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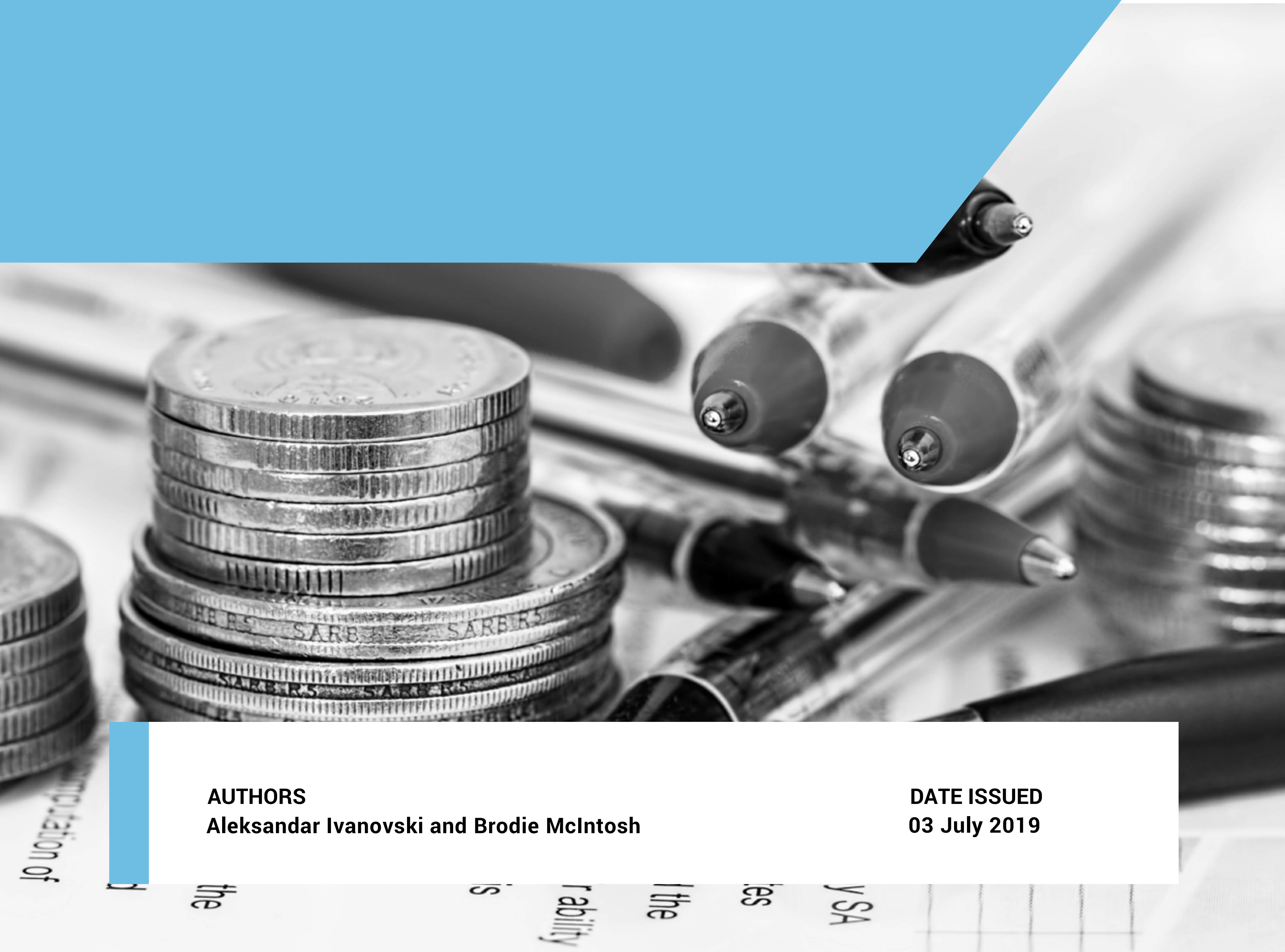
EU Tax Policy Report

January – June 2019



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CFE's EU Tax Policy Report provides a detailed analysis of primary tax policy developments at EU level of interest to European tax advisers. It also includes an overview of relevant CJEU case-law European Commission decisions covering the first half of 2019.

Highlights

This year began with a bang, with the Commission issuing a communication in January setting out a 4-step plan identifying certain areas in tax matters where it proposes to move to qualified majority voting (QMV) by making use of the Passerelle clauses contained in the Treaty on European Union. However, the prospects of the plan seem bleak, as Ministers at the February 2019 ECOFIN meeting were quick to call for keeping the current balance of voting rules in taxation and certain Member States since stating they would oppose the proposals. As in 2018, progress of the EU digital tax proposals was again a main focus of the ECOFIN Council (Economic and Financial Affairs), but progress under the Romanian Presidency was also frustrated. Attention turned quickly to the OECD, and the public consultation in March saw new proposals from the OECD that effectively go beyond digital and certainly beyond the Arm's Length Principle.

The first half of 2019 was also in large part dominated by the run up to the EU elections, meaning there were fewer tax legislative proposals emanating from the European Commission. In the run up to the EU elections, the Brussels-bubble was dominated by the various debates between the likely candidates for the post of the EU Commission president. Politico Europe, Maastricht University and the European Youth Forum organised the *Maastricht debate*, where candidates expressed their support for more regulation of the American tech companies operating in the Single Market as a matter of priority. Frans Timmermans stated that the EU must act to tax the big tech companies and to ensure that citizens retain ownership and control over their personal data. Considering the public interest in the regulatory and enforcement powers of the European Commission vis-à-vis these businesses, it is likely that many related policy areas such as taxation, copyright and data protection will continue to be high-up on the next Commission's agenda. In addition to digitalisation, climate change and sustainability, taxation was among the topics that raised interest and debate.

As to the files to watch in the upcoming semester, the Council of EU High Level Working Party (Taxation) convened a meeting on 7 May in Brussels, to discuss significant taxation issues faced by the EU. The Working Party exchanged views on international digital taxation, the state of play of the Financial Transaction Tax, a Commission Communication on energy/climate and taxation and transfer pricing. In relation to indirect taxation matters, the group examined excise duties on alcohol in relation to a submission to ECOFIN concerning amendments to the Council Directive, as well as the common system of VAT in relation to SMEs, which is anticipated to be agreed in the coming months.

All eyes are now on Brussels, where the European Council leaders are discussing names for the top EU jobs, including the EU Commission & EU Council presidency and the head of the European Central Bank - the regulator of the Eurozone.

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QMV…NOT TO BE…? 01

The EU Commission's Qualified Majority Voting Roadmap

On 15 January, the European Commission published a communication which set out a 4-step plan as to how decision making on tax matters could be modified to take place by way of qualified majority voting. The Commission proposes that the European Council could utilise the Passerelle clauses contained in Article 48(7) and Article 192(2) of the Treaty on European Union, which allows the Council to change decision making from unanimity to qualified majority voting, whereby legislative proposals can become EU law if supported by a minimum number of EU countries, representing a minimum share of the EU population. The clauses would allow Council to produce initiatives indicating the scope of proposed changes in the decision-making procedure, and notify National Parliaments. If not opposed within 6 months, the European Council can then adopt the decision by unanimity, after obtaining the consent of the European Parliament.

The Commission in its communication states that unanimity in decision making in tax matters has hampered progress on important tax initiatives, needed to strengthen the Single Market and boost EU competitiveness, and identifies the "cost" of non-action in EU Tax Policy as failure to progress the VAT definitive regime, CCTB & CCCTB, the financial transactions tax and the digital services tax proposals. The communication proposes a 4-step process to modify the way the EU exercises its competences in taxation as follows:

Part 1 – Employ QMV for measures that have no impact on Member States' taxing rights, bases or rates, but are critical to combat tax fraud, evasion and avoidance and in facilitating tax compliance in the Single Market.

- Aimed at measures such as administrative cooperation and mutual assistance, legislating BEPS actions and reporting obligations.
- Suggested timeframe of Commission: "decision to be taken swiftly".

Part 2 – Employ QMV for measures of a fiscal nature designed to support other policy goals.

- Aimed at measures that support EU policy goals such as measures concerning climate change, environmental protection, public health or transport policy.
- Suggested timeframe: "decision to be taken swiftly".

Part 3 – Introduce QMV in areas that are largely harmonized but which must evolve and adapt to new circumstances.

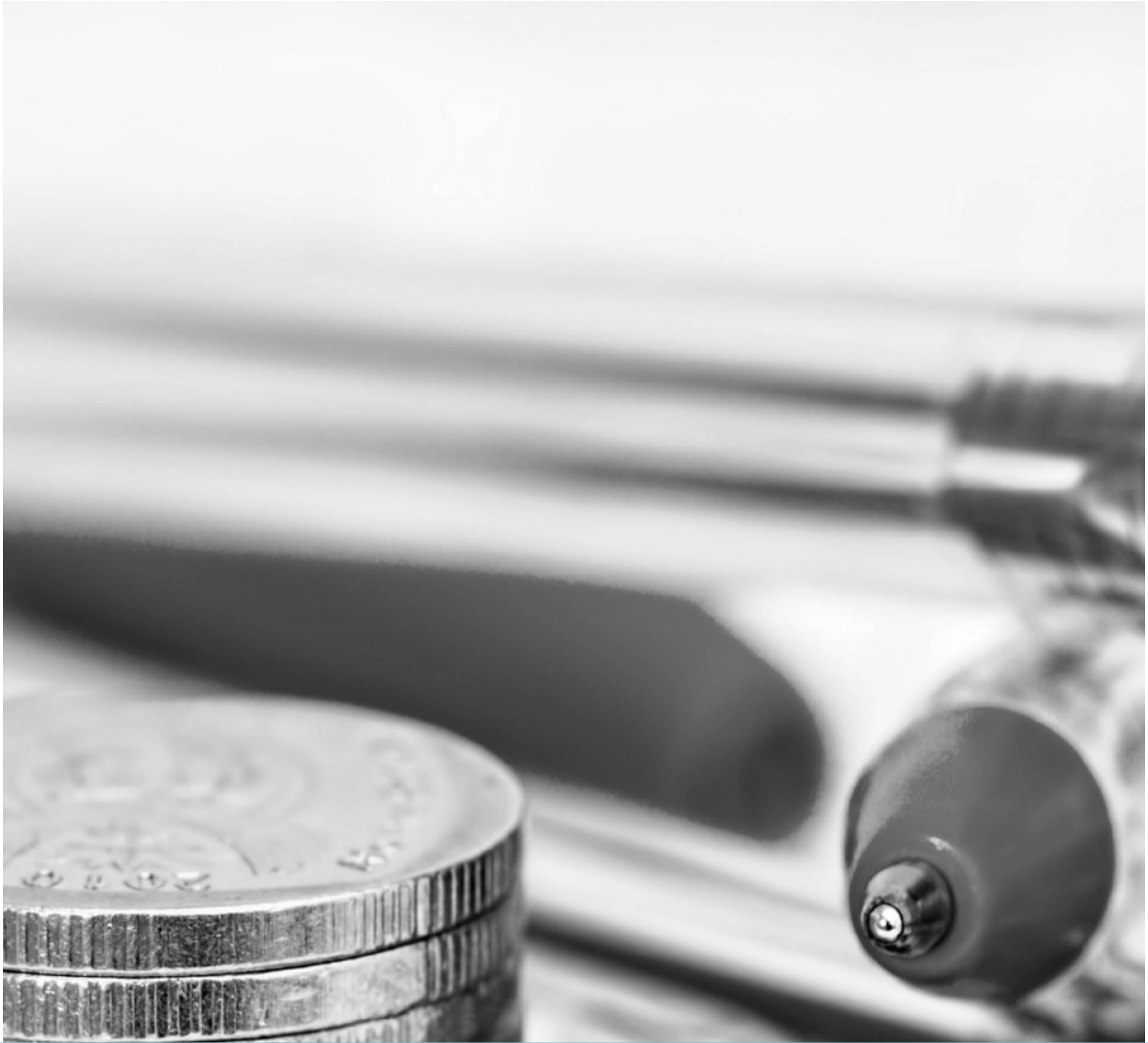
- Aimed at measures relating to VAT and excise duties.
- Suggested timeframe for implementation: by 2025.

Part 4 – Introduce QMV for other initiatives in the taxation area necessary for the Single Market and for fair and competitive taxation in Europe.

- Aimed at initiatives/measures such as CCCTB, taxation of the digital economy etc.
- Suggested timeframe: by 2025.

At the ECOFIN meeting on 12 February 2019, ministers held an exchange of views on the Roadmap, during which a number of ministers called for keeping the current balance of voting rules in taxation, noting the considerable work achieved to date in the area of EU tax legislative files under current rules. Whilst others showed openness towards examining whether there is room for improvement, Croatia, Cyprus, Czechia, Estonia, Hungary, Ireland, Latvia, Lithuania, Luxembourg, Malta, The Netherlands, Poland, Slovakia, Slovenia and Sweden were reportedly all opposed. In May, Ireland and the Netherlands, ahead of the EU summit which took place in Romania concerning the future of the EU, stated that the countries *"strongly believe that tax is a sovereign issue, that individual member states should decide for themselves".* Ireland then went on to issue a government statement saying that Dublin "does not support any change being made to how tax issues are agreed at EU level". Malta's Finance Minister has also stated Malta will oppose any attempt to erode any rights obtained by membership.

It would seem that agreement on use of the Passerelle clauses, for now, is at an impasse.



Taxation of the Digital Economy

02

Taxation of the Digital Economy: The New WTO (World Tax Order)?

EU PROGRESS GRINDS TO A HALT…

During the course of the Romanian Presidency, the Council of the European Union sitting as ECOFIN (Economic and Financial Affairs Council) failed to reach agreement on European Commission proposals for a digital services tax in the EU. This was not surprising given the (then) Austrian Presidency note at the end of 2018 concerning the proposed EU digital tax, which set out that certain delegations were as a matter of principle unable to agree to the proposal, irrespective of technical revisions made by the Presidency, and that a number of other delegations reportedly had concerns as to specific provisions in the draft legislative proposal. The Nordic countries and Ireland reportedly vetoed the EU plans in March at Council level.

The frustrations of some Member States in the stalling of the process led to the introduction of unilateral digital taxes at national level by Austria, Czechia and Italy this semester. To date, Austria, Czechia, France, Italy and Spain have all imposed national measures. The UK also launched a consultation in December 2018 concerning imposing its own national digital tax.

In May, Ireland and the Netherlands reiterated that both countries support global solutions to issues surrounding taxation of large corporations, and opined that the OECD was making good progress on finding a fair method to tax digital entities.

EU Finance Ministers were accordingly unable to agree a common position for OECD negotiations on digital tax reforms at their latest ECOFIN meeting ahead of the G20 Osaka summit which took place on 28-29 June, with some countries noting they wanted to contribute independently to the OECD work and others preferring a European position. Speaking recently in Paris, Margrethe Vestager, EU Competition Commissioner and an EU Commission presidency candidate, expressed her support for digital tax plans, saying, "The *best thing at present is a global solution, but if we want solutions in a reasonable time, then Europe must step forward."*

BUT SIGNIFICANT MOVEMENT AT THE OECD … THE PLACE TO BE …

March Consultation Document

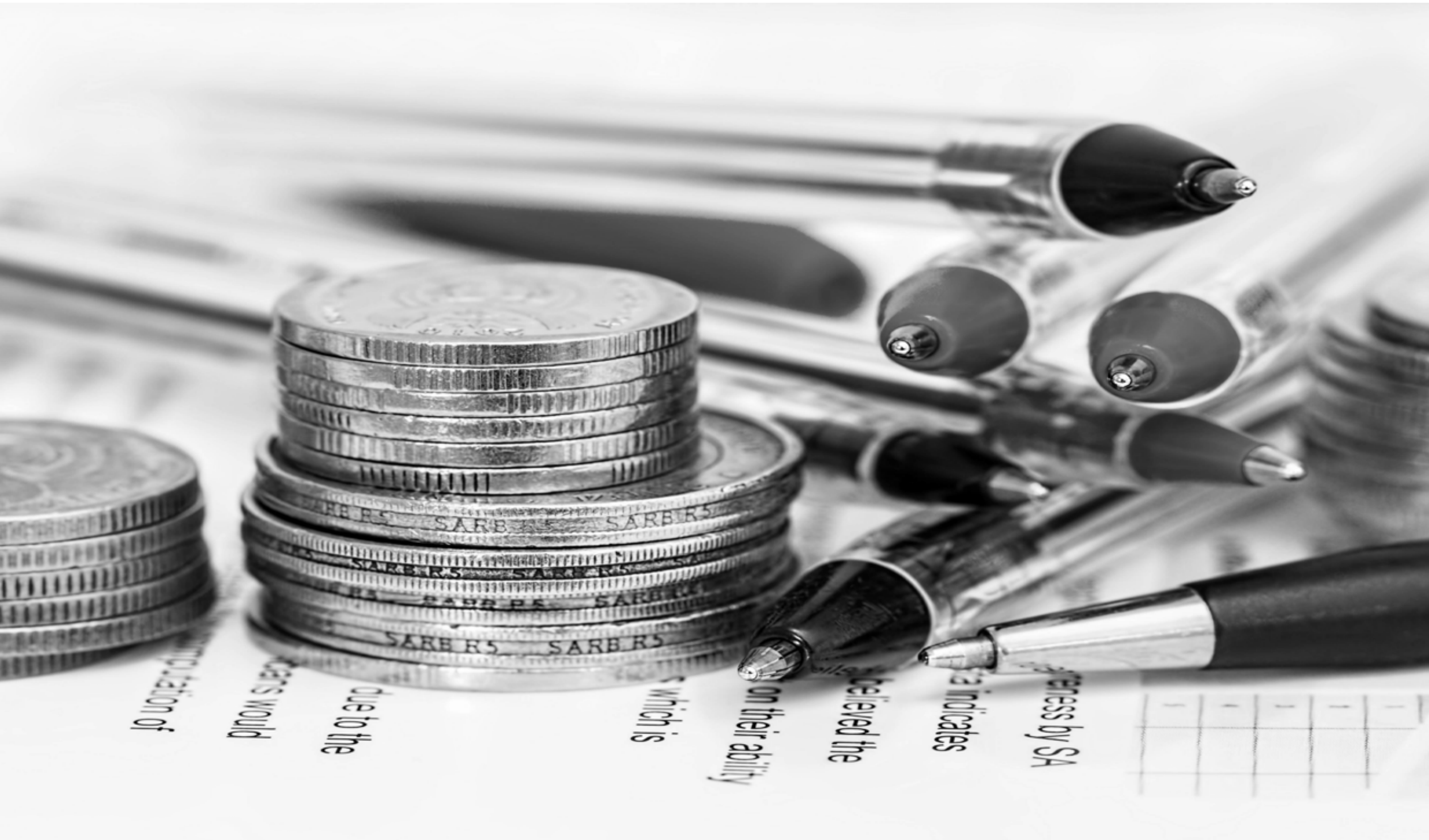
The OECD's Inclusive Framework held a public consultation on 13 and 14 March 2019 in Paris as part of the meeting of the Task Force on the Digital Economy. The consultation was launched following publication of a Policy Note identifying that discussions at OECD level would be based around two pillars. The first pillar focusses on how the existing rules that divide the right to tax the income of multinational enterprises among jurisdictions could be modified to take into account the changes that digitalisation has brought to the world economy.

The second pillar aims to resolve remaining BEPS issues and explores two sets of interlocking rules designed to give jurisdictions a remedy in cases where income is subject to no or only very low taxation. The consultation document invited input concerning a number of technical and policy matters. CFE's submissions concerning the consultation can be viewed here. The consultation document sets out that the Inclusive Framework were at that point in time considering three "solutions" to the question of how to tax the digital economy, namely:

1. **The "user participation" proposal** – this proposal envisages profit allocation changes based on engagement and active participation of users resulting in profit generation, such as from social platforms, search engines and online marketplaces. The proposal sets out that profits derived from user participation could be calculated through non-routine or a residual profit split approach.

2. **The "marketing intangibles" proposal –** this proposal envisages changing profit allocation and nexus rules, applying not only to user participation but also to businesses which are able to either remotely or through a limited local presence create a customer base, such that the market jurisdiction would be entitled to tax some of the non-routine income associated with intangibles.

3. **The "significant economic presence proposal" –** This proposal envisages that having a taxable presence in a jurisdiction would be dependent on a company meeting certain criteria that would establish "*purposeful and sustained interaction with a jurisdiction" sufficient to amount to a significant economic presence*". Allocation of profit under this proposal would be based on a fractional apportionment method.



Consultation Outcomes

400 invited stakeholders from business, professional and trade associations, practice, NGOs and academics attended the March consultation, including CFE Tax Advisers Europe. Not surprisingly, digital businesses expressed reservations about the scope of the user participation proposal and the 'arbitrary' distinction in ring-fencing particular business models. Conversely, non-digital companies articulated concerns about the scope of the marketing intangibles proposal by modifying the application of the arm's length principle. The common ground in discussions concerning the revised profit allocation rules was the importance of simplicity, certainty, the absence of double taxation or unilateral measures and presence of mandatory dispute resolution mechanisms in any future solution. Considering that proposals one and two (user contribution and marketing intangibles) bear similar features, it was suggested these proposals could be implemented through adjusting the present framework without the need to dismantle the whole international tax system. Some participants suggested alternative proposals, and even formulary apportionment, to the extent an agreement on the formulary elements was possible.

More concerns were raised regarding the global anti-base erosion proposals, with some participants highlighting that the residual BEPS issues have little to do with income allocation. Once the profit allocation issues have been resolved, a business representative said, the pressure on pillar two will be reduced considerably. The tax on base eroding payments was assessed as very complex, with issues identified relating to double tax treaties, lack of dispute resolution and, significantly, possible EU law challenges. CFE warned that the pillar two proposals are likely to continue to put pressure on the existing transfer-pricing framework: any disparity in the implementation of minimum tax rate proposals is inevitably going to lead to double taxation.

June Work Programme

In June, the OECD published a work programme on the next steps on taxation of the digital economy. The document also set out modified proposals for profit allocation and nexus rules that take into account tax challenges of the digital economy, based on developments since its March consultation.

The OECD acknowledged the political imperative on reaching an early consensus, considering that the rules will have an impact on revenues and the overall balance of taxing rights among jurisdictions. Regarding the profit allocation methods, the document no longer operates with the proposals set out in the March consultation document, i.e. marketing intangibles and users contribution approach, introducing three similar concepts instead, being:

- Residual profit splits (modified residual profit split method);
- Fractional apportionment method;
- Distribution-based approaches.

On the new nexus rules, the programme indicates that the OECD is now considering new Permanent Establishment rules to take into account digital presence, hence potential modifications to articles 5 & 7 of the OECD Model Tax Convention. The second pillar of residual BEPS issues aims to address further corporate base-eroding practices, with establishment of ab=n income inclusion rule and a tax on base-eroding payments.

The OECD also recently published the Secretary General Report to the G20 Finance Ministers and central banks' governors, which sets out the OECD progress on the international tax reform agenda. The Director of the OECD Centre for Tax Policy and Administration, Pascal Saint-Amans, reported that the US Treasury Secretary Mnuchin, in spite of opposition to the UK and French unilateral measures on digital tax, apparently recognised the positive impetus of such actions in facilitating an internationally agreed consensus, in absence of which, a patchwork of unilateral rules emerges. The bottom line for the US is a solution that will not discriminate between traditional and digital businesses. India, on the other hand, made their case for the significant economic presence proposals.

Progress on the issue of taxation of the digital economy in both the EU and at the OECD level will remain an ongoing priority for CFE.

EU Policy – Direct Tax Files

03

Carrot & Stick: Tax Dispute Resolution Directive & ATAD Become EU Law

ATAD Enters into Force

The provisions of the EU Anti-Tax Avoidance Directive (ATAD) became applicable on 1 January 2019, which was the implementation deadline for national transposition legislation. The Directive contains five legally binding anti-abuse measures, which all Member States should apply against common forms of aggressive tax planning. The anti-abuse measures, apart from hybrid mismatches, include: CFC rules, switchover rules, exit tax rules, as well as GAAR and interest limitation rules.

Article 4 of ATAD required EU Member States to introduce interest limitation rules before 1 January 2019. According to Article 11(6) ATAD, Member States which had existing national rules for preventing BEPS risks as at 8 August 2016, and which are equally effective to the interest limitation rule set out in the ATAD, may apply these targeted rules until 1 January 2024, in line with the OECD minimum standard regarding BEPS Action 4.

On 7 December 2018, the European Commission published in the Official Journal a Notice on national interest limitation measures considered equally effective to Article 4 of the Anti-Tax Avoidance Directive. The measures include: *Spain* — Articles 16 and 63 of 'Ley 27/2014, Del Impuesto Sobre Sociedades (territorio comun)' and Article 24 of 'Ley Foral 26/2016, Del Impuesto Sobre Sociedades (Navarra); *France* — Article 212 bis of 'Code général des impôts ("rabot")'; *Slovakia* — Section 21a of Act No 595/2003 Coll; *Slovenia* — Article 32 of 'Zakon o davku od dohodkov pravnih oseb' (ZDDPO-2); and, *Greece* — Article 49 of Law 4172/2013.

EU Tax Dispute Resolution Directive Enters Into Force

The Council Directive on tax dispute resolution mechanisms in the European Union entered into force on 1 July 2019. It will apply to complaints submitted from 1 July 2019 onwards on disputes relating to income or capital concerning the tax year commencing on or after 1 January 2018. The Directive will significantly improve the tax dispute resolution process; alleviate instances of double taxation and provide for binding dispute resolution process with improved tax certainty for taxpayers. CFE has welcomed the developments with this Directive and will soon publish a statement highlighting the elements of the Directive that merit further consideration, for the benefit of the taxpayers and efficiency of the process.

The Directive enacts an enforceable obligation on Member States to arrive at a resolution of all disputes within the scope of the directive within two years in the process of a tax treaty dispute. Member States will constitute an Advisory Commission to arbitrate if at the end of this period the dispute has not been resolved. If Member States fail to do so, the taxpayer can bring an action before the national courts to unblock the process. This Advisory Commission will have six months to deliver a final, binding decision. This decision will be immediately enforceable and must resolve the dispute. The Directive envisages significant transparency improvements, with an obligation to notify the taxpayers and publish abstracts of the final decisions.

The EU Commissioner for Taxation, Pierre Moscovici, said: "*A fair and efficient tax system in the EU should also ensure that the same revenue is not taxed twice by two different Member States. When that happens, the problem should be solved swiftly and efficiently. From today, resolving tax disputes will be a lot easier. Companies, in particular small businesses, and individuals that may be experiencing cash flow problems as a result of double taxation will see their rights considerably enhanced. They can now be more certain that their tax matters will be resolved by the relevant judicial authorities in an acceptable and predictable timeframe, instead of dragging on for years.*"

A Bit More of the Transparency, Please: Public Country-by-Country Reporting Back on Council Agenda

Ahead of the Council of EU Company Law Working Party group meeting of 24 January, the Romanian EU Presidency published a presidency compromise text on the revised proposal for public country-by-country reporting (CbCR) in the EU. The proposal does not introduce significant amendments compared to the compromise reached earlier in the negotiations. Considering that no significant action has been taken since the EU Parliament vote in 2017, the Member States are still assessing the situation. Whilst previous Council Presidencies were taking a “wait and see” approach, the incoming Finnish Presidency is keen on re-examining the proposal.

Progress on public CbCR came to a halt when the Council Legal Service issued its opinion in November 2016. The Opinion concluded that public CbCR was a taxation matter and not a matter falling within the ambit of the Accounting Directive, as was initially found by Commission legal services. The Opinion is based on the premise that the purpose of the proposals is the protection of the functioning of the internal market and prevention of tax avoidance rather that the protection of shareholders and the public interest under Article 50 TFEU. In order for the public CbCR proposals to be characterised a “tax file” by the EU Commission, Member States must unanimously request that the Commission do so, therefore the legal Opinion alone has limited practical consequences without subsequent action. Some Member States continue to challenge the proposed legal basis in the original proposal, suggesting that it relates to taxation matters therefore falls within the ambit of Article 115 TFEU.

The European Parliament appears to be maintaining its steadfast support and went a step further in its initial opinion. The parliamentary Rapporteurs originally proposed the reduction of the 750 million euro threshold to 40 million and extending the scope of the publication of the information beyond that relating to EU countries to every country in which they operate. The question of the legal basis was also assessed. After the vote on the report in a joint committee meeting on 12 June 2017, the amendments were adopted by Plenary on 4 July 2017 (including a compromise on the 750 million euro threshold) and the file was referred back for inter-institutional negotiations.

CFE Tax Advisers Europe will closely monitor developments in relation to this file.

EU Reporting Requirements for Intermediaries: DAC Implementation Report

IMPLEMENTATION REPORT & REGULATIONS

The European Commission published the first report on the implementation of the Directive on Administrative Cooperation (“DAC”) early in 2019. The report highlights the EU’s improved tax transparency record due to DAC implementation and the automatic exchange of information (“AEOI”). Notably, in 2017 alone Member States exchanged information on almost 9 million financial accounts with a total balance of nearly €3 trillion. The report also indicates that Member States were able to use such data to increase their tax base due to awareness of potentially taxable foreign income and capital of their tax residents.

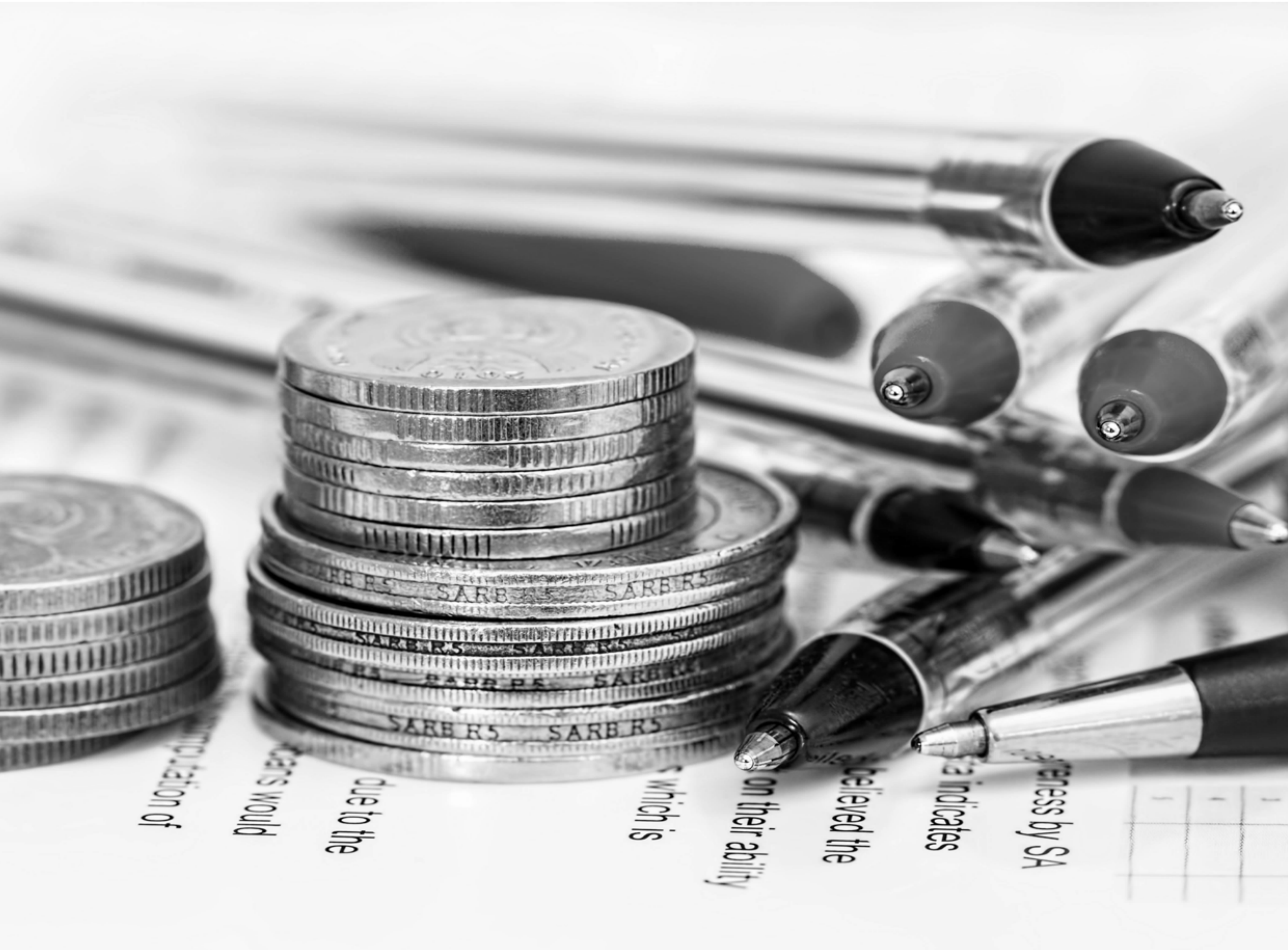
By way of conclusions, the report identifies that tax authorities mainly use the AEOI for risk assessment and personal income tax assessment. However, several Member States still make very limited use of the information they receive. The main benefits of AEOI lie in the increased tax compliance and in the deterrent effect for taxpayers. Member States often send information that does not include all necessary identification elements, which would permit an automated matching of this information with what is available nationally. As a way forward, two areas of improvement were identified: enhanced quality of information and better use of data received via AEOI. Such support mechanisms already exist within the FISCALIS programme of the European Union.

As reported in the Second Semester CFE Tax Policy Report of 2018, the DAC6 directive entered into force on 25 June 2018, introducing complex mandatory disclosure rules for intermediaries across the EU. Intermediaries who design and/or promote reportable tax planning schemes will be required to disclose them to their national tax administrations, who will then automatically exchange the information with other Member States through a centralised database.

Although Members States have until 31 December 2019 to implement the Directive into domestic legislation, and disclosure requirements will only apply to intermediaries from 1 July 2020, given that all arrangements initiated after 25 June 2018 that fall within the scope of the Directive are reportable, there have been increased calls for the Commission to issue technical guidance to provide more clarity for tax advisers in the course of transposition of the directive.

To that end, in April, the European Commission has published [Implementing Regulation (EU) 2019/532](#) amending Implementing Regulation (EU) 2015/2378 as regards the standard forms, including linguistic arrangements, for the mandatory automatic exchange of information on reportable cross-border arrangements.

The short text of this Implementing Regulation concerning the Directive on Mandatory Disclosure Rules, commonly referred to as DAC6, adds a requirement of including a reference number of the reportable cross-border arrangement to the standardised form for the mandatory automatic exchange of information on reportable cross-border arrangements pursuant to Article 8ab of Directive 2011/16/EU. The Implementing Regulation shall apply from 1 July 2020.



Positive Developments: Whistleblowers Protection Approved

On 11 March 2019, EU Council and Parliament negotiators reached provisional agreement on the proposed directive to establish EU-wide rules for the protection of whistleblowers who report on breaches of EU law, including those reporting on issues related to tax fraud and money laundering. Thereafter, on 16 April, the EU Parliament voted to adopt the directive providing for EU-wide protection of those people reporting breaches of EU law, including those reporting on issues related to tax fraud and money laundering, with 591 votes in favour of the measures, 29 opposed, and 33 abstentions.

The proposed directive will provide those persons reporting on breaches of EU legislation with internal and external reporting procedures for whistleblowing. Companies and authorities will also have feedback obligations, such that they have 3 months to respond to whistleblower reports under the proposal. The directive also includes provisions which would forbid all forms of retaliation, to be enforced by means of sanctions. Whistleblowers are also to be provided with access to free independent information, advice, legal aid and remedies in instances where retaliation is experienced, with the burden of proof to be reversed such that the organisation or person must prove they are not acting in retaliation against the whistleblower, as well as financial and psychological support.

In July 2018, the CFE issued an Opinion Statement on the EU Commission proposal, which set out CFE's support for proposals that seek to establish horizontal rules for protection of whistleblowers, as well as their role in advancing public policy interests, specifically reporting tax fraud, corruption, abusive and illegal practices.

The law will now be approved by EU ministers, and Member States will have two years to implement the new rules. The directive will enter into force 20 days after publication in the EU Official Journal.

Neverending Stories: Common Corporate Tax Base (CCTB)

In March, the EU Commission published a taxation working paper containing a detailed analysis of the potential impact the introduction of the European Commission proposal for a Common Corporate Tax Base that was relaunched in 2016 would have on the tax burden of corporations in Member States.

The paper evaluates the impact of the CCTB proposals on the effective corporate tax burdens in the 28 EU Member States and assesses the relative importance of single elements of the harmonised tax base, comparing the original 2011 proposals with the recast 2016 proposals. The executive summary sets out that the aim of the study is *"to evaluate the impact [of the proposal]…on the effective corporate tax burdens in the 28 EU Member States and to assess the relative importance of single elements of the harmonised tax base".*

The study demonstrates that, when incorporating the Allowance for Growth and Investment provided for in the proposal as a means of interest deduction and the research and development incentives, there is an average decrease in effective tax burdens of 5.1%. The study determines that newly founded, profitable and growing companies would benefit from the growth and investment allowance in particular. In a situation where national research and development incentives already apply, it was found that introduction of the CCTB would still reduce the effective tax burden by an average of 3.9%.

The CCTB proposal was listed as a priority by the Romanian Presidency and is the subject of ongoing discussion at the EU Council, and is listed as a priority for discussions by the incoming Finnish Presidency. To that end, the latest Presidency compromise text of the Proposal for a Council Directive on a Common Corporate Tax Base (CCTB) has been published by the Council of the European Union.

Germany Pushes Forward on FTT: EU's Financial Transaction Tax

The Council of the EU (ECOFIN) discussed on 14 June the state of play with the Financial Transaction Tax (FTT). The Member States participating in the FTT enhanced cooperation procedure (Austria, Belgium, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and Spain) updated the Council on the recent progress with this file, and the intention to present the final proposal by the end of this year, with 1 January 2021 as the implementation deadline. If adopted under EU law, the FTT shall be applicable only to the Member States participating in the enhanced cooperation mechanism, after a unanimous Council decision of the participating countries and in consultation with the European Parliament.

According to the note submitted by Germany to the Council, the compromise model should resemble the French solution, whilst the generated revenue shall be distributed by way of a compensation mechanism among the participating Member States. The precise scope and technical solution are yet to be defined, but it is understood that the FTT rate will be set at no less than 0.2% of the value of the transaction.

"Financial transaction tax is on the way. We want to establish the foundation for the tax within this year – in order to implement it in 2021. Our aim: To raise revenue to finance our communities.", the German Finance Minister Olaf Scholz announced. Mr Scholz hopes that the "compensation solution" would incentivise other Member States, in particular the smaller ones, to join the initiative.

CFE understands that Finland's upcoming Presidency with the Council of the EU is ready to advance the discussions on this file.

EU Tax Policy – Indirect Tax

04

Definitive VAT Regime Progress

Progress on VAT files concerning the definitive VAT regime has been limited so far in 2019, despite the fact that the European Parliament at its plenary session on 12 February voted and adopted a legislative resolution setting out its opinion on recommended amendments to the EU Commission proposal for a Council directive as regards the introduction of the detailed technical measures for the operation of the definitive VAT regime system for the taxation of trade between Member States.

Parliament has called on the Commission to establish strict harmonised criteria and guidelines through which enterprises can benefit from being categorised as a certified taxable person, with common rules and provisions concerning fines and penalties for non-compliance. Further, Parliament has called on the Commission to analyse whether the temporary application of the reverse charge mechanism ought to be repealed following implementation of the definitive VAT regime. As concerns SMEs, the Parliament recommended a web information portal be accessible for businesses providing up-to-date information about VAT rates for goods and services in different Member States, as well as a tailored procedure for SMEs. Parliament also called on the Commission to guarantee the transparency of the definitive VAT regime system, and to publish annual reports concerning VAT fraud.

In April, the European Commission adopted a proposal that an exemption from VAT and excise duties should be included in the VAT Directive concerning supplies made to armed forces, when the forces are deployed in a European defence effort outside their member state.

This proposal is made in line with the EU's Common Security and Defence Policy, and aims to amend the VAT Directive to include an exemption that would mirror the one currently in place for supplies made to forces engaged in NATO defence efforts. The revision would ensure equal treatment of supplies concerning defence efforts under the NATO and EU frameworks.

In May, the EU Commission published a study concerning domestic and cross-border intra-EU VAT refunds, examining in detail the current processes for tax administrations and taxpayers for VAT refund claims.

The report examines Member States' implementation of the directive for cross-border intra-EU refunds into national legislation, and CJEU case law concerning domestic VAT refund claims. It also highlights practical issues stemming from implementation issues, particularly from the perspective of taxpayers and tax advisers in claiming VAT refunds in cross-border situations. The results of the study will be used by the EU Commission to inform future action to address inconsistencies and implementation issues related to the cross-border intra-EU refunds directive.

Discussions between Members States at the EU Council concerning the proposed directive as regards the introduction of the detailed technical measures for the operation of the definitive VAT regime system are ongoing. Discussions are also ongoing in relation to the Commission's proposed Directives on reform of VAT rates, to create a simplified list of products subject to the standard rate, and to allow Member States to have two separate reduced rates, one reduced rate and one exemption. The proposal setting out simplification of VAT rules for SMEs, by way of introducing new simplified measures regarding invoicing, VAT registration, accounting and returns for SMEs acting both in wholly domestic markets and also cross-border across the EU, has also not yet been agreed.

Council discussions concerning the legislative proposals that introduce the definitive VAT system, and the above proposals are ongoing, and will remain a focus of the Indirect Taxes Subcommittee of CFE.

BREXIT & Tax

05

Back to "B": The Tax Implications of Brexit...

The UK and EU Government in the past six months have published and updated various technical papers that set out guidance for citizens and business in the event of the United Kingdom exiting from the European Union without any agreement.

In February, the UK revenue authority, HMRC, wrote to almost 150,000 VAT-registered businesses detailing simplified transitional procedures that will come into effect in the instance of a "no-deal" Brexit. Businesses established in the UK which import goods from the EU into the UK that register to be subject to transitional simplified procedures will be entitled to transport and import goods without the need for making customs declaration duties at the border. They will also be entitled to delay payment of import duties, if so desired.

In February, the European Commission also launched a webpage providing information for SME businesses on customs preparedness in the event that a "no deal" Brexit should take place, based on the then deadline of the United Kingdom withdrawing from the European Union on 29 March 2019.

The webpage detailed that customs formalities would apply from the exit date onwards for businesses trading with the United Kingdom, including requirements concerning custom declarations, import/exporting licenses, and the payment of duties on imports. In addition, the website set out that VAT will be due on importation, and that rules concerning cross-border refunds will change. The webpage provides links to a Brexit factsheet, a checklist for traders, as well as notices concerning specific topics and contact numbers for the customs authorities in each Member State.

On 13 March, the UK government published details of a temporary tariff regime that will apply in the event of no-deal Brexit for an initial period of 12 months, to be thereafter reviewed. Under the published regime, the vast majority of goods being imported, around 87% of goods, would be eligible for tariff-free importation.

Tariffs would apply to imports on finished automobiles to maintain the UK's automobile industry, certain fertilisers and fuels to protect against dumping, beef, lamb, pork, poultry and dairy products to protect the UK farming industry, and on bananas, raw cane sugar and certain fish, to continue commitments to provide preferential access to the UK for developing markets. However, import tariffs would not apply to goods being imported from Ireland into Northern Ireland, as the government also announced it would temporarily not impose any new controls on imports at the Northern Ireland land border.

This regime is in addition to the simplified transitional procedures that will come into effect in the instance of a no-deal Brexit, whereby businesses established in the UK that import goods from the EU into the UK and register to be subject to transitional simplified procedures will be entitled to transport and import goods without the need for making customs declaration duties at the border.

In March, in light of the increasing likelihood of a no-deal Brexit, the EU Commission and Council completed final preparedness preparations. In the event there is a no-deal Brexit, the EU will apply third-country tariffs and customs rules at its borders with the UK, including customs checks and controls, as well as verification of compliance with EU norms. Significant delays at borders would be expected. As concerns State aid, current EU rules also provide a means for assisting businesses encountering no-deal Brexit difficulties. The EU Council also passed a series of legislative measures as part of the no-deal preparedness preparations, concerning social security, fisheries, transport and the Erasmus programme, amongst others. Detailed tax-related no-deal Brexit preparedness documents can be located here.

Since the last CFE Tax Policy Report, the possibility of a 'no-deal' scenario has become increasingly more likely due to political volatility in the UK surrounding Brexit, which ultimately led to the resignation of Theresa May. Whether the Brexit Withdrawal Agreement endorsed in November 2018 at the special EU summit meeting will be agreed by the current exit date by her successor remains to be seen.

EU Policy – Blacklist & TAX3

06

Tax Good Governance Standards: EU Blacklist & Code of Conduct Group

The EU's list of non-cooperative jurisdictions for taxation purposes was updated three times in the first semester of 2019. Agreement was reached at the ECOFIN Council meeting on 12 March to update the "Blacklist" following on from the Code of Conduct Group on Business Taxation's review of commitments made by jurisdictions to implement tax good governance principles of transparency, through automatic exchange of information and becoming members of the Global Forum or ratifying the OECD Multilateral Convention on Mutual Administrative Assistance. Accordingly, the jurisdictions of Aruba, Barbados, Belize, Bermuda, Dominica, Fiji, Marshall Islands, Oman, United Arab Emirates and Vanuatu were added to the list for failing to comply with commitments by agreed deadlines.

In May, Council amended the list further, removing Aruba, Barbados and Bermuda from the EU Blacklist. Finally, in June the ECOFIN Council approved the removal of Dominica from the EU list of non-cooperative jurisdictions for tax purposes. The jurisdictions were determined to have addressed the EU concerns as regards automatic exchange of financial information, in particular by taking steps to sign and ratify the OECD multilateral convention on mutual administrative assistance. In addition, in June the EU finance ministers endorsed the report on the EU Code of Conduct Group (Business Taxation).

At present, 11 jurisdictions remain on the EU list of non-cooperative jurisdictions for tax purposes: American Samoa, Belize, Fiji, Guam, Marshall Islands, Oman, Samoa, Trinidad and Tobago, United Arab Emirates, US Virgin Islands and Vanuatu. Countries who made high-level commitments to remedy EU concerns and reform tax policies will be subject to close monitoring by the Council.

The Code of Conduct Group (Business Taxation) of the Council of the European Union also published a Work Programme early in the year. Areas of priority for the Code of Conduct Group included:

- Developing guidance on coordinating implementation of OECD BEPS conclusions on Actions 8-9-10, concerning aligning transfer pricing outcomes with value creation, and Action 13, concerning transfer pricing documentation;
- Developing guidance on notional interest deduction regimes;
- Reviewing the list of non-cooperative jurisdictions for tax purposes;
- Developing draft guidance concerning coordinated defensive measures against non-cooperative jurisdictions; and
- Assessing Member States' compliance with Guidance issued in 2000 on rollback and standstill concerning finance branches, holding companies and headquarter companies.

Monitoring the work of the Code of Conduct Group and changes to the EU list of non-cooperative jurisdictions for tax purposes will remain an ongoing priority for CFE Tax Advisers Europe.

EU Tax Inquiry Committee: TAX3 Report Adopted & Published

MORE OF THE PARLIAMENTARY TAX JUSTICE QUESTS

On 26 March, the European Parliament adopted the final report of the Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance, "TAX3", presenting the recommendations of the Committee following ten months of hearings concerning anti-money laundering and aggressive tax planning.

Key recommendations in the report are that the Commission and Council adopt a comprehensive definition of aggressive tax planning, as well as a definition of permanent establishment, economic activity requirements and expenditure tests to avoid companies having an artificial taxable presence in a Member State.

The Committee further recommends that EU efforts to fight corporate aggressive tax planning are strengthened, that the BEPS action plan is supplemented, and that Member States' tax systems are scrutinised. They recommend golden visas being phased out. They also call on the Council to adopt the proposals on CCTB and CCTB as well as the digital tax package proposals.

The Committee calls for a broader scope for the exchange of tax rulings and for broader access by the Commission to those rulings, and guidance concerning what constitutes tax-related State aid and appropriate transfer pricing. The rapporteurs welcomed the VAT action plan, but expressed regret that no safeguards were adopted concerning the Certified Taxable Person proposal.

Additional recommendations include that an EU anti-money laundering watchdog ought to be established and that the Commission ought to propose that a European financial police force be established. An amendment which recommends imposing a mandatory rotation for auditors after 7 years of service was also approved. Seven EU countries (Belgium, Cyprus, Hungary, Ireland, Luxembourg, Malta and the Netherlands) were criticised by the Commission for shortcomings in their tax systems that facilitate aggressive tax planning. The European Parliament also expressed regret that Denmark, Finland, Ireland and Sweden continue to maintain their opposition to EU digital tax proposals.

It is widely expected that the newly elected Parliament will establish a permanent tax inquiry committee. The first European Parliament plenary is being held this week in Strasbourg.

Doing Business in the Single Market: EU Company Law Package

The European Commission proposals of April 2018 to reform and digitalise EU company law in order to make it easier for companies to reorganise - merge, divide or move within the EU Single Market - were adopted by the EU Parliament in April of this year. The proposal was not a taxation proposal, meaning unanimity in voting was not required.

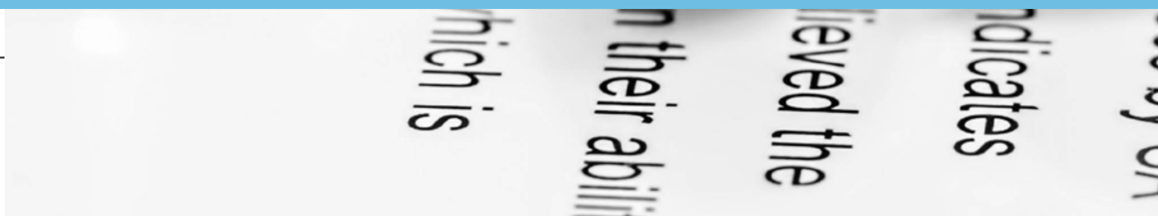
The proposal on cross-border conversions, mergers and divisions provides for common EU rules aiming to update existing ones to facilitate reorganisation, allowing companies to register, set up new branches or file documents online, provided that there is genuine economic activity being carried on in the Member State where the company is being established. One of Commission's policy objectives with this proposal is to increase the cross-border accessibility to company-related information that will help ensure fair taxation where profits are generated.

The proposal includes provisions for safeguards against abuse of the conversion and division procedures to create artificial arrangements aimed at obtaining undue tax advantages. Further, the proposal sets out safeguards for employee rights, whereby companies will be required to inform employees on the legal and economic consequences of a cross-border operation, and to comply with safeguards concerning the prevention of cross-border operations which have abusive, criminal or fraudulent aims.

The proposal must now be voted by the EU Council before being published in the EU Official Journal and will enter into force 20 days thereafter.

International Policy – OECD, IMF & UN

07



OECD Update

Signatories to OECD's MLI Tax Treaty Continue to Increase

So far in 2019, Albania, Morocco and Papua New Guinea became signatories to the OECD's Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting. The jurisdictions of Belgium, Curacao, Finland, France, Georgia, India, Ireland, Luxembourg, Malta, Monaco, the Netherlands, New Zealand, the Russian Federation, Serbia and the United Arab Emirates have also all deposited instruments of ratification concerning the convention. The multilateral tax treaty allows jurisdictions to update their existing double tax treaties and transpose measures agreed in the BEPS project without further need for bilateral negotiations.

There has also been an increase in jurisdictions joining the OECD's BEPS Inclusive Framework. Members of the Inclusive Framework have the opportunity to work together on an equal footing with other OECD and G20 countries on implementing the BEPS package consistently and on developing further standards to address remaining BEPS issues. There are now 129 jurisdictions that are participating in the project.

OECD Tax Moral Consultation

In May, the OECD invited public comments on a draft report which analyses the factors that contribute to the tax morale and the modality to improve the revenue collection mechanisms through voluntary compliance. This report specifically focuses on tax morale in developing countries, using recent data to help identify the drivers of tax morale among individuals and businesses.

The consultation was launched following a Public Consultation Document which updates previous OECD research on tax morale in individuals and, additionally, presents a new business section, using OECD tax certainty data to discuss business tax morale in developing countries. The forthcoming publication, entitled "What is driving tax morale? An empirical analysis on social preferences and attitudes towards taxation" is expected to be published later in 2019. The comments submitted from CFE on behalf of the Global Tax Advisers Platform can be viewed on our website.

Model Tax Convention

In April, the OECD published the full version of its 2017 Model Tax Convention on Income and Capital. The model convention is aimed at providing a standard for concluding bilateral tax conventions between countries in order to facilitate economic development, to prevent tax evasion, and to settle circumstances where international double taxation arise. The model stresses the importance for taxpayers of standardising taxation in cross-border trade.

The 2017 model incorporates revisions to treaty-related measures following on from outcomes of the OECD BEPS Project, in particular concerning hybrid mismatches, treaty benefits, permanent establishment and dispute resolution.

Global Forum on VAT

Delegates attending the OECD's Global Forum on VAT which took place on 20 – 22 March in Australia unanimously voted to endorse new rules concerning the collection of VAT by online platforms/marketplaces and to allow for data sharing and enhanced co-operation between tax authorities and online marketplaces. The agreed measures were contained in a new report of the OECD, The Role of Digital Platforms in the Collection of VAT/GST on Online Sales, which builds on the 2015 BEPS Action 1 Report on the Tax Challenges of the Digital Economy. As over two-thirds of online transactions take place by way of marketplace/platform, it is hoped the agreed measures will allow authorities to focus on the compliance of platforms, rather than the individual trader, and significantly increase the amount of revenue collected.

Forum on Tax Administration

The OECD's Forum on Tax Administration (FTA) met in Chile on 26-28 March and agreed an ambitious agenda focused on tax certainty, enhanced tax co-operation and the collective challenges of digital transformation in relation to tax administration. This year's plenary session focused on delivering on BEPS and tax certainty, improving tax co-operation, supporting the continued digitalisation of tax administrations and building capacity for developing countries.

Significantly, the OECD's FTA recognised that a successful delivery on the wider tax certainty agenda is conditional upon a comprehensive and interlinked agenda focused on dispute resolution and prevention. To that end, the OECD continues to prioritise implementation of the OECD/G20 international tax agenda, with notable progress in the implementation of Country-by-Country reporting (CbC), the Mutual Agreement Procedure (MAP) and the exchange of rulings.

Beneficial Ownership

The OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes released a beneficial ownership toolkit in March, aimed to assist governments in implementing the Global Forum's standards concerning the ultimate beneficial owner of a company or entity. The toolkit includes explanations of the technical and legal requirements concerning beneficial ownership, the criteria to be used to identify the beneficial owner, as well as explanations of existing measures which ensure the availability of beneficial ownership information and its role in automatic exchange of information regimes.

Anti-Money Laundering Handbook

In June, the OECD published a handbook aimed to help tax administrations in addressing anti-money laundering issues more efficiently. The handbook was initially published in 2009 as a means to facilitate the anti-money laundering efforts of tax authorities and the anti-money laundering and terrorist-financing competent authorities. The new handbook includes updated money laundering indicators and new material to increase detection and reporting of terrorist financing, relating to reporting suspicious transactions and on reporting and investigating money-laundering offences.

Tax news from the IMF

In March, the International Monetary Fund (IMF) published a policy paper evaluating the current state of international corporate tax reform and setting out the ambition to build on the recent progress in international cooperation on tax matters. The paper takes stock of the international progress to date, providing a high-level overview of the key economic considerations and implications of various reform proposals. The IMF is not a standard setting body in the area of international tax, and as such continues to support the work undertaken by the OECD. Whilst accepting that the current international tax governance arrangements are broadly appropriate, the Board of IMF suggested that the Platform for Collaboration on Tax (bringing together the IMF, OECD, UN and World Bank) could have a more meaningful future role in supporting international tax coordination.

The IMF Board of Directors welcomed the considerable progress made at OECD level in addressing the BEPS issues by expanding the scope of cooperation to include non-OECD countries via the Inclusive Framework. In respect of the current debate to address the tax challenges of the digitalising economy, the IMF recognised the complexity of the process from a political and technical perspective, noting that views on the matter continue to differ significantly among countries. Hence, the IMF paper refrained from endorsing any of the proposals for tax reform arising from the OECD debate. Instead, the paper focuses on the residual BEPS issues, in particular profit shifting and harmful tax competition, which is of critical concern for the ability of emerging and developing countries to secure their tax bases on inward investment.

In addition, the International Monetary Fund (IMF) and the OECD published a joint report in June on the recent work undertaken on tax certainty, as presented by the OECD Secretary General on 8 June 2019 at the G20 ministerial meeting in Fukuoka, Japan. The G20 Leaders reaffirmed the importance of prioritising policies that enhance tax certainty, as a follow-up to previous reports published in 2017 and 2018.

The report covers matters related to both tax policy and tax administration, highlighting the importance of dispute prevention (as opposed to dispute resolution), focusing on the integrity, efficiency and accountability of tax administrations, as well as on simplicity of tax rules as key element of tax certainty. Building on previous OECD work, the report has sought to link tax certainty with tax morale, in particular with reference to developing countries, developments which were recently welcomed in a joint statement of the Global Tax Advisers Platform (GTAP).

UN Tax Committee Discuss Model Double Taxation Convention

In April, the 18th Session of the Committee of Experts on International Cooperation in Tax Matters ("UN Tax Committee") discussed the update of the UN Nations Model Double Taxation Convention between Developed and Developing Countries, as well as the next update of the UN Transfer Pricing Manual. Other items on the agenda included the mutual agreement procedure and dispute avoidance and resolution.

The experts in attendance, including representatives of CFE Tax Advisers Europe, addressed the report of the subcommittee on updating the United Nations Model Double Taxation Convention, including: taxation of royalties; taxation of collective investment vehicles; tax and the Sustainable Development Goals; update of the United Nations Practical Manual on Transfer Pricing for Developing Countries; update of the Handbook on Selected Issues for Taxation of the Extractive Industries by Developing Countries; update of the Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries; environmental tax issues and lastly, the tax consequences of the digitalising economy, with particular focus on issues of relevance for developing countries. The session was held alongside the ECOSOC Special Meeting on International Cooperation on Tax Matters.

EU State Aid & Competition Developments

08

Commission Opens In-Depth Investigation into Nike

In January, the European Commission opened an in-depth investigation into tax rulings made by the Netherlands concerning two Nike companies established in the Netherlands, and whether through those rulings they gave the companies an unfair advantage over their competitors. The Commission will investigate whether the accepted transfer pricing method used to establish royalty payments made by two operating companies to the Dutch partnerships which owned the IP rights of the products sold by the entities were in keeping with the arm's length principle. The partnership entities were not taxed in the Netherlands.

Speaking in relation to the investigation, Commissioner Vestager stated "*Member States should not allow companies to set up complex structures that unduly reduce their taxable profits and give them an unfair advantage over competitors. The Commission will investigate carefully the tax treatment of Nike in the Netherlands, to assess whether it is in line with EU State aid rules. At the same time, I welcome the actions taken by the Netherlands to reform their corporate taxation rules and to help ensure that companies will operate on a level playing field in the EU."*

The Commission's interpretation of the arm's length principle is currently being examined by the Court of Justice of the European Union in relation to other recent Commission State aid cases, including Starbucks, Apple and Amazon.

Commission Opens Investigation into Interest-Free Loans

In March, the EU Commission opened an in-depth investigation into whether tax rulings granted by Luxembourg to food and drink packaging company Huhtamäki may have given the company an unfair advantage over competitors, in breach of EU State aid rules. In May, the Commission published the decision which opened the in-depth investigation.

Huhtamäki has its headquarters in Finland, but operates a group structure. The Commission will investigate three tax rulings of the Luxembourg government to the Luxembourg-based entity of the company, Huhtalux. One of these rulings was disclosed as part of the Luxleaks investigation.

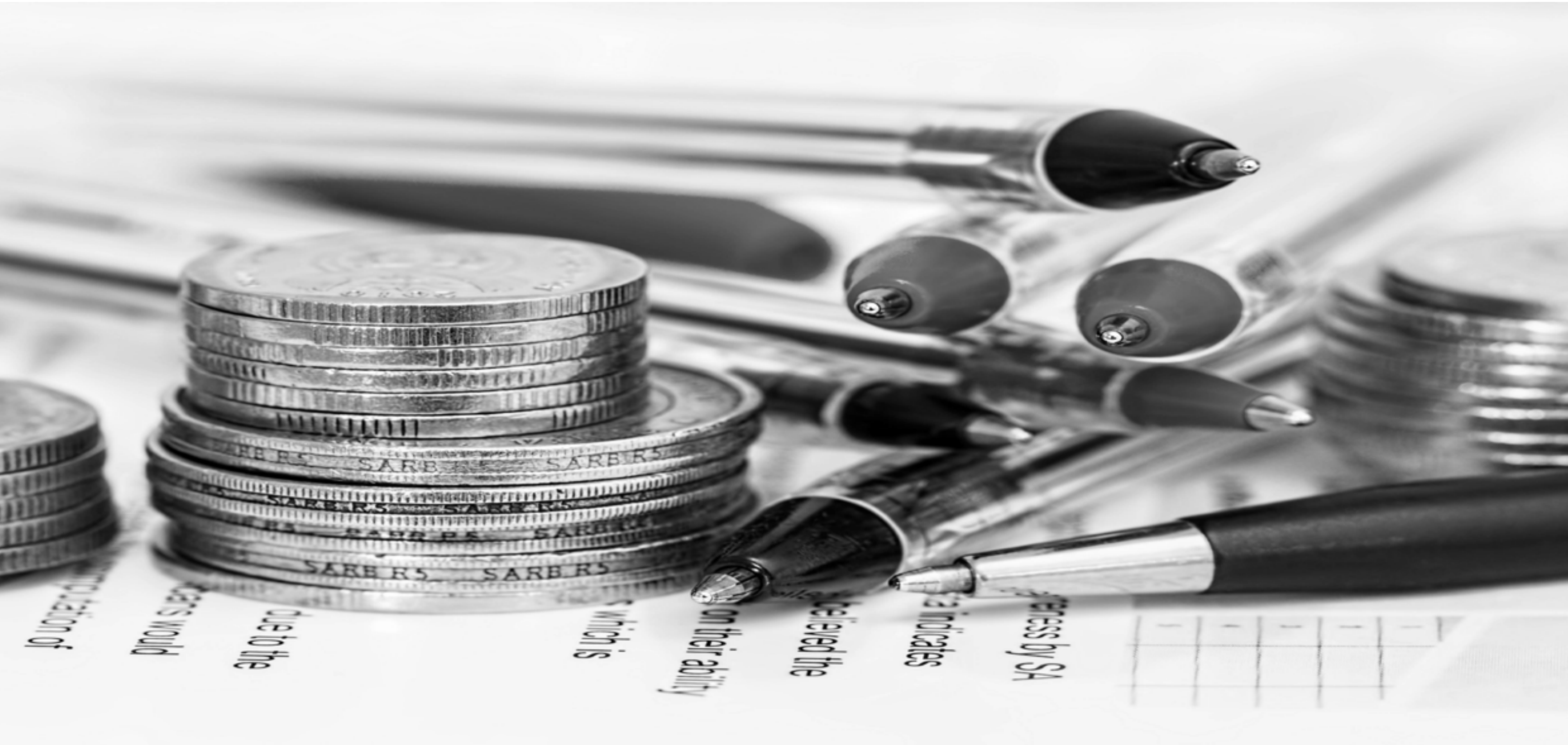
The rulings approved the tax treatment of intra-group financing structures in place, whereby Huhtalux received interest-free loans from a company in the group, then used to finance other companies in the group through interest-bearing loans. The rulings allowed the Luxembourg company to deduct the interest payments from the interest-free loans, interest which was not actually paid, and reduce the company's tax base. The Commission believes the ruling approving this deduction has resulted in a selective advantage being conferred on the group as compared with stand-alone companies.

EU Commission Declares Part of UK CFC Rules in Breach of State Aid Law

The European Commission concluded on 2 April an investigation into the compliance of UK's Controlled Foreign Company (CFC) legislation with the EU State aid rules, declaring that the application of the Group Financing Exemption contained in the Finance Act 2012 partly constitutes unlawful State aid to certain multinational companies. The Commission also stated that the present UK CFC regime, introduced with ATAD as of 1 January 2019, no longer gave rise to any State concerns.

Between 2013 and the end of 2018, the UK CFC rules included a Group Financing Exemption that allowed multinational companies to benefit from a full or partial exemption on interest payments from loans, i.e. on payments related to certain financing income. According to the European Commission, the exemption is compliant with the State aid rules where the financing income is derived from non-UK activities. Conversely, the Group Financing Exemption on financing income derived from UK activities was considered to be in breach of the State aid rules. As a consequence, the Commission concludes, the beneficiaries of the measure received an undue advantage over UK competitors who were not able to rely on such exemption and were subject to the headline corporate tax rate. Further technical detail of Commission's reasoning will become available in due course with publication of the decision in the Official Journal of the European Union.

It is not yet clear how the HMRC will enforce this EU decision against the companies identified as tax exemption beneficiaries, considering the Brexit uncertainty. The EU has stated that the State aid rules continue to apply to the United Kingdom until it has formally left the EU, whereas the UK Government has indicated a close regulatory alignment of UK's post-Brexit State aid regime with the European, as set out in the draft UK State Aid (EU Exit) 2019 Regulations.



Case Law of the CJEU: State Aid

09

General Court Annuls Commission's State Aid Decision in Belgian 'Excess Profit' Scheme

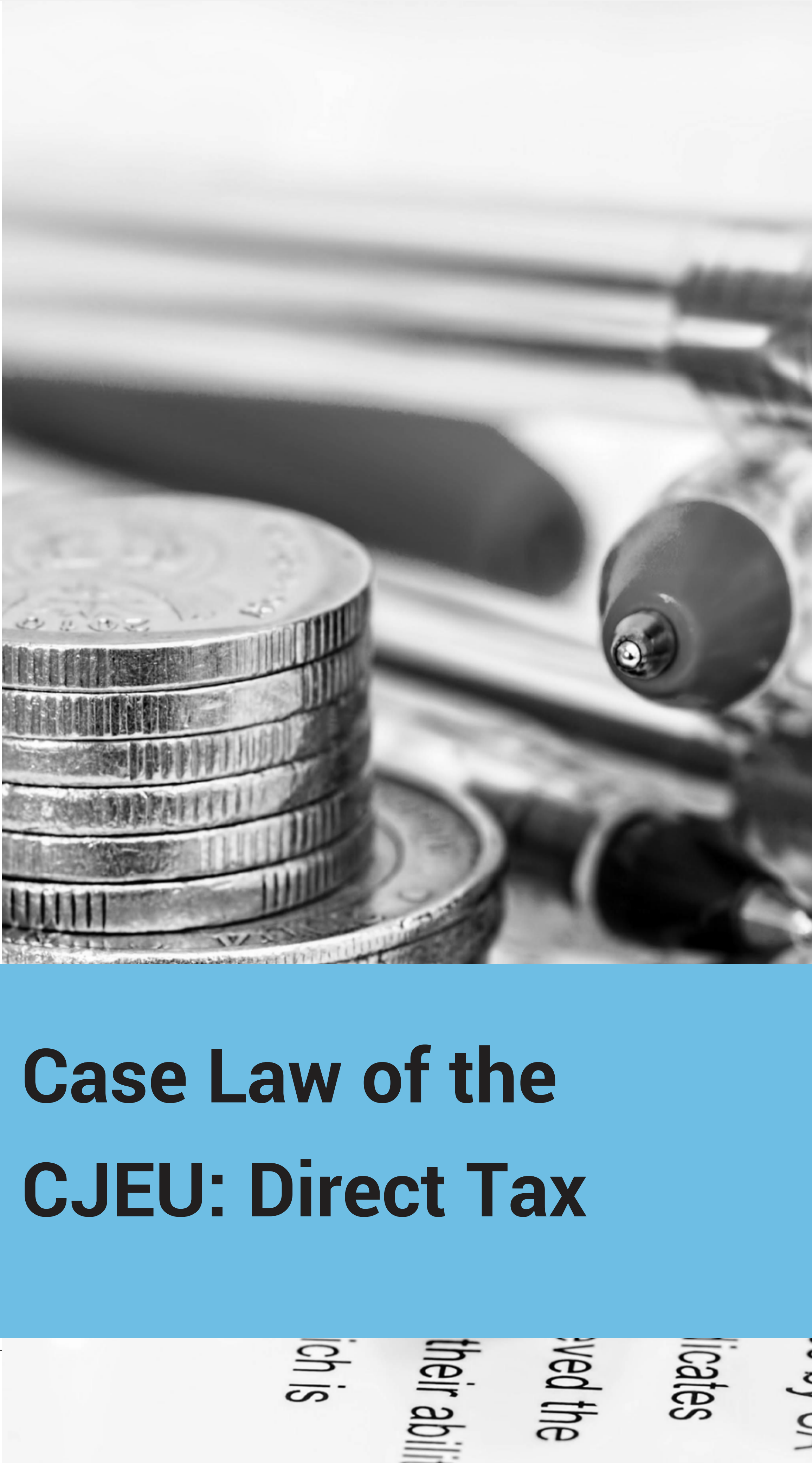
In February, the General Court annulled the Commission tax related State aid decision in the Belgian excess profit rulings cases (Cases T-131/16 and T-263/16 Kingdom of Belgium v European Commission). This was a highly anticipated decision considering that the Court for the first time had an opportunity to interpret the Commission's understanding of the arm's length principle under EU State aid law and the competence of the Commission to assess individual tax rulings. It transpires that the decision did not invalidate Commission's substantive interpretation of the State aid rules, but challenged the methodology of assessment and the classification of the aid as a "scheme". Further clarity on the matter will be offered on potential appeal and in highly anticipated rulings in the cases like Apple, Starbucks and Fiat.

The original Commission decision established that the Belgian "excess profit" tax scheme had allowed multiple European MNEs in Belgium to benefit from a corporate tax base reduction for the generated excess profits. Commission's State aid investigation found that Belgium had established an "aid scheme", derogating from Belgian tax law and the "arm's length principle" as interpreted by the European Commission. The "excess profit" scheme was marketed by the Belgian government under the strapline "Only in Belgium".

The alleged error in law brought up by the Belgian government and the beneficiaries amounted to competence issues and methodology- related arguments. Belgium challenged European Commission competence to assess the State aid compliance of administrative measures in the direct tax area (tax rulings), invoking national sovereignty prerogative and methodological arguments related to the assessment of the alleged aid as an "aid scheme". The General Court dismissed the first plea, reaffirming Commission's competence to assess the State aid compliance of national direct tax measures, including administrative decisions such as tax rulings.

The Court noted that while direct taxation, as EU law currently stands, falls within the competence of the Member States, they must nonetheless exercise that competence consistently with EU law, in particular primary EU law (fundamental freedoms and State aid rules). Accepting the second plea, the Court disagreed with the Commission's assessment that the tax rulings constituted an "aid scheme". Significantly, the Belgian tax authorities had influence over the essential elements of the tax rulings system, which precludes the existence of an aid scheme. Further, it was established that the Procedural Regulation (EU/2015/1589) defines aid beneficiaries "in a general and abstract manner" for an infinite period of time, which was not the case with the Belgian "excess profit" rulings.

Appeal documents concerning the decision of the General Court to annul the Commission's decision in the Belgian 'excess profit" State aid cases have recently been published. The Commission has now launched an appeal against the General Court's judgment which annulled the Commission's decision in the cases. The Commission argues that the Court incorrectly classified the "excess profit" tax ruling practice as a scheme under Article 1(d) of Regulation 2015/1589, and misinterpreted the first, second and third condition of Article 1(d) in its decision.



Case Law of the CJEU: Direct Tax

10

CJEU Decisions in "Danish Beneficial Ownership Cases"

On 27 February, the Court of Justice of the European Union handed down the long-anticipated decisions in the joint cases of T 116/16 -T Danmark & 117/16 - Y Danmark, concerning the Parent-Subsidiary Directive, and joined cases C 115/16 – N Luxembourg 1, Case C 118/16 - X Denmark, Case C 119/16, C Danmark I and Case C 299/16, Z Denmark, concerning the Interest and Royalty Directive.

The Danish companies in the cases concerned were owned by parent companies in other Member States, who were themselves owned by companies in third countries. Dividends or interest were paid by the Danish companies to the EU parent companies, which the Danish companies argued were either free of withholding tax according to the Parent-Subsidiary Directive or Interest and Royalty Directive. The Danish tax administration disagreed, arguing that given recipients of the dividends/interest were not the beneficial owners of the payments, the exemption should not apply.

Concerning the Interest Directive, the CJEU was accordingly asked to indicate whether the recipient of the interest payment was indeed the beneficial owner and could avail itself of the withholding tax exemption in the directive. In answering the question, the Court looked to the OECD Model Tax Convention for the definition of beneficial ownership, and held that if a company would be deemed to be a beneficial owner under the OECD Convention, i.e. benefited economically, it would be likely that it would be a beneficial owner of interest under the Interest and Royalty Directive.

In respect of the Parent-Subsidiary Directive, the beneficial ownership test was not relevant. However, it mandates that a Member State must apply either the credit method or exemption method to a dividend paid to another Member State, except in the case of fraud or abuse. The Court was accordingly asked whether the anti-abuse provision needs to be enacted in domestic legislation in order for a Member State to invoke this argument. The Court held that a general anti-abuse provision can be relied on by a Member State, based on the EU principle of abuse of law, such that no domestic legislative provision is necessary. However, the Court noted that the *Cadbury Schweppes* test concerning abuse, i.e. that the transaction is purely artificial and was designed to circumvent the proper application of legislation of the Member State in the case in question, must continue to be met.

CFE's ECJ Taskforce has published an opinion statement on the decisions, which acknowledges that the cases address a number of important and timely issues, especially with regard to the concept of abuse in EU law. Those include (1) the expansion of the general anti-abuse principle enshrined in EU law to areas of tax law that are subject to minimum harmonization, (2) the use of the OECD materials to define the beneficial ownership concept, (3) the conflation of the beneficial ownership concept with the general anti-abuse principle and the Court's attempt to give the notion of "abuse" workable contours, and (4) the reading of an effective subject-to-tax clause with regard to the interest income into the definition of a "company" laid down in the Interest-Royalties-Directive (IRD).

However, CFE Tax Advisers Europe also expects that domestic courts will likely struggle to translate the abstract guidance of the “Danish beneficial ownership cases” into concrete judgments, that practitioners and academics alike will have to discuss building blocks and nuances of the Grand Chamber’s judgments for quite some time to come, and that consideration needs to be given on what impact those cases have on current tax structures.

Testing the Waters for DST: Vodafone Magyarország – AG Kokott Delivers Opinion on Hungary’s Telecom Turnover Tax

In June, Advocate General Kokott handed down her opinion in the case of Vodafone Magyarország, concerning a tax imposed by the Hungarian tax administration on Vodafone’s revenue according to its turnover. The final outcome of the case is being closely monitored, as it will have implications for the proposed means of imposing a EU turnover tax on digital services.

AG Kokott sets out at paragraph 20 of her Opinion that the CJEU was asked to consider whether legislation which has the effect that the tax burden falls on foreign-owned taxable persons is indirectly discriminatory and incompatible with EU law, whether a Member State is precluded from imposing a turnover tax calculated on a progressive tax rate and whether, if the tax burden falls on foreign-owned taxable persons, the legislation is discriminatory and amounts to prohibited State aid. Finally, she sets out that the Court was asked to consider whether the tax was compatible with the VAT Directive as it was a special turnover tax.

AG Kokott held in relation to whether the tax was compatible with the VAT Directive that the special tax did not fit the characteristics of VAT as it did not apply to all transactions and was not passed on to the consumer, and Hungary was therefore not prevented from applying the tax by the VAT Directive.

As to whether imposing a turnover tax on a progressive tax rate is discriminatory, AG Kokott held that the principle of the welfare state justifies a progressive tax rate imposing a heavier burden on those with greater financial capacity, as does the administrative simplicity of imposing a tax on turnover rather than profit, and does not constitute a selective advantage for lower-turnover undertakings, nor State aid. Similarly, AG Kokott held that *“different taxation arising from a progressive rate does not constitute an indirect restriction of freedom of establishment, notwithstanding whether larger undertakings are taxed more heavily or owned by foreign shareholders.”* AG Kokott opined this could only be the case if conduct amounting to an abuse of rights can be demonstrated concerning the Member State.

The decision of the Court is expected in the coming months. The opinion of AG Kokott is not binding on the Court’s decision.

EU Tax Policy Report

January – June 2019

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