**SPECIAL LEGISLATIVE PROCEDURE – CONSULTATION**

**European Parliament legislative resolution on the proposal for a Council Directive amending laying down rules against tax avoidance practices that directly affect the functioning of the internal market**

**1. Rapporteur:** Hughes BAYET (S&D/BE)

**2. EP reference number:** A8-0189/2016 / P8\_TA-PROV(2016)0265

**3. Date of adoption of the resolution:** 8 June 2016

**4. Subject:** Rules against the avoidance of corporate income tax

**5. Interinstitutional reference number:** 2016/0011(CNS)

**6. Legal basis:** Article 115 TFEU

**7. Competent Parliamentary Committee:** Committee on Economic and Monetary Affairs (ECON)

**8. Commission’s position:**

Some of the amendments:

* support the Commission’s policy but are premature or redundant because the matter is still under discussion or regulated elsewhere;
* go beyond the Commission's proposal and cover topics that are out of the scope of the Directive.

The tenor of certain amendments is acceptable for the Commission as these amendments are in line with the Commission's position.

**a)** **Definition of "taxpayer" (Amendment 34)**

This definition is not needed as the scope of the Directive is already defined in Article 3. Therefore, the amendment cannot be accepted.

**b) Definition of "royalty costs" (Amendment 35)**

The Commission cannot accept this amendment. The Commission has not proposed a limitation to the deductibility of royalty costs. Royalty payments pose different base erosion and profit shifting (BEPS) risks than interest payments and therefore require different measures such as the modified nexus approach to remove the harmful features of intellectual property (IP) boxes, enhanced transfer pricing rules to properly value intangibles (which is much more complicated than valuating loans), exit tax and CFC rules (which have been included in the Directive) to counter re-allocation of intangibles to low or no tax jurisdictions.

**c) Definitions of "secrecy or low tax jurisdiction" (Amendment 36) and "tax haven" (Amendment 38) and withholding tax on payments to a "secrecy or low tax jurisdiction" (Amendment 53)**

As regards the approach of low tax third countries, the Commission has addressed this in its recent External Strategy[[1]](#footnote-1). This Strategy sets out a common EU approach towards assessing, screening and listing third countries for tax purposes. This EU approach will be founded on clear, coherent and internationally recognised tax good governance criteria, which are consistently applied in relation to third countries. It will not only have a stronger deterrent effect for "tax havens" but would also ensure greater clarity and legal certainty for businesses and the EU's international partners. The Commission intends to use a comprehensive set of indicators to identify third countries which may pose risks to Member States' tax bases. As outlined in the Strategy, the Commission will prioritise third countries for screening on the basis of a scoreboard of indicators to determine the potential impact of jurisdictions on Member States' tax bases (such as economic ties with the EU, the level of financial activity and institutional and legal factors). The first findings of the scoreboard will be presented to Member States in the Code of Conduct Group by autumn 2016. As the next step, on the basis of the scoreboard, Member States should decide which jurisdictions should be assessed against the EU's updated good governance criteria. In the final step, third countries found to be problematic on tax matters will be included in a common EU list. As part of the process, the Council will also explore coordinated defensive measures at EU level.

With regard to the amendment on the introduction of a withholding tax, the aim of this Directive is not to introduce new taxes, but to strengthen the existing corporate tax systems of Member States against aggressive tax planning. Furthermore, it is unclear what kind of payments should fall under this rule as this is not defined in the amendment. Therefore, the Commission cannot accept the proposed amendments.

**d) Definition of associated enterprises (Amendment 44)**

The Commission could agree with the idea that an enterprise should be deemed associated with the taxpayer if there is a participation of at least 25 %.

**e) Definition of permanent establishment and profits attributable to a permanent establishment (Amendments 37, 51 and 52)**

Rules on permanent establishments are especially relevant for tax treaties. The Commission addresses this issue in its Recommendation of 28 January 2016 on the implementation of measures against tax treaty abuse[[2]](#footnote-2). In this Recommendation, Member States are explicitly encouraged to implement in their tax treaties the new Article 5 of the OECD Model Tax Convention as proposed in the report on BEPS Action 7 in October 2015 (so as to address artificial avoidance of taxable presence in the form of a permanent establishment). The Commission has addressed this issue in a Recommendation rather than a Directive because, as opposed to purely national rules, tax treaties are negotiated agreements between two (or more) countries via which the contracting states allocate taxing rights amongst themselves. Moreover, the definitions proposed by Parliament deviate significantly from the definition of a permanent establishment in the OECD Model Convention. Therefore, the Commission cannot accept the proposed amendments.

**f) Definition of "minimum economic substance" (Amendment 39) and "letterbox companies" (Amendment 43)**

These amendments are not acceptable.

The question of economic substance could be relevant in the context of the controlled foreign company (CFC) rule. The Commission believes that this issue has been dealt with by the substance requirement in the CFC rules. It has been laid down the CFC rules may be applied within the EU where the CFC does not carry on a substantive economic activity supported by staff, equipment, assets and premises, as evidenced by relevant facts and circumstances.

With regard to **Amendment** **43**, it cannot be prescribed how enterprises should organise their business, at least not in a tax Directive. The fight against letterbox companies should not lead to the stigmatisation of company forms. There are many reasons why companies are established abroad. Legitimate reasons for establishment should be protected. The Court of Justice has ruled in case Inspire Art (Case C-167/01) that the fact that a company does not conduct any business in the Member State in which it has its registered office and pursues its activities only or principally in the other Member State is not sufficient to prove the existence of abuse or fraudulent conduct. This directive includes several measures to combat tax avoidance practices without limiting the freedom of businesses to set up separate companies.

**g) European tax identification number (TIN) (Amendments 40 and 90)**

As regards a harmonised common European TIN, the Commission work on a feasibility study is ongoing. This study explores a series of options (including EU TINs) to enhance the identification of taxpayers involved in cross-border transactions. The information on national TINs on the TIN on Europa portal has been updated early 2016 in order to ensure that, when applicable, the on-line check module allows validation of the structure and syntax of TINs of individuals for all Member States.

**h) Definition of transfer prices and rules on transfer pricing (Amendments 41 and 64)**

Within the Commission, work is ongoing concerning transfer prices between associated enterprises in accordance with the OECD Transfer Pricing Guidelines (**Amendment** **64**). Furthermore, the EU Joint Transfer Pricing Forum (JTPF) under its 2015-2019 work programme is already working on the development of good practices that ensure how the OECD's fairly broad guidelines can actually be applied to the specific situation in the EU. These good practices will aim at ensuring the appropriate allocation of resources and will take into account the compliance burden the OECD principles create for tax administrations and companies. The new G20/ OECD guidelines on Transfer Pricing should help link profits to the economic activities which generate them. The Commission, with the assistance of its Expert Group, the JTPF, will monitor Member States' implementation of the new rules developed under the G20/ OECD BEPS project and the implication of these rules.

**i) Patent boxes (Amendments 42 and 101)**

Member States have accepted the new "modified nexus approach" as the future basis for patent boxes. The Commission will, in the framework of the Code of Conduct Group, continue providing guidance to Member States on how to implement patent box regimes in line with this new approach so as to ensure that they are not harmful, and (together with the Code of Conduct Group) will carefully monitor implementation. If Member States are not applying the new approach appropriately, then the Commission will consider introducing legislation to ensure its proper implementation. The Commission has not brought forward harmonising measures regarding the promotion of R&D and patent boxes due to Member States’ agreement on the nexus approach. No measure advancing the abolition of the existing patent box regimes has been brought forward for the same reason.

**j) Interest limitation (Amendments 46-50)**

Reducing the deductible interest to a ratio from 30 % to 20 % of the EBITDA would increase the impact of the interest limitation rule and could obstruct genuine business investments. The same goes for the safe harbour rule; Member States want that interest is always deductible to an amount of EUR 3 000 000. This threshold is acceptable to the Commission.

The tenor of **Amendment** **47** on the optional carve-out for public infrastructure projects is acceptable for the Commission. The same goes for **Amendment** **48** on a limitation of five years to carry forward unused interest capacity. **Amendment** **49** on a limitation of five years and 20 % of the EBITDA to carry forward non-deductible exceeding borrowing costs is not acceptable for the Commission. This would affect adversely companies that have made losses when there is no risk of base erosion. **Amendment** **50** on interest limitation rules for financial undertakings is not acceptable for the Commission. The Commission should not be bound to review the scope of the Article depending on developments at the OECD. However, if the discussions on financial undertakings are sufficiently conclusive in the international and Union context a specific rule regarding financial undertakings might be considered by the Commission.

**k) Exit tax (Amendments 54-57 and 63)**

The tenor of the clarifications in **Amendments** **54-57** as regards the moment when and to what extent exit tax may be imposed is acceptable for the Commission. **Amendment** **63** is not acceptable for the Commission: not applying the exit tax to transfers of tangible assets transferred to generate active business income would reduce the effectiveness of the rule and would limit Member States' already existing rights to tax unrealised gains upon a transfer of assets.

**l) Switch-over clause (Amendment 102)**

The switch-over clause has been taken out of the final Presidency's compromise proposal. Although the Commission would have preferred to have it in, the Commission can accept the deletion of the switch-over clause as this was needed to reach an agreement. Moreover, the CFC rules have been strengthened in the sense that they now include permanent establishments as well.

**m) General Anti-abuse rule (GAAR) (Amendments 68, 70, 96-98)**

The tenor of the wording included in **Amendment** **68** is acceptable for the Commission. **Amendment** **70** is not acceptable for the Commission: it is obvious that Member States should implement and apply the provisions of this Directive. But Member States cannot be obliged to allocate additional resources to their tax administrations to this end. **Amendment 97** is not acceptable for the Commission: detailed provisions to provide clarification on non-genuine arrangements would be contrary to the rationale of the GAAR and might be circumvented. **Amendment** **98** is not acceptable for the Commission: the Commission is monitoring and countering BEPS and tax avoidance on various fronts. A separate BEPS Control and Monitoring Unit is not deemed to be necessary.

**n) Controlled Foreign company (CFC) (Amendments 73-74, 103, 104, 105)**

The Commission does not support **Amendment** **73** to apply the CFC rules if more than 25 % of the entity's income is tainted because in that case too many companies would fall under the scope of the rule. **Amendment** **74** is not acceptable for the Commission: the CFC rules should not be extended to income from goods traded with the taxpayer or its associated enterprises. Income from traded goods is less likely to be diverted to the entity as this income does not involve mobile or intangible assets. The transfer prices of the traded goods can already be adjusted on the basis of the arm's length principle. **Amendment** **103** is not acceptable for the Commission: a calculation of the tax liability by reference to the economic substance as defined in **Amendment 39** on minimum economic substance does not give a clear guidance on how the tax liability should be calculated when applying the CFC rules. With regard to **Amendment** **104**, the Commission does not support an effective tax rate triggering requirement with a fixed rate that is lower than the corporate income tax rates of some Member States. As regards **Amendment** **105** on the application of CFC rules within the EU: the Commission would not support any changes to this proposal.

**o) Hybrid mismatches (Amendments 45, 77, 80 and 81)**

The tenor of **Amendments** **45**, **77** and **81** could be acceptable for the Commission as regards the third country dimension of these amendments. The Commission agrees that more work needs to be done particularly as regards hybrid mismatches involving third countries. **Amendment** **80** is not acceptable for the Commission because tax treaties are about sharing taxing rights among states. Hybrid mismatches cannot be sufficiently countered by means of a tax treaty.

**p) Effective tax rate (Amendment 82)**

Member States' tax systems are very different. Developing a method of calculating the effective tax rate to which all Member States agree is not easy as there is no common ground yet among Member States about what should be included in the tax base. Therefore, the Commission cannot accept the amendment.

**q) Tax treaty abuse (Amendment 83)**

This amendment is not acceptable for the Commission. Measures against treaty abuse should be subject of a Recommendation because, as opposed to purely national rules, tax treaties are negotiated agreements between two (or more) countries via which they allocate taxing rights amongst themselves. Nevertheless, the Commission thinks that it would be useful if it were to receive more systematically authorisation to negotiate tax agreements with third countries, notably in the area of administrative cooperation, where the EU has exercised its competences since 2004 through the signature of the agreements on taxation of savings with Switzerland and four other EU neighbours. These agreements have already been, or will be, brought into line with the EU and international developments on automatic exchange of financial account information. An EU-wide approach makes it easier to achieve full reciprocity in negotiations with third countries.

**r) Good governance in tax matters (Amendments 32 and 84)**

The Commission is already committed to the promotion of good governance in international trade agreements and economic partnership agreements on the basis of a mandate from the ECOFIN in May 2008. In the External Strategy, the Commission proposed the core elements for a revised clause taking account of the updated good governance standards. This will be further discussed with Member States within the Code of Conduct Group. This Directive is not the right place for such a commitment.

**s) Penalties (Amendment 85)**

Member States have the duty to uphold the provisions of this Directive. Member States must have sufficient rules in place to ensure that the taxpayers observe the rules of the Directive and if needed, apply sanctions against non-compliant taxpayers. However, it would go beyond the scope of the Directive to oblige Member States to apply penalties.

**t) Review, assessment and monitoring of the Directive (Amendments 86-89)**

It is for the Commission to monitor the functioning and effectiveness of the Directive.

**u) Mandatory automatic exchange of information (Amendment 91)**

The automatic exchange of information is dealt with by other Directives. Thus, this amendment cannot be accepted.

**9. Outlook for amendment of the proposal**: The Commission will not table a modified proposal in respect of the additional amendments proposed by Parliament.

**10. Outlook for the adoption of the proposal**: ECOFIN reached a political agreement on 20 June 2016. The proposal was subsequently adopted by ECOFIN on 12 July 2016.

1. Communication from the Commission to the European Parliament and the Council on an External Strategy for Effective Taxation, COM(2016) 024 final. [↑](#footnote-ref-1)
2. C(2016) 271. [↑](#footnote-ref-2)