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GLOBAL TAX WEEKLY
a closer look

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SUBJECTS TRANSFER PRICING INTELLECTUAL PROPERTY VAT, GST AND SALES TAX CORPORATE TAXATION INDIVIDUAL TAXATION REAL ESTATE AND PROPERTY TAXES INTERNATIONAL FISCAL GOVERNANCE BUDGETS COMPLIANCE OFFSHORE

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The Deep Black Holes In The European Union's Blacklist

by Paul Tadros and Marc Schwartz,
Schwartz International

Introduction

Earlier this year, the European Union ("EU") published a blacklist of several countries, with both the methodology employed and the countries listed causing some controversy. The major reason it provided for pursuing a blacklist is that its member states have lost or could lose tax revenues due to those countries' tax legislation, policies, and administrative practices.

Two very important points to note regarding the aforementioned methodology and reasons are that: (1) the metrics on which the EU based its assessments have not been released; and (2) G20 countries such as Argentina, Brazil, China, India, Russia, Saudi Arabia, South Africa, and Turkey did not make the blacklist, despite arguably demonstrating some of the characteristics for which smaller countries were included. Conversely, the inclusion of jurisdictions such as American Samoa and Guam on the list also lead one to question the rationale and methodology utilized; the magnitude of the tax revenue losses to the EU flowing through American Samoa and Guam must surely not be significant.

Preliminary Observations

While several countries (the US has not and will not, due to the "limitation of benefits" provisions in its treaties) have signed the OECD's Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (most often referred to as the multilateral instrument, or "MLI"):

1. Several have expressed their reservations on most, if not all, of the provisions; and
2. It recently came to light that the Netherlands is lamenting the extent to which its treaty partners (notably Germany, Italy, and Switzerland) are reluctant to adjust their treaties. The Netherlands now expects only 44 out of 94 of its treaties to be affected.

This article focuses on one country on the EU blacklist: the Republic of Trinidad and Tobago (or "TNT", as it is locally known).

The EU stated that TNT is on the blacklist because it:

1. Failed to sign and ratify the OECD Multilateral Convention on Mutual Administrative Assistance ("MAA");
2. Maintains a harmful and preferential tax regime; and
3. Failed to join the OECD Global Forum on Transparency and Exchange of Information for Tax purposes.

However, it is interesting to observe that, in the recently released Financial Secrecy Index rankings by the Tax Justice Network, all of the G20 countries are in the top 50, *i.e.*, they harbor secrecy the most. And one of the least secretive? TNT, sitting at 107 out of 111.

Based on this information alone, one may well reach an opinion that the EU "cherry-picked" the countries it wanted to target, applying illogical assessments to arrive at contradictory conclusions. Scratch the surface a little more, and such opinion may be vindicated when questioning how TNT could have a harmful and preferential tax regime when it is excluded from another EU list of those facilitating harmful offshore structures; and furthermore that TNT actually meets the minimum BEPS standards (about which more below).

TNT And Its Tax System

Introduction

The larger island, Trinidad, is commercial and industrial, with the energy sector being the economic engine. The first oil well was drilled in 1857, and the first commercial production of oil was in 1908. By using natural gas (which it produces in large quantities) as a feedstock, it produces nitrogen, urea, ammonia, and methanol. It is now the largest exporter of methanol.

Some of the largest players in the energy sector operate in Trinidad, for example BP (formerly Amoco); Air Liquide; BHP Billiton; Methanex; PCS (Potash Corporation of Saskatchewan) Nitrogen; Nutrien; Norsk-Hydro; Baker Hughes; Bechtel; and Halliburton.

The tax system

Taking the below into account, the characterization of TNT as having a preferential and harmful tax regime could be seen as questionable.

First, if a corporation (domestic or foreign) is a tax resident of TNT, it is taxable on its worldwide income. The following taxes are imposed:

1. Income tax:
   (a) On the first TTD1m (approximately USD148,105), the rate is 25 percent. The excess is taxed at 30 percent for corporations not in sectors (b) and (c) below.
   (b) Downstream petrochemicals and related industries (*e.g.*, methanol, urea, *etc.*) are taxed at 35 percent.
   (c) Upstream oil and gas are taxed at 55 percent plus supplemental taxes.
2. The business levy (a gross receipts tax) is imposed at 0.6 percent on gross receipts/sales creditable against the income tax liability. In essence, it acts as a minimum tax if there is, for example, a loss.
3. The green levy (another gross receipts tax) is imposed at 0.3 percent on gross receipts/sales and is due independent of the income tax and business levy.

It is important to note that while TNT may grant tax concessions to certain industries (ownership is not a determining factor), such concessions (say, an income tax holiday) are for a limited duration and come with a price. For example, tax depreciation must be claimed during the holiday period; thus, unless significant additional investments are made in plant and equipment, the undepreciated balances after the holiday expires are not significant.

Also notably, such concessions are covered in most, if not all, of TNT's treaties with European countries via the tax sparing provisions. As these are bilateral negotiated treaties, if this is what the EU now considers to be a preferential or harmful practice or "revenue loss", then the goalposts appear to have been shifted.

In the case of individuals, the income tax rates are 25 percent on the first TTD1m, and 30 percent on the excess. Most tax credits were replaced by a personal allowance of TTD72,000. Unlike corporations, an individual who is a tax resident of TNT but not domiciled therein is taxable only on income from TNT sources and foreign sources remitted to TNT (the carryover of the UK's "non-dom" provision from when it was a British colony).

Other corporate tax features

TNT's corporate tax system contains various other measures and restrictions, including measures that meet the OECD's recommendations under its BEPS project:

1. While net operating losses can be carried forward indefinitely, no carryback is allowed.
2. While long-term capital gains (arising from assets held for more than 12 months) are not taxable, (a) long-term capital losses are not deductible; and (b) short-term capital gains are taxable as ordinary income.
3. Foreign-source dividends are fully taxable with a foreign tax credit allowable under certain conditions.
4. Related party interest is not deductible; any "interest" payments are treated as non-deductible distributions.
5. Convertible debt is automatically treated as equity.
6. Management fees are broadly defined such that their deductibility is limited to 2 percent of total expenses excluding depreciation, amortization, and management fees.

Conclusion

No country is perfect, and TNT's tax administration, as is the case for many countries, may well need an overhaul. But the EU's/OECD's heavy handed approach is not a helpful one, in the authors' opinion.

Given TNT's commercial and industrial economy, and that it is a relatively high-tax country that already has provisions to combat base erosion and profit shifting, one would hope that the EU and the OECD would rather encourage their member countries to enter into bilateral treaties with TNT.