



BDO Seidman, LLP
Accountants and Consultants

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International Tax Alert

Subject:

International Tax Reforms: Tax Rate Changes in the UK, China and Germany

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Date/Timing

Immediate

Affecting

U.S. Multinational Groups.

Background

In recent months we have seen tax reforms being initiated in countries that are major trading partners of the United States. Such reforms include a number of countries reducing the headline rate of Corporation Tax. Countries that have recently introduced changes in rates of their Corporation Income Tax include:

Country	Rate of Corporation Tax		Date	
	Old	New	Law Enacted	Changes effective from
China (Standard Rate)	33%	25%	March 16, 2007	January 1, 2008
China ¹ (Foreign Invested Enterprises) ("FIE's")	15%/24%	25%	March 16, 2007	January 1, 2008
Denmark	28%	25%	June 1, 2007	With retroactive effect from January 1, 2007
Germany ²	25%	15%	To be enacted upon publication in the Federal Gazette	Measures generally have effect from 1 January 2008 (includes tax years ending in 2008)
United Kingdom	30%	28%	July 19, 2007	Financial years starting April 1, 2008

Other countries that have proposed significant tax reforms (some of which include changes to tax rates) are Canada, France, Mexico and Japan.

Impact on Financial Reporting

All tax reforms, especially changes in tax rate, will have potential accounting implications, including impact on FAS 109 (Accounting for Income Taxes) and FIN 48 (Accounting for Uncertainties in Income Taxes).

FAS 109 – paragraph 27 requires that deferred tax assets and liabilities should be adjusted for the effect of a change in tax laws or rates. The effect of the change in tax rate should be included in income from continuing operations for the period that includes the enactment date. As such, many businesses will need to have assessed the provisions of the new international tax reforms in time for their quarterly reporting deadlines. Companies that adopted FIN 48 will be required to analyze the uncertainties using the recognition and measurement principles of FIN 48.

Change in Tax Rates

To use UK changes as an example: The Finance Act 2007 (FA 2007), which included the reduction of the Corporate Tax rate from 30% to 28%, received Royal Assent on July 19, 2007 and as such was enacted on the same date. However, the reduction in the rate of Corporation Tax is only effective for financial years starting April 1, 2008. Therefore, a company's temporary differences and carryforwards existing as of the date of enactment must be analyzed in order to determine when such differences are expected to reverse and the tax rate applicable in the accounting period of reversal.

Temporary differences that are expected to have reversed prior to the date that the change in tax rate is effective should be accounted for under the current law (being the 30% tax rate). Whereas, temporary differences that are expected to reverse after the effective date for the change in law should be accounted for using the new tax rate provided for by FA 2007 (being 28%). As mentioned above, the effect of the change in tax rate should be included in income from continuing operations for the period that includes the enactment date.

In the case of the UK, the change in tax rate is not complicated and will merely decrease to 28% with effect from April 1, 2008. Calculating the impact of a change in tax rates under FAS 109 is likely to be a harder task where taxes are phased in, as is the case with the changes in the tax rate for Foreign Investment Enterprises (FIEs) in China. In summary, the tax rates for FIEs will be gradually increased from the current reduced rates of 15% or 24% to the standard rate of tax of 25% within five years after implementation of the Chinese Corporate Income Tax Law which was enacted March 16, 2007. Guidance has yet to be issued on how the transitional rules will be applied to FIEs.

As with the case of change in tax rates, other significant tax reforms that impact deductions or the treatment of income will also have to be considered by businesses when analyzing and interpreting the effect of the changes to the tax laws under FAS 109 and FIN 48 principles.

¹ Tax rates for FIE's will be gradually increased to the standard rate of tax within five years after implementation of the Chinese Corporate Income Tax Law which was enacted March 16, 2007.

² The solidarity surcharge of 5.5% remains, so that the combined rate of tax is 15.825%, down from 26.375%. However, any consideration of the headline tax rate paid by German companies must also take account of trade tax. The overall effect of the changes to corporate tax and trade tax is a combined effective average rate of tax in 2008 going forward of 29.8%, compared to about 39% currently.

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