributions must be paid both by employees and employers. It covers healthcare, sickness, accidents at work, maternity, unemployment, old-age pension, invalidity pension and survivor pension. Rates for employees range from 10.80% to 11.05% of the employment income. Rates for employers range from 12.72% to 14.89%.

### 27.4.4. Inheritance tax and gift tax

Inheritance tax is due on all the deceased's assets, except for real estate located outside Luxembourg if the last residence of the deceased was in Luxembourg (if not, transfer tax applies, which is charged only on the real estate located in Luxembourg).

Inheritance tax and transfer tax have progressive rates with a range between 0% and 48% depending on the degree of relationship between beneficiary and deceased and the value of the inherited property.

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28. Transposed into Luxembourg law by the Ministerial Regulation of 5 August 2004, published in the *Mémorial A* No. 151 from 18 August 2004, and by the Law of 22 December 2006 concerning the state receipts and expenses budget for the financial year 2007 (*Loi concernant le budget des recettes et des dépenses de l'Etat pour l'exercice 2007*).

Gift tax is levied on the donee of a gift. If the donor is a Luxembourg resident, the tax is levied on any asset received. If the donor is a non-resident, the transfer tax is only levied on immovable property in Luxembourg.

Rates range from 1.8% for relatives in a direct line up to 14.4% for non-related persons.



# Notes

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