Minimum level of taxation for multinational groups

2021/0433(CNS) - 22/12/2021 - Legislative proposal

PURPOSE: to swiftly implement the international agreement on minimum taxation of multinationals to ensure a global minimum effective tax rate of 15% for large multinationals operating in the European Union.

PROPOSED ACT: Council Directive.

ROLE OF THE EUROPEAN PARLIAMENT: the Council adopts the act after consulting the European Parliament but without being obliged to follow its opinion.

BACKGROUND: the anti-tax avoidance directives have laid down rules against the erosion of tax bases in the internal market and the shifting of profits out of the internal market. Those rules converted into Union law the recommendations made by the Organisation for Economic Cooperation and Development (OECD) in the context of the initiative against base erosion and profit shifting (BEPS) to ensure that profits of multinational enterprises (MNEs) are taxed where economic activities generating the profits are performed and where value is created.

The proposal delivers on the EU's pledge to move swiftly to implement the recent comprehensive tax reform agreement of the OECD and G20 inclusive framework agreed by 137 countries in October 2021 on a two-pillar solution to the tax challenges raised by the digitalisation of the economy, which aims to bring fairness, transparency and stability to the international corporate tax framework. The discussions centred around two main themes: Pillar 1, which deals with the partial reallocation of taxing rights, and Pillar 2, which concerns the minimum level of taxation of profits of multinational enterprises.

With the present proposal, the European Commission wishes to implement Pillar 2 of the Global Agreement. There is a political urgency to move forward with the project - i.e. to apply the OECD Model Rules in the EU from the beginning of 2023, as agreed by the Inclusive Framework.

CONTENT: the proposed directive sets out the method for calculating the effective tax rate by jurisdiction and includes clear and legally binding rules that will ensure that large groups operating in the EU pay a minimum rate of 15% for each jurisdiction in which they operate.

Scope

The proposed Directive will apply to any large group, both domestic and international, including the financial sector, with combined financial revenues of at least EUR 750 million a year in its consolidated financial statements in at least two of the last four consecutive fiscal years, and with either a parent company or a subsidiary situated in an EU Member State.

Governmental entities, international organisations, non-profit organisations, pension fund and investment funds are excluded from the scope of the Directive.

Calculation of the effective tax rate

The proposal provides that if the effective tax rate applicable to entities in a given jurisdiction is below the 15% minimum, then the group will have to pay a top-up tax to bring its rate up to 15%. This top-up tax is known as the Income Inclusion Rule'. This top-up applies irrespective of whether the subsidiary is located in a country that has signed up to the international OECD/G20 agreement or not.

The effective tax rate is established per jurisdiction by dividing taxes paid by the entities in the jurisdiction by their income.

Groups established in a third country

The proposal also ensures effective taxation in cases where the parent company is located outside the EU in a low-tax country which does not apply equivalent rules. Member States would then apply the under-taxed payments rule, designed as a safety net to the primary income inclusion rule.

In practice, a Member State will collect the top-up tax due at the level of the entire group if some jurisdictions where entities are based impose tax below the minimum level and do not impose any domestic top-up tax.

Exemptions

In order to reduce compliance burdens in low-risk situations, an exclusion applies to minimal amounts of profit: the de minimis income exclusion. This is when profits of the MNE groups constituent entities in a jurisdiction are below EUR 1 million and revenues below EUR 10 million. To reduce the impact on groups carrying out real economic activities, companies will be able to exclude an amount of income equal to 5% of the value of tangible assets and 5% of payroll.

Moreover, due to its highly volatile nature and the long economic cycle of this industry, the international shipping sector has traditionally been subject to alternative or supplementary tax regimes in Member States. The proposal therefore excludes income generated by this sector from the scope of application.

Special rules for mergers and acquisitions

The proposal contains special rules for mergers, acquisitions, joint ventures and certain multi-parented multinational enterprises. It provides for the application of a consolidated revenue threshold to group members in a merger or demerger situation.