SPAIN

Spanish Windfall Tax Prompts Repsol To Suspend Hydrogen Projects

by William Hoke

Repsol SA has suspended its investments in three Spanish green hydrogen projects, apparently following through with a previous warning about a controversial windfall profits tax on the energy sector.

The Madrid-based energy and petrochemical company said October 21 that it has halted work on the three projects, which rely on renewable energy to break apart water molecules into oxygen and hydrogen, with the latter then being used as a source of emission-free fuel.

The announcement came shortly after the government said it will move ahead with plans to make permanent a temporary tax on windfall profits in the energy and banking sectors. In December 2022 parliament passed a 1.2 percent tax on the revenues of energy companies that had at least €1 billion of sales in 2019. (The parliament also approved a windfall tax of 4.8 percent on the net interest income and fees of banks that had at least €800 million of such income in 2019.) In January parliament indefinitely extended the windfall taxes, which were scheduled to expire at the end of 2023.

Repsol had said in October 2023 that its future investments in Spain might be impacted if parliament extended the windfall tax.

Reuters reported October 21 that Repsol will suspend the three green hydrogen projects, which have a combined capacity of 350 megawatts. Repsol's planned investment in the projects totals more than €700 million. ■

SWITZERLAND

Swiss Tax Agency: Arm's-Length Markup Only on Operative Costs

by Alexander F. Peter

A recent judgment by Switzerland's Federal Supreme Court that all costs must be included in the market price of related-party transactions does not apply to international fact patterns, the Swiss Federal Tax Administration has said.

In its October 8 statement, the tax administration clarified that a June 11 decision (9C_37/2023) by Switzerland's Federal Supreme Court (Bundesgericht) interpreting the cost-plus method under article 58(3) of the Federal Direct Tax Act covers only entities providing public services of general interest (like utilities companies) in a domestic setting.

Switzerland's arm's-length principle, as enshrined in article 58(1) of the Federal Direct Tax Act, disallows as a deduction "non-business-related benefits to third parties." Article 58(3) stipulates a more specific rule that "services provided by mixed-business companies operating in the public interest primarily to related parties are to be valued either at the respective market price, or at the respective production cost plus an appropriate mark-up, or at the respective final selling price less an appropriate profit margin; the result of each company is to be adjusted accordingly."

In its June 11 judgment, the Federal Supreme Court held that taxes are part of the production cost base under article 58(3) subject to the relative profit level indicator. The OECD transfer pricing guidelines are not indicative for article 58(3)'s construction and can — if at all — serve only an auxiliary role in interpreting article 58(3). The element in paragraph 2.37 et seq. of the 1995 OECD transfer pricing guidelines (paragraph 2.49 et seq. of the 2022 guidelines) requiring the elimination of taxes from the cost base because they are not related to a company's function is therefore irrelevant by virtue of a different Swiss practice, the court said.

"The historical background to that 'Swiss practice' is that, in the 1950s, Switzerland issued a circular stating that companies with a strong foreign business focus were effectively not taxable

in Switzerland due to the allocation of that tax base to abroad," Thomas Hug of Deloitte AG's Zurich office told *Tax Notes* October 21. "Consequently, the tax administration declared in that circular that Swiss taxable income was to comprise at least 10 percent of total business costs, including taxes."

In 2004 Switzerland abandoned this practice in a new memorandum (Circular No. 4) and aligned with the OECD transfer pricing guidelines, Hug said.

"Article 58, paragraph 3, which applies to companies operating in the public interest, reflects this old practice," Hug said. "The Federal Supreme Court's ruling has caused significant international confusion, partly because the tax administration reaffirmed its OECD-compliant position in a Q&A in February."

In question 5 of the February Q&A, the tax administration refers to the OECD's position that "a fundamental distinction must be made between operating costs, i.e. expenses that a company regularly incurs to keep business processes and systems running and to provide services that generate value added, and non-operating costs, such as taxes and financing costs." It said that "financing costs (at least for typical service companies and non-capital-intensive (routine) production companies) are also not usually incurred during actual operating activities and do not generate value added. As non-operating costs do not contribute to a company's value added, they are generally not included in the cost base."

In its October 8 statement, the tax administration reiterated that the hypothetical or calculatory approach to the cost-plus method, which includes taxes, is not compliant with the OECD transfer pricing guidelines and does not represent the tax administration's position for cross-border situations, which typically uses benchmark studies for comparables without taxes. Hence, in those cases, only operating expenses must be considered as part of the cost basis, and nonoperating ones like taxes are excluded, the statement says.

"The clarification by the Swiss tax administration is welcomed," Hug said. ■

UKRAINE

Tax Liabilities of U.K. Resident's PE In Ukraine Clarified

by Iurie Lungu

Ukraine's State Fiscal Service (SFS) has issued a guidance letter clarifying the tax implications of a U.K. resident company's transactions with its permanent establishment in Ukraine.

According to Guidance Letter 4799/IPK/99-00-21-02-02 (dated October 14), Tax Code article 14, subsection 14.1.122, says the list of taxable persons in Ukraine includes nonresident legal entities that derive income from Ukrainian sources as well as nonresidents' PEs and other stand-alone affiliates in Ukraine that derive income from Ukrainian sources or are otherwise required to pay corporate tax in Ukraine.

According to article 64, section 64.5, and article 133, nonresident legal entities must register with the Ukrainian tax authorities as nonresident corporate taxpayers upon the occurrence of any of the following events:

- the commencement of their operations in Ukraine through a stand-alone division (including a PE);
- the acquisition of immovable property in Ukraine;
- the opening of accounts in Ukrainian banks;
- the carrying out of activities through a PE in Ukraine; or
- the acquisition of an investment asset in the form of securities, derivatives, or other corporate rights in the capital of a Ukrainian resident legal entity from another nonresident that does not have a PE in Ukraine.

Referring to article 14, subsection 14.1.193, the SFS said that for tax purposes, a PE is a fixed place through which a nonresident fully or partially carries out business activities in Ukraine.

Therefore, the SFS said, a nonresident carrying out business activities through a PE in Ukraine falls under the definition of a PE provided in subsection 14.1.193. It must register as a corporate taxpayer in Ukraine, file corporate tax returns, and pay the corporate tax due in Ukraine at a rate of 18 percent.