

## INTERNATIONAL TRADE AND FINANCE MASTERCLASS

PART 12 OF 25 · SECTION V: THE INTERNAL FINANCIAL ARCHITECTURE

# PART 12

## VAT, GST, DIGITAL SERVICES TAXES, AND CFC RULES

*The tax layer that US-trained CFOs almost always get wrong — how VAT works fundamentally differently from sales tax, the import VAT cash flow trap, digital services taxes across fourteen countries, and how GILTI and FDI affect every US multinational.*

### IN THIS PART

- How VAT works — the multi-stage input/output mechanism
- The import VAT cash flow problem and how to solve it
- EU VAT — the One Stop Shop and IOSS for e-commerce
- Digital services taxes — France, UK, India, and beyond
- CFC rules and Subpart F income explained simply
- GILTI, FDI, and the global minimum tax

### CASE STUDIES

*Each part includes fully worked case studies with detailed calculations, real-world context, and practical lessons for CFOs and finance leaders.*

## ■ THE TAX LAYER MOST CFOS MISS

### Why VAT Is Not Sales Tax — The Fundamental Difference

When a US-trained CFO first encounters Value Added Tax, the most natural instinct is to treat it like US sales tax — a percentage added on top of the price, collected from the customer, and remitted to the government. This intuition is partially correct in describing the final result, but it fundamentally misses the mechanism. Sales tax in the United States is a single-stage tax collected only at the point of final sale to the consumer. VAT is a multi-stage tax collected at every step in the supply chain — from raw material supplier through manufacturer, distributor, and retailer. At each stage, the business remits only the net difference between the VAT it charged on its sales and the VAT it paid on its purchases. The consumer ultimately bears the full VAT burden, but every business in the chain is simultaneously a tax collector and a taxpayer.

## ◆ VAT – COMPLETE SUPPLY CHAIN MECHANISM

## HOW VAT WORKS – COMPLETE SUPPLY CHAIN ILLUSTRATION

UK VAT rate: 20%

Supply chain: Raw Material > Manufacturer > Distributor > Retailer > Consumer

## STAGE 1: Raw Material Supplier

Sells to Manufacturer at GBP 100 + GBP 20 VAT = GBP 120

Remits to HMRC: GBP 20 (no input VAT to deduct)

## STAGE 2: Manufacturer

Paid GBP 20 input VAT on purchase

Sells to Distributor at GBP 250 + GBP 50 VAT = GBP 300

Remits to HMRC: GBP 50 output - GBP 20 input = GBP 30

## STAGE 3: Distributor

Paid GBP 50 input VAT on purchase

Sells to Retailer at GBP 400 + GBP 80 VAT = GBP 480

Remits to HMRC: GBP 80 output - GBP 50 input = GBP 30

## STAGE 4: Retailer

Paid GBP 80 input VAT on purchase

Sells to Consumer at GBP 600 + GBP 120 VAT = GBP 720

Remits to HMRC: GBP 120 output - GBP 80 input = GBP 40

**TOTAL VAT COLLECTED BY HMRC: 20+30+30+40 = GBP 120**

**CONSUMER PAID: GBP 120 = 20% of GBP 600 selling price**

**BUSINESSES ARE COLLECTION AGENTS – they bear no net VAT cost**

PROVIDED they can reclaim input VAT promptly

**The CASH FLOW burden of paying VAT before reclaiming it**

**is where the real financial impact lies**

## The Import VAT Cash Flow Problem

When goods are imported into a VAT country, import VAT is charged at the border at the same rate as domestic VAT. The importer must pay this VAT upfront and then reclaim it on its next VAT return — typically thirty to sixty days later. The timing difference between paying import VAT and reclaiming it creates a working capital funding requirement that many companies fail to plan for when entering new markets.

## ◆ IMPORT VAT CASH FLOW MANAGEMENT

## IMPORT VAT CASH FLOW – COST AND SOLUTION

Monthly imports into Germany: EUR 2,000,000

German VAT rate: 19%

Import VAT due at border: EUR 2,000,000 x 19% = EUR 380,000

## WITHOUT DEFERRED PAYMENT SCHEME:

Pay EUR 380,000 on day of clearance

Reclaim approved in approx 37.5 days (average)

Cost of funding: EUR 380,000 x 8% x 37.5/365 = EUR 3,123/month

Annual cash flow cost: EUR 37,476

## WITH GERMAN DEFERRED PAYMENT SCHEME:

Import VAT deferred to end of following month

VAT return filed and refund processed simultaneously

Net cash impact: near zero

Annual saving vs. immediate payment: EUR 37,476

Registration time: 2-3 weeks – register before first import

## FISCAL REPRESENTATIVE REQUIREMENT:

Non-EU companies importing into EU may need a fiscal rep

Fiscal rep is jointly and severally liable for VAT

Cost: EUR 3,000-8,000 per year plus transaction fees

Required in: France, Italy, Spain, Belgium, and others

## Digital Services Taxes: The New Tax Frontier

The rise of digital business models created a fundamental problem for traditional international tax rules. Companies can generate substantial revenues in a country without any physical presence there — no employees, no offices, no servers. Traditional tax rules required a taxable physical presence before a country could tax business profits. Many countries responded by creating unilateral Digital Services Taxes levied on revenues from specific digital activities, regardless of where the company is based.

Country	Rate	Revenue Threshold	Activities Covered	Status
France	3%	EUR 750M global + EUR 25M French	Digital advertising, marketplaces, data transmission	Active since 2019
United Kingdom	2%	GBP 500M global + GBP 25M UK	Social media, search, online marketplaces	Active since April 2020

Country	Rate	Revenue Threshold	Activities Covered	Status
India	2%	INR 20M from Indian users (~\$240K)	Digital advertising, e-commerce digital goods supply	Active — Equalization Levy
Italy	3%	EUR 750M global + EUR 5.5M Italian	Digital advertising, marketplaces, data transmission	Active since 2020
Spain	3%	EUR 750M global + EUR 3M Spanish	Online advertising, marketplaces, user data	Active since 2021
Kenya	1.5%	No threshold — all digital services	Any digital marketplace or digital content	Active since 2021
Canada	3%	CAD 1B global + CAD 20M Canadian	Digital advertising, user data, social media	Proposed — implementation pending

## CFC Rules, GILTI, and FDII: The US International Tax Framework

For US multinational companies, the Controlled Foreign Corporation rules represent one of the most consequential elements of international tax. A Controlled Foreign Corporation is any foreign corporation in which US shareholders own more than fifty percent of the vote or value. The CFC rules require US shareholders to include certain categories of foreign income in their US taxable income currently — without waiting for a dividend. This prevents the indefinite deferral of tax on foreign income by leaving it offshore.

The 2017 Tax Cuts and Jobs Act introduced two new provisions that fundamentally changed the US international tax framework. GILTI — Global Intangible Low-Taxed Income — taxes US shareholders on foreign profits that exceed a ten percent routine return on tangible assets, treating the excess as income from intangible assets that must be taxed currently. FDII — Foreign-Derived Intangible Income — provides a deduction for income from serving foreign markets, effectively taxing this income at a reduced rate to incentivize keeping intellectual property in the United States.

## ◆ GILTI AND FDII – COMPLETE CALCULATIONS

## GILTI CALCULATION – COMPLETE EXAMPLE

Irish CFC:

Net tested income: \$12,000,000

Qualified Business Asset Investment (QBAI): \$8,000,000

Net Deemed Tangible Income Return: \$8M x 10% = \$800,000

**GILTI inclusion: \$12,000,000 - \$800,000 = \$11,200,000**

## US PARENT TAX ON GILTI:

**GILTI inclusion: \$11,200,000****Section 250 deduction (50%): \$5,600,000****Taxable GILTI: \$5,600,000****Tentative US tax (21%): \$1,176,000****Less: 80% foreign tax credit****Irish tax paid: \$12M x 12.5% = \$1,500,000****80% FTC: \$1,200,000****Net US GILTI tax: \$1,176,000 - \$1,200,000 = \$0**FTC offsets at 12.5% Irish rate – but at lower rates  
(e.g., a zero-tax jurisdiction), GILTI creates real US tax

## FDII DEDUCTION:

US company with \$20M income from serving foreign markets

**FDII deduction (37.5%): \$20M x 37.5% = \$7,500,000****Effective tax rate on FDII: 21% x (1-37.5%) = 13.125%****Tax saving vs. regular rate: \$20M x (21%-13.125%) = \$1,575,000**

## 01

## CASE STUDY 1

**CloudSoft Solutions***EU VAT Compliance Failure — EUR 5.2M in Back Taxes and Penalties***Background**

CloudSoft Solutions is a US SaaS company that had been selling project management software to EU consumers since 2017, generating four million euros of annual EU revenue from fourteen thousand customers across twenty-two member states. The company had never registered for VAT anywhere in Europe, incorrectly believing that as a US company without a European presence it had no EU VAT obligations. A German customer's request for a VAT invoice revealed the five-year oversight.

## ◆ EU VAT NON-COMPLIANCE COST ANALYSIS

## CLOUDSOFT – EU VAT NON-COMPLIANCE COST

Annual EU B2C revenue: EUR 4,000,000

Blended EU VAT rate: 21%

Annual VAT owed: EUR 4,000,000 x 21% = EUR 840,000

Years of non-compliance: 5

**Total VAT principal: EUR 840,000 x 5 = EUR 4,200,000**

**FULL ASSESSMENT (before voluntary disclosure):**

VAT principal: EUR 4,200,000

Interest (avg 5% for 3 yrs): EUR 630,000

Penalties (blended 20-30%): EUR 840,000

**Total: EUR 5,670,000**

**WITH VOLUNTARY DISCLOSURE (60% penalty reduction):**

VAT + interest: EUR 4,830,000

Penalties (40% of EUR 840K): EUR 336,000

**Total: EUR 5,166,000**

**GOING FORWARD – EU ONE STOP SHOP (OSS):**

Single registration in Ireland covers all EU B2C VAT

One quarterly return covers all 27 member states

Annual compliance cost: \$18,000

Had they registered in 2017: zero penalty risk

Compliance cost over 5 years: \$90,000

Saving vs. non-compliance: EUR 5,166,000 - \$90,000

## 02

## CASE STUDY 2

**Digital Marketplace Inc.**

*Multi-Country DST Burden — Modeling \$1.7M of Digital Services Tax*

**Background**

Digital Marketplace Inc. operates an online marketplace generating one hundred and fifty million dollars of annual fee revenue. The company's finance team identified that it was subject to Digital Services Taxes in France, the UK, Italy, Spain, India, and Kenya. The CFO needed to quantify the total DST burden and model its impact on effective tax rate.



## ◆ IP STRUCTURE – TAX COMPARISON

ATLAS – ONSHORE vs. OFFSHORE IP STRUCTURE

Annual IP royalty income: \$50,000,000

## OPTION A: IP IN US PARENT (FDII benefit):

80% of royalties from foreign licensees = FDII

FDII: \$50M x 80% = \$40,000,000

FDII deduction (37.5%): \$15,000,000

Taxable income: \$50M - \$15M = \$35,000,000

US tax: \$35,000,000 x 21% = \$7,350,000

Effective rate: 14.7%

## OPTION B: IP IN IRISH SUBSIDIARY:

Irish corporation tax: \$50M x 12.5% = \$6,250,000

GILTI FTC offsets most US tax (as shown above)

Additional US tax (residual): approximately \$800,000

Total tax: \$6,250,000 + \$800,000 = \$7,050,000

Effective rate: 14.1%

## COMPARISON:

Option A (US + FDII): \$7,350,000 per year

Option B (Ireland + GILTI): \$7,050,000 per year

Annual saving from Irish structure: \$300,000

IP migration cost: \$2,000,000

Payback period: 6.7 years – marginal benefit

Plus: Pillar Two minimum tax reduces Irish advantage further

CONCLUSION: Post-TCJA, keeping IP onshore with FDII

is increasingly competitive vs. offshore structures