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EU Tax Policy Report

CFE TAX ADVISERS EUROPE

The European Association of Tax Advisers founded in 1959.

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CFE's EU Tax Policy Report provides an analysis of key tax and other policy issues at EU level of interest to the European tax advisers covering the period July through December 2017.

Highlights

The Estonian Presidency set out a number of priorities however, in reality the last 6 months has been all about the big proposals and less about the existing files. On the direct tax side, the fair taxation of the digital economy has been in the spotlight whilst on the indirect tax side, the European Commission published long awaited proposals for a move toward a destination-based definitive VAT regime.

Back in November 2017 the International Consortium of Investigative Journalists ("ICIJ") revealed documents related to off-shore activities of individuals and companies named "Paradise Leaks".

Simultaneously with these public disclosures, the last six months has seen the results of many transparency initiatives, including the final report and recommendations of EU Parliament's 'PANA' Committee of Inquiry, new beneficial ownership transparency requirements in context of the politicial agreement on the 5th EU Anti-Money Launderign Directive, as well as policy initiatives for mandatory disclosure of aggressive tax avoidance schemes at both EU (The 'Tax Intermediaries' Directive) and OECD level (model mandatory disclosure rules).

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Tax Intermediaries Directive

01

EU Commission's 'Tax Intermediaries' proposal...

Renewed anti-tax avoidance efforts

Back in May 2016, the ECOFIN Council of EU finance ministers invited the Commission to consider legislative initiatives on mandatory disclosure rules inspired by OECD BEPS Action 12 in order to introduce effective disincentives for intermediaries who assist in tax evasion or avoidance schemes. The European Commission proposal arrived mid-2017 as a directive on mandatory disclosure of reportable cross-border schemes coupled with automatic exchange of information among Member states. Commission had in mind transparency rules for tax intermediaries that develop, market, sell and assist in tax avoidance schemes. Pressure to introduce mandatory disclosure rules at EU level came from the European Parliament with the resolution of 6 July 2016 on tax rulings and other measures similar in nature or effect.

Technical aspects of the proposed directive

The proposal foresees that intermediaries bear the burden of disclosure to tax authorities, if they are involved in the design or promotion of an aggressive tax planning arrangement with cross-border implications. The disclosed information to national tax authorities shall be automatically exchangeable by tax authorities of all member states. Where the obligation to disclose is not enforceable due to absence of an intermediary, or due to legal professional privilege, the directive defaults the disclosure obligation to a taxpayer who is benefiting from the arrangement.

On basis of the proposal, intermediaries shall disclose reportable arrangements within 5 days beginning on the day after an arrangement becomes available for implementation to the taxpayer. With taxpayers, the obligation to disclose is within 5 days once implementation has commenced. In respect of hallmarks, the proposed directive operates with a main benefits test alongside generic and specific hallmarks. The generic hallmarks include: confidentiality from competitors, confidentiality from the tax authorities, premium fees and 'off-the-shelf' schemes. Specific hallmarks include hallmarks related to the main benefit test, specific hallmarks related to cross-border transactions, to transfer-pricing and specific hallmarks concerning automatic exchange of information.

The Commission proposal comes in the form of a 5th amendment to the Directive on mandatory automatic exchange of information in the field of taxation ("DAC"). As with all tax files, per Article 115 of the Treaty on the functioning of the European Union, this Commission proposal requires a unanimous support in Council by all member states, following an opinion from the European Parliament.

...and European tax advisers' position.

CFE Tax Advisers Europe welcomed Commission's policy direction on increased tax transparency, but urged a cautious approach and technical refininement of the proposal before adoption.

The European tax advisers welcomed EU's policy direction for increased transparency and efforts to strengthen the integrity of the tax systems, in particular the renewed efforts for increased tax certainty. CFE opined that the design of certain aspects of the proposal had nevertheless left scope for uncertainty and could face the challenge of divergent implementation in member states.

A technical refinement of the proposal necessitates clear and concise definitions. Rules that are too widely drawn are overly burdensome for taxpayers and unhelpful for tax authorities, which stand to receive massive numbers of disclosures but very little useful information.

CFE argued that the proposal could benefit from including a requirement for member states' tax administrations to issue implementation guidance, providing clarity in relation to determining what is required to be disclosed. CFE further advocated adherence to the OECD BEPS 12 principles, whereby the member states define country specific hallmarks together with a list of excluded tax regimes and outcomes that are not required to be disclosed.

Bearing in mind that hallmarks define what constitutes a reportable cross-border arrangement, these essential features should be well-defined, clear and concise. CFE argued that the 'main benefits test' needs to be applicable to all hallmarks in order to ensure that the reporting obligation is limited to relevant arrangements only. The directive should specify a range of penalties applicable to infringement of national provisions adopted pursuant to the directive concerning Article 8aa) and Article 8aaa). Conversely, penalties that are 'effective, proportionate and dissuasive' could be subject to different interpretation by member states.

CFE welcomed the professional privilege waiver of the proposal, however remarked that a clear distinction needs to be acknowledged between ordinary tax advice (as it is provided by the vast majority of tax advisers) and marketed, 'off-the-shelf' schemes (provided by a small minority).

Direct Tax

02

Taxation of the digital economy.

The last 6 months has seen the EU, OECD and national governments intensively focusing on the fair taxation of the digital economy – and in particular ensuring that the large U.S. tech giants pay a "fair share" of tax in Europe, where these companies have thriving consumer markets. The following is a summary of the main developments across the different institutions.

Priority of Estonian Presidency & European Commission letter of intent.

The Estonian Presidency highlighted that the taxation of the digital economy would be a priority and followed through by initiating a high-level discussion in July 2017. The Estonian position was bolstered with a letter to the Presidency on 13 September from President Juncker indicating the European Commission's intent that a legislative proposal would be published in spring 2018 establishing EU rules for the fair taxation of profits generated by digitalised MNEs in Europe.

This was followed by technical work being carried out and discussed at the informal ECOFIN in Estonia on 15 and 16 September. Finance ministers discussed the proposals for a fundamental reform of the international tax rules to amend the definition of the concept of permanent establishment, with the introduction of the concept of 'virtual' PE, whereby a taxable presence for multinational companies would be considered sufficient to have a taxable presence. Technical discussion also examined the specifics of the sharing economy and the valuation of data for tax purposes.

France, Germany, Spain & Italy put the pressure on tech giants….

Concurrently, the domestic political establishments of France and Germany began an initiative to tax large U.S. Tech companies operating in their markets. The French Tax authorities had recently suffered defeat in the French Supreme Court and failed in their attempt to establish the existence of a PE by Google's Irish entity (Google Ireland Limited) in France and consequently levy 1.2 billion euro in tax. France, Germany Italy and Spain issued a letter calling on the European Commission to explore options and "*propose any effective solutions based on the concept of establishing a so-called "equalisation tax" on the turnover generated in Europe by the digital companies*". The letter further stated that '*The amounts raised would aim to reflect some of what these companies should be paying in terms of corporate tax*." The letter was subsequently signed by 6 other Member States.

European Commission's #DigiTax proposal.

The proposal came at a time when the OECD was also indicating its openness to examining the definition of PE in the context of the taxation of the digital economy. The OECD released a public consultation for input on the tax challenges of the digitalised economy in October 2017. The consultation formed part of the work being carried out by the OECD Taskforce for the Digital Economy's. An interim report is expected in 2018 with a final report due in 2020. CFE submitted an Opinion Statement in response to this consultation.

On 21 September 2018, days after taxing the digital economy took centre stage at the informal ECOFIN meeting in Estonia, the European Commission published its communication to the European Parliament and Council entitled, 'A fair and efficient tax System in the European Union for the Digital Single Market' (the "Commission Communication"). The accompanying Commission Press Release stated that the Commission was pursuing an ambitious EU agenda on the fair taxation of the digital economy in order to ensure a "*common EU approach to influence the international discussion*", in order to create "*meaningful solutions*" at international level by Spring 2018. At this point the press release indicated that the Commission wished to utilise the existing CCCTB framework as the optimal means by which to address the tax challenges that arise from the digital economy in the context of the revised permanent establishment rules and the use of formulary apportionment for allocating the profit of large multinational groups. In addition, the Communication stated that "*There is scope within the current CCCTB proposal to examine further enhancements to ensure that it effectively captures digital activities*".

The Commission Communication contained a detailed analysis of digitalisation and its growing impact on the economy. New business models emerging in the digital economy were also examined. It highlighted the effective average tax rates paid by traditional business models versus the newer digital business models – with traditional international business model paying an average effective tax rate of 23.2% compared to a digital B2C model paying 10.1% and digital B2B 8.9%.

The Communication identified two main policy challenges when seeking to tax the digital economy: nexus and value creation, i.e. where to tax and how best to tax. It acknowledged that "the ideal approach would be to find multilateral, international solutions to taxing the digital economy given the global nature of this challenge" but highlighted the lack on international momentum or consensus at that point in time. It was proposed that the EU would be in a much stronger position to lead the international debate if a common position within the EU could be reached.

The Communication outlined three options which should be considered as short-term solutions.

- **Equalisation tax on turnover of digitalised companies**

  This is envisaged to be a tax on all untaxed or insufficiently taxed income generated from all internet-based business activities, including business – to - business and business-to-consumer, creditable against the corporate income tax or as a separate tax.

- **Withholding tax on digital transaction**

  The communication states that this would constitute a standalone gross-basis final withholding tax on certain payments made to non-resident providers of goods and services ordered alone.

- **Levy on revenues generated from the provision of digital services or advertising activity**

  The possibility of applying a separate levy to all transactions concluded remotely with in-country customers where a non-resident entity has a significant economic presence.

The Communication was followed with the publication of a Public Consultation with stakeholders on 26 October seeking input on the shortcomings of the current international taxation framework and possible solutions – both long and short-term to address those shortcomings.

CFE submitted both a response and an Opinion Statement in relation to the Commission Consultation.

What was agreed at the December ECOFIN...

The December ECOFIN Council Conclusions (the "Conclusions") will form the input for discussions at international level on 'digital taxation'. The Conclusions will also serve as a reference for further work at EU level, including with a view to Commission legislative proposals expected in spring 2018. The Conclusions highlight the urgent need to reach a globally accepted tax policy response to the taxation of the digital economy. Whilst accepting that the implementation of the OECD BEPS action items should substantially address the BEPS issues exacerbated by the digital economy, it highlights the need to address the remaining challenge of ensuring that international tax rules are modernised and made suitable for both the digital and traditions sectors of the economy. In this regard it identifies the concept of permanent establishment, together with transfer pricing and profit allocation rules as the essential principles for the global allocation of taxing rights on profits.

The concept of a virtual PE is addressed along with revisiting the transfer-pricing and profit allocation rules in line with the arm's length principle. The Conclusions express the view that the appropriate nexus in the form of a virtual permanent establishment, alongside any changes to the transfer pricing and profit-allocation rules should take into account how value is created within various business models. Furthermore, the Conclusions urge the OECD to come up with appropriate solutions for the network of double tax treaties that are fit for purpose for the global challenges related to taxation of the digital economy. They also reiterate that unilateral solutions in the absence of international consensus can lead to double taxation disputes between Member states that could undermine the Single Market. Finally, the Conclusions state that the EU should closely follow the international response in particular at OECD level and consider appropriate responses. The OECD is expected to publish its report on the taxation of the digital economy in April 2018. The Bulgarian EU presidency intends to follow-up with an EU legislative proposal in spring 2018.

Meanwhile at the OECD.

The proposal came at a time when the OECD was also indicating its openness to examining the definition of PE in the context of the taxation of the digital economy. The OECD released a public consultation for input on the tax challenges of the digitalised economy in October 2017. The consultation formed part of the work being carried out by the OECD Taskforce for the Digital Economy's. An interim report is expected in 2018 with a final report due in 2020. CFE submitted an Opinion Statement in response to this consultation.

Direct Tax –
The ‘Other Files’

03

CCTB/CCCTB.

During the summer months the French Government worked with the German government to formulate a simplified bilateral CCTB proposal no later than 2018 that they believe should serve as basis for tax (rates) harmonisation within the Eurozone. A multilateral agreement known as 'enhanced coopoeration' is possible within the EU, with a possibility for other EU member states to join at a later stage. Under the so-called 'enhanced cooperation' procedure at least nine EU member states can do so, with voluntary participation of other EU countries. The CCCTB was discussed also in the context of the digital economy as an effective long term means of taxing the digital economy. The European Commission Public Consultation on the Fair taxation of the Digital Economy listed it as a possible long term solution by implementing new permanent establishment and profit attribution rules through modifications to the existing CCCTB proposal. Two draft reports were published in the European Parliament in July. The following is a summary of the main points contained in the Report regarding CCTB**:**

- Alignment with CCCTB (Cannot exist without CCCTB, therefore link must be strengthened; Propose aligning implementation date of 2 directives (2020) Temporary provisions (cross-border loss relief) should be excluded
- Digital PE (Inclusion of factors to define digital presence in terms of establishment of a permanent establishment, Definition should also address "situations in which companies which engage in fully dematerialised digital activities are considered to have a permanent establishment in a Member State if they maintain a significant present in the economy of that country" (Amendment 19)
- Lower Threshold (Reduction of 750 million euro to 40 million euro, Minimum Rate of Taxation, Propose introduction of a minimum rate of taxation in order to level the playing field between MNEs and SMEs)

The following are some of the main points made in the Report concerning the consolidation aspect, the CCCTB: Flexible mechanisms are necessary to adjust to BREXIT and expected overhaul of the U.S corporate tax system; The specifics of the Digital Economy must be captured; Commercial value of personal data must be taken into consideration. More specifically it was proposed that within formulary apportionment a fourth factor should be included – personal data collection and exploitation for commercial purposes. Finally, it was proposed that implementation of the consolidation element must be aligned with the CCTB. A debate of the European Parliament on 30 August 2017 exposed the divergences of opinion held by MEPS on these Reports. A final plenary vote is scheduled for 18 January 2018. However, it should be noted that the Parliament is only empowered to issue a non-binding opinion in relation to this and other tax files.

Country-by-Country Reporting.

The summer months saw a number of developments in the path towards public country-by country reporting.

European Parliament

On 12 June, two committees of the European Parliament, the Committee on Economic and Monetary Affairs (ECON) and the Committee on Legal Affairs (JURI) approved a proposal requiring MNCs to report details of their activities in every EU country in which they operate. The information to be published will include turnover, profits and taxes paid. A carve-out was included in the proposal whereby MNCs will not be obliged to publish commercially sensitive information. The Committees failed to reach the qualified majority required to enter into negotiations with the Council. Therefore, the draft report was sent to the fully constituted Parliament to be debated in a plenary session.

On 4 July the Parliament debated the proposals and took a vote to amend the original Commission proposal on public CbCR. Under the proposed changes, MNCs with a global turnover above €750 million per year or more will publish CbCR data in each country they operate in the world, and not only for EU countries and tax havens as indicated in the original Commission proposal. Under the voted text, the income tax information of MNCs will be available publicly on a standardised template, stored in a registry which is to be maintained by the Commission. In a compromise among the various political groups in the European Parliament, MEPs voted to protect commercially sensitive information by allowing MS to grant exemptions from the public CbCR requirements. Data shall still be confidentially submitted from the MS to the Commission. After approving the report by 534 to 98 votes with 62 abstentions, the report was sent back to the Committees (ECON, JURI and DEVE) to commence negotiations with Council in first reading on the basis of a plenary mandate.

Council

On 22 June 2017, the Council issued a proposed Directve compromise text. The Presidency compromise document highlights the changes compared to the Commission's original proposal. The Parliament and the Council have opposing positions on some central elements of the proposals including the threshold MNCs must reach to come within the proposals – with the Parliament proposing a 40 million threshold as opposed to the much higher 750 million threshold being proposed by the Council. In addition, the latest compromise text sees the introduction of measures such as an exception whereby MNCs will not be obliged to publish information which would be seriously prejudicial to the commercial position of the undertakings to which it relates.

ATAD Implementation & Agreement on ATAD2.

Member States are in the process of drafting the necessary legislation to implement the Anti-Tax Avoidance Directive measures. Some Member States are engaging stakeholders and having consultations whilst others are not. Member States are required to have the ATAD 1 measures adopted by 1 January 2019, and the exit tax provisions adopted by 1 January 2020. The ATAD 2 was agreed in May of the year (discussed in the May edition of the EU & Tax Policy Report) with implementation due for 1 January 2020 and 1 January 2022 for reverse hybrid mismatches.

Dispute Resolution.

In May 2017, The Council of the European Union (ECOFIN) agreed the Directive introducing a new system for resolving double taxation disputes between member states. The Directive was adopted in October. The directive strengthens the mechanisms for resolving disputes among member states that arise from the interpretation of double taxation conventions. The provisions will apply from 1 January 2019.

CFE welcomed the Commission's proposals to expand and improve the mechanisms available to Member States to resolve double taxation disputes with the introduction of a Council Directive.

In particular, CFE welcomed the following salient improvements:

- Extension of the scope: A crucial element of the Proposed Directive is the extension of the scope of relevant disputes beyond just transfer pricing to include all taxpayers that are subject to taxes on income and capital under bilateral tax treaties and the Convention.
- Increased effectiveness & efficiency in the process: In order to increase effectiveness the Proposed Directive introduces a stipulation for the mandatory resolution of disputes subject to strict and enforceable timelines, this is a positive development for taxpayers and for tax certainty generally.
- Taxpayers' role and rights: The Proposed Directive seeks to empower the taxpayer and strengthen their role in the process. Taxpayers have always had the right to institute proceedings. However, the Proposed Directive seeks to empower the taxpayer during the process, for example, by notifying them of the terms of reference of the dispute, the proposed timeframe for completion and the terms of conditions of taxpayers' or a third parties involvement. CFE welcomes these proposals and believes such measures will increase tax certainty and reduce administrative burden for taxpayers. CFE believes that the proposal allowing the taxpayer recourse to the national courts to ensure compliance in the event that the appropriate mechanisms are not applied is essential to a successful system of dispute resolution. In addition, the incorporation of an independent advisory council to make assessments at different stages, for example, if a taxpayer's complaint is rejected, or in the event that the two Member States fail to reach agreement to eliminate double taxation pursuant to the MAP procedure will be an invaluable development from the perspective of ensuring taxpayers' right are protected.
- Alternative dispute resolution mechanisms: One of the salient improvements under the Directive is the inclusion of an additional layer of protection in the form of an automatic and mandatory arbitration procedure to be completed within fifteen months in the event that the Member States fail to reach a conclusion to the initial MAP phase. CFE welcomes the proposal to have an option between an Advisory Commission and an Alternative Dispute Resolution Commission. In particular, CFE believes the broader and more flexible approach to the form of alternative resolution procedure, which can be applied, will greatly improve the process for both the competent authorities and the taxpayer.

Indirect Tax

‘The Main Event’

04

Commission's VAT proposal.

On 4 October the European Commission published a comprehensive proposal to completely overhaul the current system of VAT in the EU, replacing the transitional system with the definitive system of VAT. The proposals follow the European Commission's VAT Action Plan of April 2016. The current system was intended to be only a transitional system but has lasted 25 years – the new proposals for what is known as the definitive VAT system have therefore been a long time goal of the Commission.

The Commission believe the transitional VAT system is no longer fit for purpose in today's more dynamic and highly digitalised economy. In its present form of operation, the VAT system is fragmented, disrupts the cross-border operations of digital businesses and SMEs and most importantly highly susceptible to fraud. The Commission aim to have a robust simple system which is resilient to fraud and lowers the compliance burden.

The proposals outline the cornerstones of the new system and seek to establish a so-called definitive VAT system for intra-EU cross-border trade based on the "destination principle". The destination principle seeks to ensure that the final amount of VAT is paid in the final consumer's Member State at the rate applicable in that Member State.

The Cornerstones:

Destination based principle

The change to a destination-principled VAT system will substantially impact all businesses trading in the EU Single Market. Under a destination-based VAT system, the supplier shall be liable for VAT at a rate applicable in the Member State of destination. Goods traded cross-border will be taxed in the country where they are consumed (the destination country) and at the destination country's tax rate, rather than where they are produced (the origin country). Under the proposal, the supplier will be obliged to account for VAT at the rate applicable in the destination Member State. Whilst tax will be collected by the country of origin it will ultimately be transferred to the destination country. The mechanism for allowing this new destination system to operate is known as the One Stop Shop.

One Stop Shop ("OSS")

The suppliers will not be required to register in the destination Member State for VAT purposes, but can avail of the 'one-stop-shop' digital portal. By means of the 'one-stop-shop' businesses will be able to file declarations and declare VAT on cross-border transactions in a single return with the same rules and the language of their state of establishment. Member states will accordingly settle their VAT that is due directly.

Cross- border B2B transactions

Under the current rules, B2B cross-border supplies of goods are exempt from VAT, in the sense that the transaction is split between an exempt intra-EU supply of goods in the Member state of origin, and, a taxable intra-EU acquisition in the Member state of destination. This design of the VAT system amounted to substantial revenue losses, with the VAT gap estimated at circa 50 billion euro per year. The Commission thus propose the introduction of a single taxable supply in the member state of destination.

Simplification of VAT invoicing rules

This would allow sellers to prepare invoices in accordance to the rules applicable in their own Member State. There will also be an end to the necessity to complete recapitulative statements (list of cross-border transactions for the tax authority).

Certified Taxable Person – a new concept in VAT

The proposed new concept of a certified taxable person ("CTP") is a key element of the new proposals regarding a definitive VAT regime. The CTP is analogous to the Authorised Economic Operator ("AEO") number in the customs context (although the AEO contains 5 eligibility criteria). A business with this certification will be considered a reliable VAT taxpayer throughout the EU and therefore be subject to lesser administrative constraints and eligible to apply some of the so-called quick fixes. In order to receive the classification, businesses must apply to the national tax authority of the Member State of establishment and demonstrate that they have satisfied the 3 criteria contained in the proposed Article 13a (2) of Directive 2006/112/EC. The 3 criteria focus on compliance record, procedures and financial solvency.

Quick Fixes & Implementation.

Quick Fixes

- Call-Off stock arrangements - Simplification and harmonisation of rules regarding call-off stock arrangements
- VAT identification number – recognition of VAT identification number of the customer as a substantive condition in order to exempt from VAT an intra-Community supply of goods;
- Chain transactions - Simplification of rules in order to ensure legal certainty regarding chain transactions
- Proof of intra-Community supply – Common frame work of recommended criteria for the documentary evidence required to claim an exemption for intra-Community supplies

Steps to implementation

The full modernisation of the exiting VAT System will be carried out in via numerous legislative proposals. In addition to the primary legislative proposals in relation to the definitive VAT regime outlined below the following legislative proposals will also be made:

- Reform of VAT rates
- Simplification of VAT rules for SMEs and
- Reinforcing the existing instruments for VAT Administrative Cooperation (discussed further below)

The definitive VAT regime will be implemented in 2 steps.

- The new VAT system will initially apply only to B2B supply of goods;
- After 5 years of monitoring by the European Commission the new system would be expanded in scope to apply also to services.

The implementation of phase 1 will in turn be split into 2 parts:

- Implementation of temporary measures known as the 4 Quick Fixes to address some of the problems in the existing system. Identify the cornerstones of the new system and reach agreement on these principles.
- The specific technical provisions of the corner stones will be published in 2018.

The CFE has issued an initial Opinion Statement on the Commission Proposals and will be following up with subsequent Opinion Statements as more details are published.

Other VAT developments:

Strenghtning administrative cooperation

On 30 November, the European Commission published a draft Regulation to strengthen administrative cooperation between the tax authorities of Member States. It seeks to amend Regulation (904/2010) regarding measures to strengthen administrative co-operation in the field of VAT. The legislative initiative seeks to swiftly improve how tax authorities cooperate not only with each other but also with other law enforcement bodies across the EU. It comes in preparation for the full implementation of the definitive VAT regime and follows on from the proposal of fundamental cornerstones of the new system as published in October.

The primary elements of the proposal seek to:

Strengthen cooperation between Member States by putting in place an online system for information sharing within 'Eurofisc', the EU's existing network of anti-fraud experts. The system would enable Member States to process, analyse and audit data on cross-border activity to make sure that risk can be assessed as quickly and accurately as possible. To boost the capacity of Member States to check cross-border supplies, joint audits would allow officials from two or more national tax authorities to form a single audit team to combat fraud - especially important for cases of fraud in the e-commerce sector. New powers would also be given to Eurofisc to coordinate cross-border investigations.

Increase interaction with other law enforcement bodies by opening new lines of communication and data exchange between tax authorities and European law enforcement bodies on cross-border activities suspected of leading to VAT fraud: OLAF, Europol and the newly created European Public Prosecutor Office (EPPO). Cooperation with European bodies would allow for the national information to be cross-checked with criminal records, databases and other information held by Europol and OLAF, in order to identify the real perpetrators of fraud and their networks.

Share key information on imports from outside the EU by further improvng information sharing between tax and customs authorities for certain customs procedures which are currently open to VAT fraud. Under a special procedure, goods that arrive from outside the EU with a final destination of one Member State can arrive into the EU via another Member State and transit onwards VAT-free. VAT is then only charged when the goods reach their final destination. This feature of the EU's VAT system aims to facilitate trade for honest companies, but can be abused to divert goods to the black market and circumvent the payment of VAT altogether. Under the new rules information on incoming goods would be shared and cooperation strengthened between tax and customs authorities in all Member States. The Proposed Regulation is available here.

Temporary reverse charge.

European finance ministers failed to reach agreement on allowing certain member states to apply a generalised reverse charge mechanism. The proposal seeks to combat VAT fraud. The generalised reverse charge proposals follow a request from member states significantly affected by VAT fraud, namely Austria and the Czech Republic.

The proposed directive offers a solution to the so-called 'missing trader' or 'carousel' fraud, where supplies are traded several times without payment of VAT due on the transactions. Under present rules, reverse charge can be applied as temporary measure only, whereas the proposed directive would establish a generalised system applicable on a voluntary basis until 30 June 2022. The Commission presented an analysis of the possible application of the generalised reverse charge mechanism in Austria and the Czech Republic. Whilst the finance ministers were positive about the proposals at the June ECOFIN meeting, potential problems were also discussed, including legal difficulties and disputes arising along with an increase in untaxed goods and services. The initiative did not reach conclusion during the Estonian Presidency, and negotiations are ongoing with no conclusions reached. It remains to be seen if it will be a priority of the Bulgarian Presidency.

VAT on E-Books.

A proposal to align the VAT rate on electronic publications with that of traditional publications had a difficult road to conclusion with failure to get unanimous support at the June ECOFIN meeting. Although the proposal had strong support from many member states the Czech Republic voted against it requesting a wider solution for VAT rates and the digital economy be looked at. This was widely seen as a negotiation tactic in the battle on the other proposal for a temporary reverse charge mechanism discussed above. However, agreement was reached between France and the Czech Republic and the proposal on EBooks was approved without debate at the December ECOFIN meeting.

EU Policy – Anti- Money Laundering

05

Agreement on the 5th AMLD.

The Council of EU and the European Parliament reached a political agreement on 15 December on the EU Commission's proposal to amend the Fourth Anti-Money Laundering Directive. The amended directive ('5th AMLD') seeks to prevent large scale concealment of funds and to introduce increased corporate transparency rules, whereby corporate and other legal entities will be required by law to publicly disclose information on the beneficial ownership.

Transparency requirements for corporate entities and trusts

Under the new rules, member states shall be required to ensure compulsory public disclosure of certain information on beneficial owners in respect of companies and legal entities engaging in profit-making activities as per Article 54 TFEU. Conversely, public access requirements are not put in place in respect of trusts and other legal arrangements. The 5th AMLD recognises that trusts may also be set up for non-commercial purposes, such as charitable aims, use of family assets, and other purposes beneficial to the community/ general public. Considering that such arrangements do not qualify as business benefits, the essential data on trusts' beneficial owners shall only be granted to persons holding a legitimate interest. Similarly, the 4th AMLD already grants competent authorities access to beneficial ownership of trusts and other legal arrangements, albeit in limited circumstances.

Virtual currencies and verification

The 5th AMLD introduces a requirement for member states to verify beneficial ownership information submitted to their beneficial ownership registers as well as an extension of anti-money laundering legislation applicability to virtual currencies.

Third-countries

With respect to transactions involving third countries, the obliged entities shall apply enhanced customer due diligence measures set out in the directive. Member States will introduce such rules as a requirement for all transactions with natural persons or legal entities established in third countries identified as high-risk countries pursuant to Article 9 (2) of the Directive.

Timeline and background

On 12 February 2016, the ECOFIN Council (EU finance ministers) called on the Commission to initiate amendments to the 4th AMLD in the second quarter of 2016 the latest. The informal ECOFIN Council also called for action in April 2016 to enhance the transparency of beneficial ownership registers, to clarify the registration requirements for trusts, to speed up the interconnection of national beneficial ownership registers, to promote automatic exchange of information on beneficial ownership, and to strengthen customer due diligence rules.

The EU's current AML revised framework was adopted on 20 May 2015, consisting of the 4th AMLD and Regulation (EU) 2015/847 on information accompanying transfers of funds. The transposition deadline for the 4th AMLD and the entry into force of Regulation (EU) 2015/847 was set for 26 June 2017. The EU's supranational risk assessment was also published in June 2017. Following the political agreement between the co-legislators and subsequent adoption of the directive, EU member states will have 18 months to implement the 5th AMLD into national legislation.

AML Supranational Risk Assessment Report.

Simultaneously with the policy developments related to the 5th European Union Anti-Money Laundering directive, the European Commission continued with steps on implementation of the 4th Anti-Money Laundering Directive. Pursuant to the mandate of Article 6 of the Directive (EU) 2015/849, before the summer holidays the European Commission finalised the supranational risk assessment report. The Report includes mapping of risks per relevant area, recommendation for member states how to identify and address the risks accordingly with focus on the supervisory activities.

PANA Committee of Inquiry, EU 'Blacklist' & #StateAid Update

06

European Parliament Inquiry Report & Recommendations.

European Parliament's prominent and assertive role in the area of tax has been visible throughout the second half of the year. Following the publication of the PANA Committee Draft Report on the inquiry on money laundering, tax avoidance and tax evasion and Draft Recommendations to the European Commission and the Council of EU of 28 June 2017, 667 amendments to the Draft Report and 783 amendments to the Draft Recommendations were tabled.

With relevance for the tax advisory profession, the Draft inquiry recommendations called for a shift from self-regulation to appropriate supervision and state controlled regulation for currently self-regulated professions via a separate and independent national regulator/supervisor. The Committee further recommended for regulation of tax intermediaries with incentives to refrain from engaging in tax evasion and tax avoidance and shielding beneficial owners, as well as creation of an EU legal framework for compulsory codes of conduct for tax intermediaries. Finally, an EU certification of intermediaries to practice as tax professionals was recommended with calls to withdraw licences from tax professionals where they are engaged in enabling tax evasion, aggressive tax planning and money laundering. The Committee also called on the Commission to propose EU-wide legislation on the protection of whistleblowers with a horizontal legislation covering both the public and private sectors.

The Report and the 211 recommendations to Council and Commission were approved at Parliament's plenary mid-December in Strasbourg, by 492 votes to 50 with 136 abstentions. The recommendations include formation during the next Parliament (2019 -2024) of a Permanent Committee of Inquiry on taxation, modelled on basis of the US congressional committees. In the meantime, a Special Committee to follow up on the recommendations would continue the investigative work through the mandate of this Parliament, until May 2019. The PANA Committee of Inquiry held the last session on the Paradise Papers before its mandate expired on 8 December 2017, followed by an address from Commissioner Moscovici who provided a round-up on the EU anti-tax avoidance initiatives.

The final recommendations include unrestricted public access to beneficial ownership registers and stricter regulation, sanctions for tax intermediaries aiding aggressive tax planning, then better regulation for protection of whistleblowers and a common international definition of what constitutes tax haven, offshore financial centre, non-cooperative tax jurisdiction and a high-risk country. MEPs called for more transparency in the Code of Conduct Group on business taxation and radical overhaul of its governance and *modus operandi*. The European Parliament also supported shift from unanimity to qualified majority voting in Council regarding taxation.

EU 'blacklist' of non-cooperative jurisdictions.

Aiming to encourage fair tax competition and global tax transparency standards, the EU approved a list of non-cooperative jurisdiction for tax purposes this December. The list includes 17 countries that are failing to meet European tax good governance standards: American Samoa, Bahrain, Barbados, Grenada, Guam, Korea (Republic of), Macao, Marshall Islands, Mongolia, Namibia, Palau, Panama, Saint Lucia, Samoa, Trinidad and Tobago, Tunisia and the United Arab Emirates. The first European list is part of the EU's efforts to promote tax good governance, to dissuade external threats to EU Member states' tax bases and to address standards of third countries that refuse to cooperate in tax matters.

The EU listing criteria included transparency, BEPS implementation and commitment to fair tax competition. In addition, 47 countries have been 'grey' listed, and have committed to addressing the deficiencies in their tax systems and to meet the required criteria, following a dialogue with the EU. In order to ensure compliance with the EU measures, the EU has designed defensive measures in tax area could be taken by the Member States. Such actions include:

- Non-deductibility of costs;
- CFC rules;
- Withholding tax;
- Limitation of participation exemption;
- Switch-over rule;
- Reversal of the burden of proof;
- Special documentation requirements;
- Mandatory disclosure of specific tax schemes with respect to cross-border arrangements.

In reaction to the EU 'blacklist', the governments of South Korea, Macau, Mongolia, Tunisia, Namibia and Panama condemned this EU action. Panama recalled its ambassador to the EU, whilst other countries denounced the EU measures as "unfair, arbitrary and discriminatory". In this global display of divergent understanding of tax transparency, Korea's finance ministry added that the European Union is not in a position to impose its tax standards on countries like South Korea.

#StateAid: EU Commission looks into U.K. CFC rules.

The European Commission published its Preliminary State Aid Decision as part of the investigation into the U.K.'s Controlled Foreign Company (CFC) legislation and whether it is in contravention of EU state aid rules. The investigation was announced on 26 October 2017. Specifically, the European Commission is looking into U.K.'s group financing exemption for certain financing income (i.e. loan interest payments) that are exempt from the remit of the CFC rules.

U.K. Group Financing Exemption

The Commission is investigating a legislative 'scheme', the UK's Finance Act 2012 which introduced a Group Financing Exemption, effective from 1 January 2013. This 'scheme' exempts from UK corporate taxation financing income received by an off-shore subsidiary from another foreign group company, which allows a UK based multinational company to provide for financing to a CFC group member via an offshore shell without taxing this income. In the absence of the Group Financing Exemption, interest income paid on loans to subsidiaries when that interest is paid into an off-shore jurisdiction would have been subject to tax.

In accordance with the EU Anti-Tax Avoidance Directive, as of 1 January 2019, all Member states must introduce CFC legislation, albeit with a caveat that the ATAD does not intend a group financing exemption such as the one under Commission's State aid investigation. The Commission investigation focuses on a legislative scheme regarding a Group Financing Exemption introduced by the UK's Finance Act 2012 and effective from 1 January 2013. The UK Group Financing Exemption, according to the EU Commission, is providing for selective advantage to multinational group companies when compared with other UK resident entities that do not operate cross-border. According to ECJ settled case-law, national anti-abuse provisions must not be selective and must be compliant with the State aid rules still.

#StateAid*:* The *Amazon* ruling.

Continuing their investigation into potential corporate tax 'sweetheart deals' with EU governments, the EU Commission adopted a decision establishing a tax liability for Amazon in Luxembourg of €250 million on basis of the EU State Aid rules.

Commission's Amazon State aid inquiry focused on a tax ruling issued to Amazon in 2003 and extended in 2011. The Commission claim that this ruling endorsed a method of calculation of annual payments from the operating company to the holding company for the rights to the Amazon intellectual property, which exceeded, on average, 90% of the operating company's operating profits. Commission say that the profits were significantly higher than what the holding company was due to pay to Amazon US under the terms of the cost-sharing agreement.

Under Luxembourg's tax law, the operating entity is subject to corporate tax whilst the holding company is not due to the chosen legal form - a limited partnership with US partners. The taxation rights to the partners' profits thus belong to the United States, with the US tax liability being consistently deferred. Under the tax ruling, the holding company was a shell company that passed on intellectual property rights to the operating company. The Commission further claim that the holding company was not actively involved in the development the IP and did not perform any activities that would justify the level of royalty it received. In this way, three quarters of Amazon's profits were unduly attributed to the holding company, where they remained untaxed. This tax structure was endorsed by a tax ruling issued by the Luxembourg government, which amounted to selective advantage for Amazon. The Commission does not challenge the structure itself, rather the tax ruling that endorsed artificial methods for taxation of profits that amounted to selective advantage for Amazon.

Commission have set out the methodology to calculate the back taxes initially estimated at €250 million, plus interest. An action for annulment of a Commission State aid decision does not have a suspensory effect, thus the Luxembourg government is obliged to recover the assessed tax. Under EU law, assessed back taxes under State air rules are not a penalty, rather an assessment that levels the playing field, and does not penalise the operating company beneficiary of the State aid.

Currently, DG Competition is looking into the more tax rulings from Luxembourg, as regards the corporate tax treatment of IKEA, McDonald's and GDF Suez (now Engie).

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