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EU Tax Policy Report

Semester II 2021

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 2021.

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Highlights

The second half of last year saw the OECD and the EU finalising their work to put forward specific proposal which are intended to 'giving life' to the Inclusive Framework agreed deal on minimum taxation of multinational companies. The OECD published the Model Rules, which set out guidance for implementation of the GLOBE rules.

Almost on Christmas Eve, the EU Commission was pleased to announce a double première: the first jurisdiction to start the legislative transposition of the OECD-G20 agreement on GLOBE (signed, sealed, delivered) and the first big player to start legislating on addressing the outstanding issues with abuse of shell companies for tax purposes. The files are now in the hands of the French presidency of the EU, who did not lose time and already held the first meeting on 4 January.

The Slovenian EU Presidency can be happy with the achievements not only in the direct tax side, but also on the indirect taxation front: Agreement on VAT Rules was reached and new VAT regime came into force, creating a simplified VAT regime for cross-border supplies of goods (B2C) and distance sales.

The publication of the Pandora Papers coincided with two initiatives intended to fight the abuse of the system for illicit money flows, money laundering and abuse of (empty) shells: a new EU AML Authority is set to be established. The European Commission adopted a proposal for a directive on the misuse of shell entities, or Unshell legislation in the EU-bubble jargon. The directive aims to enable more tools for tax authorities to detect the misuse of shell entities, by requiring reporting (relevant disclosure) in tax returns and consequently denying benefits of tax treaties and EU tax law.

Following the completion of COP26, an ambitious climate policy package was announced, encompassing multiple policy instruments to deliver on the European Green Deal Commitment to make Europe a carbon neutral continent by 2050, and to cut carbon emissions 55% by 2030. With the rising energy prices, climate taxation will remain both extremely relevant and under close scrutiny.

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OECD Pillar 1 & 2 Developments

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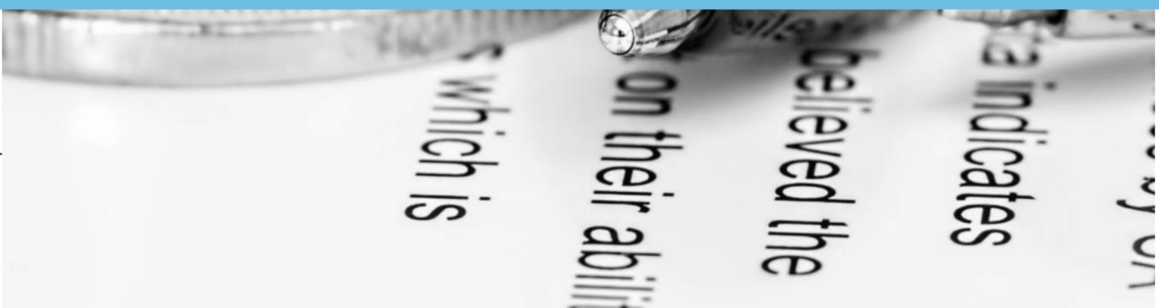

Historic Global Minimum Corporate Tax & Profit Reallocation Agreement Under OECD Auspices

In October, following years of difficult discussions, under the auspices of the OECD and G20, 136 jurisdictions released a Statement on the agreement on global minimum tax and partial reallocation of profit to market countries, marking the most significant reform of international tax rules in history.

The Statement released by the OECD/G20 Inclusive Framework on BEPS sets out the detail of the agreement and implementation timeline. Under the agreement, more than $125 billion from circa 100 of the largest MNEs will be reallocated to countries in which such companies have had extensive operations and revenue, but did not have taxable presence for corporation tax purposes under existing rules. Ireland, Estonia and Hungary withdrew their objections to agreement after sustained pressure from the European Council, paving the way for implementation of the deal in the European Union with instruments of EU law. The OECD Inclusive Framework member countries that have not joined the agreement are Kenya, Nigeria, Pakistan and Sri Lanka.

Pillar One, the profit reallocation element of the agreement, will be implemented by way of a new multilateral instrument to be finalised in 2022 which will come into effect from 2023. Notably, regarding Pillar One, the agreement ensures a standstill clause under which existing Digital Service Taxes and other similar relevant unilateral measures must be frozen or abolished in due course, under certain conditions. This was to avoid potential problems with US implementation, given the concerns expressed by US Secretary of Treasury Yellen who urged Congress to implement the deal swiftly by way of reconciliation process. Under said process, the US Senate could pass the bill implementing Pillar 1 with a simple majority of senators. Regarding Pillar Two, OECD worked to develop model rules by the beginning of 2022, which will be enacted into domestic legislation to be effective in 2023.

On 13 October, G20 Finance Ministers endorsed the agreement reached by 136 jurisdictions on global minimum tax and partial reallocation of profit to market countries, stating in its Communique that *"This agreement will establish a more stable and fairer international tax system. We call on the OECD/G20 Inclusive Framework on BEPS to swiftly develop the model rules and multilateral instruments as indicated in and according to the timetable provided in the Detailed Implementation Plan, with a view to ensure that the new rules will come into effect at global level in 2023."*

Following the announcement, Austria, France, Italy, Spain and the United Kingdom issued a joint statement with the United States, setting out an agreement reached for a transitional approach to walking back the existing unilateral digital taxes in those countries. They agreed that their unilateral measures will remain in force until Pillar 1 is implemented, but that if the amount of tax collected in the jurisdictions exceeds the equivalent amount that would be due under Pillar 1 in the first full year of implementation, that the excess amount will be creditable against the portion of the corporate income tax liability associated with Amount A as computed under Pillar 1 in these countries, respectively. Further, the United States agreed to terminate any proposed trade action and refrain from taking any further action against Austria, France, Italy, Spain, and the United Kingdom in relation to their unilateral digital taxes until the implementation of Pillar 1 takes place.

Signed, Sealed, Delivered: EU Commission Adopts Directive on Minimum Tax & OECD Model Rules Published

On 22 December 2021, the European Commission adopted the proposal for an EU directive on global minimum level of taxation for multinational groups. The directive intends to implement the OECD Pillar 2 agreement into the European Union, and will become EU law once adopted with unanimous vote of all Member states. The College approval follows the publication of the OECD Pillar 2 Model Rules, which contain detailed rules to assist governments in the implementation of minimum 15% tax rate as of 2023.

"The model rules are a significant building-block in the development of a two-pillar solution, converting the foundations of a political agreement reached in October into enforceable rules. The fact that Inclusive Framework members have managed to reach a consensus on this detailed and comprehensive set of technical rules demonstrates their commitment to a co-ordinated solution to addressing the challenges raised by an increasingly digitalised and globalised economy.", said Pascal Saint-Amans, Director of the OECD Centre for Tax Policy and Administration. Further detail on the implementation rules (ie. the commentary) is expected in January 2022.

The EU Directive implementation Pillar 2 directive into EU law follows the OECD model rules to ensure consistency, with one notable departure: in addition to cross-border operating MNEs, the EU directive is intended to apply to domestic groups reaching the threshold of €750 million revenue (combined financial revenues per year), with either a parent or a subsidiary situated in an EU Member State. The provision on application of the directive to domestic entities is unlikely to have significant impact and is intended to ensure consistency with EU law principles, notably the principle of equal treatment (non-discrimination). As consequence, the Under-Taxed Payments Rule will only apply to external transactions, and not on intra-EU level.

The implementation of the Pillar 2 directive affects existing EU tax law provisions (ATAD), specifically for the Controlled Foreign Company (CFC) rules, which could interact with the Income Inclusion Rule, the primary rule of Pillar 2, which merits amendments of ATAD. In practice, ATAD CFC rules will take precedence and any additional taxes paid by a parent company under a CFC legislation in a given fiscal year will be taken into consideration by attributing those to the relevant low-taxed entity for the purpose of computing its (jurisdictional) effective tax rate.

Some Member states like Estonia have expressed their reservations, with the file now in the hands of the upcoming French presidency of the EU. Additional hurdles include problems with US implementation, where the Build Better Act (which passed the House) has been effectively blocked in the Senate by Democratic Senator Joe Munchin, citing fears of rising inflation and the effect of the bill on the US federal deficit. The White House specifically named Senator Munchin as putting in jeopardy not only the minimum tax provisions but also President Biden's flagship $1.75 trillion social spending bill.

EU Commissioner Paolo Gentiloni, responsible for Economy, said that he is confident the bill would pass the US Senate, and the Commission is already looking towards the new framework for business

taxation in the EU (BEFIT), aimed to streamline corporate taxation rules and create a more business-friendly environment in the Single Market.

Commissioner Gentiloni also added: *"In October of this year, 137 countries supported a historic multilateral agreement to transform global corporate taxation, addressing longstanding injustices while preserving competitiveness. Just two months later, we are taking the first step to put an end to the tax race to the bottom that harms the European Union and its economies. The directive we are putting forward will ensure that the new 15% minimum effective tax rate for large companies will be applied in a way that is fully compatible with EU law. We will follow up with a second directive next summer to implement the other pillar of the agreement, on the reallocation of taxing rights, once the related multilateral convention has been signed. The European Commission worked hard to facilitate this deal and I am proud that today we are at the vanguard of its global rollout."*

EU Commission Vice-President Dombrovski added: *"By moving quickly to align with the far-reaching OECD agreement, Europe is playing its full part in creating a fairer global system for corporate taxation. This is particularly important at a time when we need to increase public financing for fair sustainable growth and investment and meet public financing needs too – both for tackling the pandemic's aftermath and driving forward the green and digital transitions. Putting the OECD agreement on minimum effective taxation into EU law will be vital for fighting tax avoidance and evasion while preventing a 'race to the bottom' with unhealthy tax competition between countries. It is a major step forward for our fair taxation agenda."*, Mr Dombrovski said.

ECOFIN are expected to have their first discussion on the file at its January meeting, with agreement to be pushed for as soon as possible by the French Presidency of the Council of the EU. Commission Gentiloni stressed that receiving Parliament's opinion quickly would be key to ensuring adoption takes place in time for rules to come into force in 2023 as planned.

EU Commission's 2022 Work Programme

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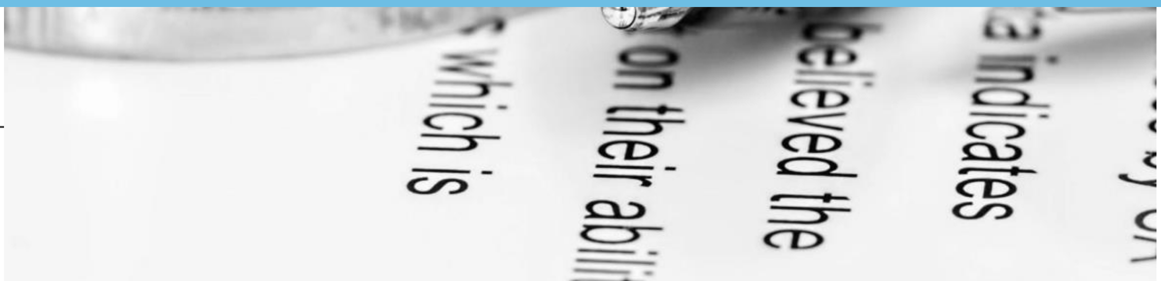

EU Commission's 2022 Work Programme

In an exchange of views with the Subcommittee on Tax Matters of the European Parliament on 30 November 2021, Commissioner Gentiloni set out the upcoming tax priorities for the European Commission as it enters the second half of its mandate on 1 January 2022.

The European Commission work programme for 2022 indicates that the EU will focus its taxation policy priorities on implementation of the global tax agreement concerning Pillars 1 and 2. The work programme states the "European Commission will now strive to show the EU's leadership in global tax fairness, by ensuring a swift and consistent implementation across the EU."

Implementation of Pillar 1 largely depends on the ongoing technical level work at the OECD, which should inform the EU legislative process. Depending on the agreed solution, EU's implementation of Pillar 1 OECD global agreement on re-allocation of taxing rights might come as a legislative item (directive), under Article 115 TFEU, which requires consensus of all Member states.

Commissioner Gentiloni also confirmed that once work by the OECD on the text of the multilateral convention for Pillar 1 is more advanced, the Commission will progress its own work in implementing the rules. In the interim the EU digital levy plans will remain on hold, said the Commissioner.

This EU proposal will be complemented with a Directive on minimum effective tax rates disclosure, concerning entities within scope of the Directive implementing Pillar 2 in the European Union.

Files to Watch in 2022

Commissioner Gentiloni outlined the following as key priorities for 2022:

Fighting Shell Entities: A proposal on fighting the use of shell entities to ensure that entities with no/minimal presence do not benefit from tax advantages in the EU, by allowing Member states to tax a shell entity located in another EU Member state, satisfying certain conditions, as if the shell were located within their own taxing jurisdiction. It is expected that the criteria identifying a company as a 'shell entity' would be based on a methodology similar to the one already used by the EU in the DAC6 hallmarks.

Updates to the List of Non-Cooperative Jurisdictions: A "more robust approach for zero tax jurisdictions in the context of the EU list of non-cooperative jurisdictions", noting that the EU expects the OECD Global Forum on harmful tax practices and the OECD Inclusive Framework to propose an international response to this issue.

Reforms for the Code of Conduct Group: Reforming the mandate of the Code of Conduct Group to fight measures leading to double non-taxation or double or multiple tax benefits, noting that although two Member States, Hungary and Estonia, continue to oppose revisions, an agreement is expected soon, and potentially this year.

Public Transparency: A proposal to "improve public transparency around the effective tax rate paid by large companies in the EU" which will make use of the method agreed under Pillar 2 for minimum taxation.

DAC8: A proposal to revise the EU directive on administrative cooperation to extend to crypto-assets.

DEBRA: A proposal for a debt-equity bias reduction allowance, to redress imbalance by ensuring a better balance between the treatment of debt and equity for tax purposes.

Further ahead, Commissioner Gentiloni stated that comprehensive reform to the EU tax system is on the agenda for 2023, when the Commission will put forward its proposals for so-called BEFIT initiative: a plan for a holistic EU business tax framework fit for the decades to come.

Landmark EU Climate Change Policy Package

03

Landmark EU Climate Change Policy Package

On 14 July, the European Commission proposed an ambitious climate policy package, encompassing multiple policy instruments to deliver on the European Green Deal Commitment to make Europe a carbon neutral continent by 2050, and to cut carbon emissions 55% by 2030. The package includes a number of instruments, which will require consent of Member states to achieve full implementation across the continent. Proposed instruments include: extension and reenforcement of the ETS to new sectors; increased use of renewables and energy efficiency; a faster roll-out of low emission transport modes and the infrastructure and fuels to support them; an alignment of taxation policies with the European Green Deal objectives, and measures to prevent carbon leakage.

Tax-related policy instruments include revisions of the Energy Taxation Directive, with a key policy goal to help Member States transition to green taxes, as less detrimental to growth and more sustainable compared to the present over-reliance on taxes on work/ labour. The Carbon Adjustment Mechanism aims to level the playing field with imported goods from countries which do not apply the same standards as Europe, thus preventing carbon leakage. To do so, the Directive aims to put a price on carbon-intensive imports, thus encouraging trade partners to implement similar green policies at home. As a result, global reduction of carbon emissions could be achieved simultaneously. A Social Climate Fund is planned to help Member states facilitate the green transition and avoid situations where certain Member states or regions are left behind.

During an event held by POLITICO in December 2021, French Secretary of State for Europe Clément Beaune confirmed that France will prioritise negotiations to reach an EU deal on the proposed Carbon Border Adjustment Mechanism when it takes over the Presidency of the Council of the EU from 1 January 2022.

Member States have pushed to exempt certain countries from the proposals, which Mr Beaune commented on during the POLITICO event, saying countries could only be exempted if they are willing to adhere to similar standards as the EU. He stated that the French approach will be to "...try to get inspiration from what we have done successfully in the end with the digital debate. So to have first an agreement at the EU level … but also to be open, which I think is the basic idea of these climate clubs, to an international negotiation with like-minded countries....the U.S., for instance, or the U.K, and to say: 'If you're ready to go with the same standards as we are doing, if you have the same green ambitions, there's no reason why we should have competition or a kind of adjustment mechanism between each other.'" New Zealand and Canada were also mentioned in the discussion as other potential countries to be included in the discussions.

President von der Leyen recently commented on the proposal prior to the COP26 conference, saying that "the EU was in favour of a global solution that would see the world's biggest emitters agree on global carbon pricing. To avoid carbon leakage, now introduce slowly but surely a carbon border adjustment mechanism that says if you come with dirty products on our market, you have to pay a price as if you were in the Emissions Trading System of the European Union. But we prefer you keep the money in your economy by putting a price on carbon in your economy."

Commissioner Paolo Gentiloni said of the proposals that this is the 'now or never' moment for the world: *“Our efforts to tackle climate change need to be politically ambitious, globally coordinated and socially fair. We are updating our two-decades old energy taxation rules to encourage the use of greener fuels and reduce harmful energy tax competition. And we are proposing a carbon border adjustment mechanism that will align the carbon price on imports with that applicable within the EU. In full respect of our WTO commitments, this will ensure that our climate ambition is not undermined by foreign firms subject to more lax environmental requirements. It will also encourage greener standards outside our borders. With every passing year the terrible reality of climate change becomes more apparent: today we confirm our determination to act before it is really too late.”* Similarly, Commission President Ursula von der Leyen said: *“The fossil fuel economy has reached its limits. We want to leave the next generation a healthy planet as well as good jobs and growth that does not hurt our nature."*

The European Commission is proposing to Member states that part of the revenue generated by the July 2021 proposal for a carbon border adjustment mechanism and the emissions trading scheme (ETS) goes direct into the EU budget, in order to finance the post-pandemic recovery of the European continent. In addition, EU’s own additional resources would come as portion of the residual profits of MNEs within scope of Pillar 1, once the Multilateral Convention negotiated by the BEPS Inclusive Framework and the related EU Directive are both in force, as follows:

- 25% of the revenues generated by EU emissions trading become an own resource for the EU budget,
- 75% of the revenues generated by a carbon border adjustment mechanism become an own resource for the EU budget,
- 15% of the share of the residual profits of the MNEs under Pillar 1.

It is estimated that the package would be worth 17 billion Euros from 2026, as part of the new multi-annual financial framework for the EU. The Commission also aims to create a carbon market for cars and buildings which is opposed at present by France and Spain, as well as a more general opposition towards certain carbon tax measures from the Eastern European Member states who fear these policies are driving energy prices higher up.

World leaders and their negotiating teams attending the UN Conference on Climate Change (COP26) agreed on a market-based mechanism to enable countries to trade in carbon offsets, in line with previous goals set under Article 6 of the 2015 Paris climate agreement. The mechanism will allow countries to trade in carbon credits, for the purposes of offsetting these against emissions, in order to meet climate targets.

Negotiators agreed a two-track system, a private system in which bilateral trades of offsets will not be subject to any tax, and a separate centralised public system in which 2% of offset credits will be cancelled, to discourage the overuse of offsets and increase cuts in overall emissions. A 5% levy will also be collected in this system, to fund adaptation for developing countries. It is expected that investment in schemes that generate carbon credits will see a significant increase following the agreement of the mechanism.

EU Policy – Direct Tax Update

04

EU Adopts Shell Entities Directive (Unshell Proposal)

In late December, the European Commission adopted a proposal for a directive on the misuse of shell entities, or unshell legislation in the EU-bubble jargon. The directive aims to enable more tools for tax authorities to detect the misuse of shell entities, by requiring reporting (relevant disclosure) in tax returns and consequently denying benefits of tax treaties and EU tax law.

The Directive does not define shell entities, but requires certain criteria to be fulfilled (gateway principle and substance requirements), to allow the tax administrations to designate an entity as a shell. In practice, the gateway principle will look into activities of the entities based on the income where 75% of an entity's overall revenue in the previous two tax years does not come from the entity's trading activity or if more than 75% of its assets are real estate property or other private property of particularly high value. The second gateway element looks at the cross-border element and it is satisfied where the relevant income is received through cross-border transactions or it is passed on to other entities abroad. The final gateway indicator is linked to the corporate management and is aimed to asses whether the administrative operations of the entity are in-house or outsourced. With some exceptions, a company which ticks the boxes for these three indicators will be required to disclose in its tax return information concerning the premises of the company, bank accounts, tax residency of its directors and its employees. If an entity fails at least one of the substance indicators, it will be presumed to be a shell.

As a consequence, where a company is considered to be a shell entity, it will be denied tax treaty and EU tax law benefits, notably arising from the Parent-Subsidiary and Interest and Royalties Directives. The Member State of residence of such company can either deny to issue a tax residence certificate or the certificate shall state that the entity is a shell company. In addition, payments to third countries will be subject to withholding tax and will not be seen as passing-through the shell for tax purposes, with inbound payments taxed in the state of the shell's shareholder as a result of this targeted tax treatment.

Commission's impact assessment and public consultation comments from professional associations note that it remains challenging to define what constitutes a shell entity and that assessing lack of substance depends on the facts and circumstances of each specific entity and transaction. Public consultation comments also highlight that taxpayers should always have an effective right to provide evidence of their specific circumstances, particularly concerning structures that are not put in place to obtain tax advantage but for valid commercial reasons, in accordance with settled ECJ case-law. To address some of these concerns, the Commission proposal includes a 'rebuttal of the presumption' provisions, where tax administrations are obliged to allow companies deemed to be a shell to rebut this presumption by providing further evidence of the commercial rationale behind their business activity.

Penalties for non-compliance with the reporting requirements of this directive include administrative sanction of at least 5% of the undertaking's turnover in the relevant tax year, if the undertaking fails to disclose relevant information or if it makes a false declaration in the tax return.

This Directive also requires unanimous support of Member states to be enacted into EU law.

EU Public Country-by-Country Reporting Directive Adopted & Published in the Official Journal of the EU

On 1 December, the Directive on Public Country-by-Country Reporting, Directive 2021/2101 amending Directive 2013/34/EU as regards disclosure of income tax information by certain undertakings and branches, was published in the Official Journal of the European Union, having been adopted by the European Parliament in November. The directive introduces public country-by-country reporting obligations for multinationals to declare amounts of tax paid in EU Member States.

Under the legislation, multinationals and their subsidiaries which have an annual revenue over €750 million and are active in more than one EU country will be required to publish the following information:

- The nature of the company's activities;
- The number of full-time employees;
- The amount of profit or loss before income tax;
- The amount of accumulated and paid income tax and accumulated earnings.

If a subsidiary is deemed to exist solely for the purpose of avoiding the reporting requirements, the subsidiary will also be required to report the same tax information. The reported information will be made publicly available online in a harmonised format.

Co-rapporteur on the file for the European Parliament, Evelyn Regner, said of the adopted legislation: *"Persistence pays off. Despite all the adversity and a five-year-long blockage in the Council, we can proudly say that the call for more corporate tax transparency has been answered. For too long, corporations have played by their own rules. Thanks to the transparency provided by public country-by-country reporting, we will now be able to shed light on this opaque corporate jungle."*

In statements issued at the EU Council's first reading of the draft public CbCR directive, several Member states rejected the legal basis of the legislative proposal, namely Croatia, Cyprus, the Czech Republic, Hungary, Ireland, Luxembourg, Malta and Sweden. The countries all set out in the statements that they are of the view that given "both the aim and the content of the proposal relate to 'fiscal provisions' ", that the proposal for the directive should be based on Article 115 TFEU, not Article 50(1). Croatia also specifically stated that it "is of the opinion that the agreed Proposal should not become precedent for a qualified majority voting in the future decision-making process in regard to tax matters."

The Directive entered into force on 21 December 2021, and Member States have 18 months to implement the directive into domestic legislation. Reporting obligations will apply from mid-2023.

EU Commission Publishes Anti-Money Laundering Legislative Package

In July, the European Commission published its Anti-Money Laundering legislative package, which will upgrade the existing EU anti-money laundering legislative (AML) framework.

The package consists of four proposals, namely:

- A Regulation establishing a new EU AML/CFT Authority;
- A Regulation on AML/CFT, containing directly-applicable rules, including in the areas of Customer Due Diligence and Beneficial Ownership;
- A sixth Directive on AML/CFT ("AMLD6"), replacing the existing Directive 2015/849/EU (the fourth AML directive as amended by the fifth AML directive), containing provisions that will be transposed into national law, such as rules on national supervisors and Financial Intelligence Units in Member States;
- A revision of the 2015 Regulation on Transfers of Funds to trace transfers of crypto-assets (Regulation 2015/847/EU).

Significantly, the package will establish an EU Anti-Money Laundering supervisory body, the Anti-Money Laundering Authority, or AMLA, which would commence operating in 2024 and is envisaged to employ around 350 people. The AMLA will establish a single integrated system of supervision across the EU, be given direct supervisory powers at EU level to monitor and coordinate national supervisory bodies, as well as be given the ability to give fines and directly supervise cross-border financial companies. The AMLA will also coordinate with national Financial Intelligence Units (FIUs) and facilitate joint analyses to detect illicit financial flows.

The package will also create a single EU Rulebook for AML across the EU, including rules on Customer Due Diligence, Beneficial Ownership and the powers and task of supervisors and Financial Intelligence Units (FIUs). Existing national registers of bank accounts will be linked to the system, providing access to FIUs on bank accounts and deposit boxes. It is also proposed that law enforcement will be provided access to the system.

Other notable elements of the package include plans to extend the full application of the AML framework to the crypto sector, impose an EU-wide cash payment limit of EUR 10,000 and create a "black-list" and "grey-list" based on the recommendations made by the global money laundering and terrorist financing watchdog, Financial Action Task Force (FATF). Any country listed in recommendations by FATF will be listed by the EU in either the "black-list" and a "grey-list", and measures will be applied by the EU on the basis of the risk level. The EU will also be able to list additional countries not subject to a FATF recommendation, based on its own assessment of risk level to the EU.

The package will now be considered by Parliament and Council. The proposals set out that the EU AML Authority would commence its duties from 2024 onwards, with the direct supervision role to commence later, after the Directive is transposed and the regulatory framework starts to apply.

Withholding Taxes – New EU System to Avoid Double Taxation

In September, the European Commission published a Roadmap concerning a new EU system on withholding taxes, designed to avoid double taxation. The publication precedes a public consultation questionnaire which will be launched in the coming months.

The Commission Roadmap states that despite prior actions by the Commission *"tax barriers to cross-border investment and the risk of tax abuse persist within the European Union. One of these remaining barriers is the problem of inefficient withholding tax relief procedures. According to the most recent publicly available data from 2016 costs related to withholding tax refund procedures, foregone tax relief and opportunity costs are estimated to a value of EUR 8.4 billion annually. The Action Plan for fair and simple taxation supporting the recovery strategy proposes to introduce a common, standardised EU-wide system for withholding tax relief at source coupled with a new exchange of information and cooperation mechanism between administrations"*.

The policy options that are currently being considered in relation to the intended proposal for a new EU system on withholding taxes includes:

Option 1: Improving withholding tax refund procedures to make them more efficient: This option entails the implementation of several measures, the objective of which is to simplify and streamline withholding tax refund procedures by making them quicker and more transparent.. These measures are not limited by but could include: the establishment of common EU standardised forms and procedures for withholding tax refund claims irrespective of the Member States concerned and the obligation to digitalise current paper based relief processes;

Option 2: Establishment of a fully-fledged common EU relief at source system: This option entails the implementation of a standardized EU-wide system for withholding tax relief at source whereby the correct withholding tax rate, as provided in the DTC is applied at the time of payment by the issuer of the security, to the non-resident investor thereby not incurring double taxation.

Option 3: Enhancing the existing administrative cooperation framework to verify entitlement to double tax convention benefits: This option envisages a reporting and subsequent mandatory exchange of beneficial owner-related information on an automated basis, to reassure both the residence and source country that the correct level of taxation has been applied to the non-resident investor.

The Commission will launch a consultation in questionnaire in the coming months concerning the above policy options, via the Have Your Say website. Input will be invited over a 12-week period via the online portal.

EU Policy - Indirect Tax Update

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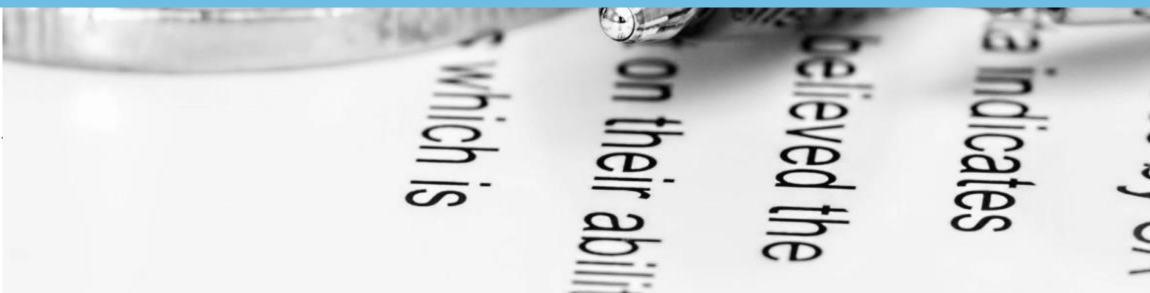

New EU VAT E-Commerce Rules Come Into Force

The new e-commerce rules entered into force on 1 July, creating a simplified VAT regime for cross-border supplies of goods (B2C) and distance sales. The new rules provide for a system to declare and pay VAT in the EU using the Import One-Stop Shop and also level the playing field between EU businesses and non-EU sellers.

Online sellers, including online marketplaces and platforms can now register in one EU Member State and this will be valid for the declaration and payment of VAT on all distance sales of goods and cross-border supplies of services to customers within the EU. According to the European Commission, online marketplaces will now benefit from a reduction in red tape of up to 95% by registering with the new One Stop Shop (OSS).

CFE Tax Advisers Europe has now published an Opinion Statement on issues with supply of goods with transport under e-commerce rules. Determining the nature of a transaction is one of the most important steps when determining the VAT treatment of supplies, including how the place of supply rules operate. It is only after the nature of a supply has been determined, including determining whether a supply should be considered a supply of goods or services, that the different rules regarding determination of the place of taxation can be applied. The situation becomes particularly complicated in cases where the supplier provides to its buyer both supplies of goods and services at the same time. In such cases it must be established whether, for the purposes of VAT, the supply should be treated as two distinct taxable transactions or as a single composite supply for VAT purposes. This question often arises when the supplier supplies goods and provides transport of the goods at the same time. Such a situation is even more common with e-commerce activities, when businesses are selling goods online to final consumers located in other Member States (distance sales of goods).

In the statement, CFE identifies that different rules apply when determining the place of supply of goods and the transport of goods, which often cause administrative problems in practice. Since there are different rules regarding determination of place of taxation for transportation services and supply of goods, CFE identifies through highlighting these issues in practice that it would be helpful if there could be some Commission guidance issued clarifying what the position is or, alternatively, if consideration could be given to making changes to the VAT Directive so that transport services are dealt with more consistently with the underlying supply.

EU VAT Committee Published Updated Guidelines

The European Commission's VAT Committee, formed of representatives from Member States and the Commission to promote the uniform application of the provisions of the VAT Directive, has now published updated guidelines following from its 118th meeting which took place on 19 April. The guidelines are of an advisory nature only and are not binding on the Commission or Member States.

The new guidelines concern the following matters:

- Quick Fixes: Return of goods placed under call-off stock arrangements, and the moment when the goods are considered as returned and accounting methods to determine which goods are returned;
- Calculation of the EU place-of-supply threshold for taxable persons making supplies of intra-Community distance sales of goods and supplies of telecommunications;
- Broadcasting and electronic services to non-taxable persons: the decision in Case C-568/17, Geelen, on interactive sessions filmed and broadcasted in real time via the internet;
- VAT rules applicable to transactions related to the recharging of electric vehicles; and
- VAT related issues in view of the withdrawal of the UK from the EU.

The guidelines can be found here.

EU Commission 2021 VAT Gap Report Published

The European Commission published the 2021 VAT Gap in the EU Report in the second half of 2021, analysing data on collection revenue from 2019. The report showed an amount of €134 billion in Value-Added Tax (VAT) was lost by the Member States in 2019 as a result of VAT fraud and evasion, VAT avoidance and optimisation practices, bankruptcies and financial insolvencies, as well as miscalculations and administrative errors. However, this figure had decreased by around €7 billion compared to 2018.

Paolo Gentiloni, Commissioner for Economy, said of the report: "Despite the positive trend registered in the last few years, the VAT Gap remains a major concern – particularly in view of the immense investment needs our Member States must address in the coming years. This year's figures correspond to a loss of more than €4,000 per second. These are unacceptable losses for national budgets, and mean that ordinary people and businesses are left to pick up the shortfall through other taxes to pay for vital public services. We need to make a joint effort to crack down on VAT fraud, a serious crime that takes money out of consumers' pockets, undermines our welfare systems and depletes government coffers."

The Commission will launch legislative proposals to further modernise the VAT system, including the reinforcement of Eurofisc, a network comprised of national officials from the 27 Member States and Norway. The network use a Transaction Network Analysis tool, financed by the EU, to exchange information on VAT, aiding in the fight against VAT fraud in the EU.

EU Blacklist & Code of Conduct Update

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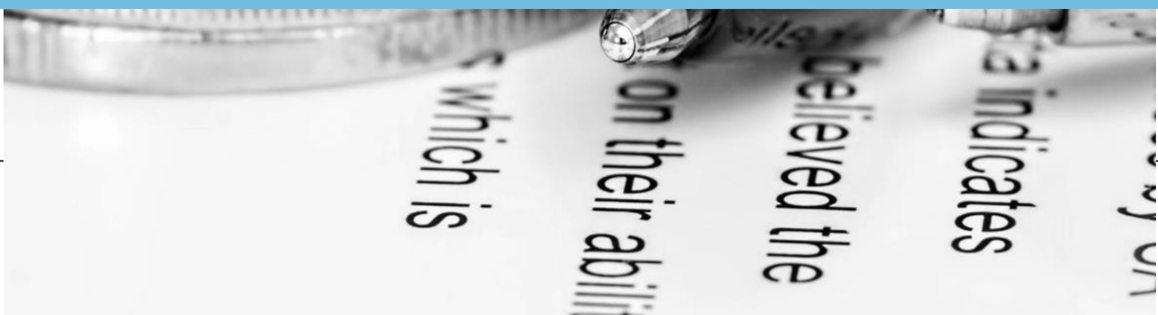

EU Updates 'Blacklist' of Non-Cooperative Jurisdictions

The Council of the European Union, sitting as ECOFIN, on its meeting of 5 October decided to remove a number of countries from the EU blacklist of non-cooperative jurisdictions for tax purposes, whilst adding certain countries to the 'watchlist'.

The Council removed Anguilla, Dominica and Seychelles from the EU list, given they were considered 'largely compliant' by the OECD Global Forum regarding the exchange of information on request. A number of countries were added to the watchlist, formally Annex II, with countries that comply with international tax standards but that have yet to implementing EU's tax good governance requirements. Costa Rica, Hong Kong, Malaysia, North Macedonia, Qatar and Uruguay have now been added to this document, while Australia, Eswatini and Maldives have have been removed for having implemented the necessary reforms, as stated by the Council.

The latest EU list update was called 'grotesque' by some European Parliament members and other critics, in light of the Pandora Papers revelations on the role of certain off-shore jurisdictions.

The EU Parliament renewed criticism of the EU Blacklist following the publication of the Pandora Papers and the latest update, adopting a Resolution at its plenary session in Strasbourg on 6 October. The Parliament and other critics of the Blacklist call for the criteria to be reviewed and linked to real economic activity in a given jurisdiction by companies, and for zero or low tax jurisdictions to be automatically included in the list.

According to the resolution, the EU should reform the Code of Conduct for Business Taxation and called on the Commission to evaluate the effectiveness of patent boxes and other intellectual property (IP) regimes under the new nexus approach defined by Action 5 of the BEPS Action Plan on HTP, including the impact on revenue losses. The European Parliament also asked the Commission to consider proposals if there is no impact of IP regimes on real economic activity, while noting that the US administration is proposing to repeal its Foreign-Derived Intangible Income (FDII) rules.

Regarding the reform of the Code of Conduct, the Parliament asked for revision of the criteria, the governance and the scope of the Group through a binding instrument built on the current intergovernmental arrangements, with involvement of experts from civil society, the Commission and Parliament, which will allow for more productive fight against harmful tax practices, the resolution concludes.

French Progressive MEP Aurore Lalucq, the parliament rapporteur, said these rules must be "a sharp weapon in the fight against tax avoidance and evasion" and proposed a revised code called FATAL, framework on aggressive tax arrangements and low-rates.

International Tax Policy Updates

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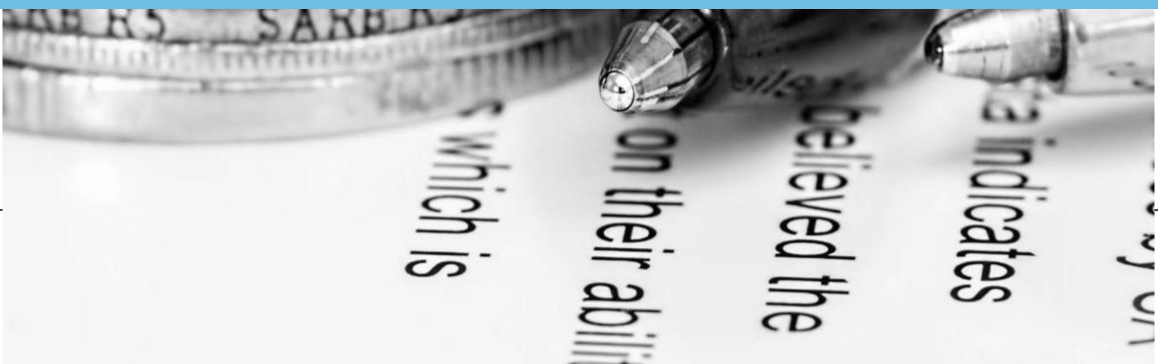

Tax Administrations Accelerate Digital Transformation

The OECD's Forum on Tax Administration has issued the Tax Administration 2021 report, which compares data on particular aspects of tax administration and tax systems across 59 economies, compiled in the 2020 International Survey on Revenue Administration. The report examines the data to highlight key trends, innovations and best practice, in order to facilitate information sharing and dialogue between tax revenues on improving tax systems.

The report highlights that in response to the coronavirus crisis, tax administrations had significantly improved their digital transformation processes, and invested resources in digital solutions for tax compliance. The report shows that 9 out of 10 business and over 80% of individuals now filed electronic returns, and that around 75% of administrations have invested in AI and machine learning in tax administration processes.

The Chair of the Forum on Tax Administration, Bob Hamilton said of the report, “Tax administrations’s efforts to move more of their processes online has not only enhanced service delivery, reduced burdens and improved compliance, but it has also made us more resilient. Leading a tax administration myself, it became immediately clear that digital service delivery would be of significant help in our response to the COVID-19 pandemic. Our digital readiness allowed us to quickly take on new roles to assist in the provision of wider government support and ensured that we could continue to deliver effective services to taxpayers during times of social distancing and remote working.”

OECD Publishes Country-by-Country & MAP Peer Review Reports

The OECD has issued a compilation of the 2021 peer review reports completed in line with Action 13 on Country-by-Country Reporting of the OECD/G20 BEPS Project, as well as the Stage 2 peer review monitoring reports of Action 14 of the BEPS Project on Mutual Agreement Procedure.

The compilation of Country-by-Country reporting covers 132 Inclusive Framework members and reviews the implementation of the Action 13 minimum reporting standards. The report notes that over 100 jurisdictions have legislation imposing filing requirements on MNEs, and that recommendations made in earlier peer review phases have largely been addressed. The report is completed on an annual basis, and the next update will be provided in Q3 of 2022.

Concerning Action 14 and the improvement of the tax dispute resolution mechanisms, the OECD issued reports for the jurisdictions of Brazil, Bulgaria, China, Hong Kong (China), Indonesia, Russia and Saudi Arabia. The reports assess the efforts by the countries to implement the Action 14 minimum standard as agreed to under the OECD/G20 BEPS Project and recommendations contained in the Stage 1 peer review reports. All jurisdictions have signed the OECD MLI except Brazil, with Indonesia, Russia and Saudi Arabia having already ratified the instrument. All jurisdictions have either updated or introduced MAP guidance, and the majority have successfully decreased the time taken to close MAP cases or added additional personnel to their competent authorities dealing with MAP cases.

OECD Paper on Cross-Border Withholding Tax Relief Procedures

The OECD has issued a paper containing best practice recommendations on co-ordinating administrative withholding tax procedures, noting the strain that has been placed on tax administrations and taxpayers in the wake of the COVID-19 outbreak to comply with normal administrative procedures. The paper contains an overview of the various cross-border withholding tax relief procedures and the features which create challenges for compliance.

The best practice recommendations include that grace periods be granted for tax residence certificates, that electronic documentation be accepted, that reliance be placed on account information which may be available from financial institutions and that any apostilisation requirements for documents be temporarily suspended.

Forum on Tax Administration Vows to Investigate Pandora Paper Data

The OECD's Forum on Tax Administration and its investigational arm, the Joint International Task Force on Shared Intelligence and Collaboration (JITSIC), issued a statement concerning the so-called "Pandora Papers", published by the International Consortium of Investigative Journalists, following an investigation carried out by over 600 journalists into the largest known data leak on the use of offshore companies. The leak comprises over 11 million files on the operations of 14 particular offshore service firms who facilitate the use of offshore companies. Individuals identified in the leak are accused of using offshore vehicles for concealing illicit assets.

The Forum on Tax Administration and JITSIC have confirmed that they will use the tools at their disposition, including JITSIC's net work of cooperation, the OECD standard on the exchange of information on request, and the OECD Common Reporting Standard, to "pool resources, share information and rapidly develop a more accurate picture of potential wrong doing in order to facilitate further investigations" and investigate and identify tax evasion or avoidance in relation to the Pandora Papers, as data becomes available.

The process will follow the model used for the Panama and Paradise Papers.

State Aid & Case Law Updates

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Nike Loses Procedural Challenge to Commission's State Aid Case

On 14 July 2021, Nike lost its challenge to Commission's State aid case on formal grounds, the General Court of the EU ruled in Case C-648/19 (Nike European Operations Netherlands BV & Converse Netherlands BV v European Commission). Nike alleged incorrect assessment of the character of the State aid; incorrect assessment of the nature of an APA in Netherlands law; and, breach of the principles of good administration and equal treatment. The second plea alleged breach of the obligation to state reasons and incorrect assessment of selectivity. The third plea alleged breach of the applicants' procedural rights; and, premature initiation of the formal investigation procedure.

The Court dismissed Nike's arguments on incorrect assessment of selectivity, citing established case-law, such as Commission v MOL: in the case of individual aid, the identification of the economic advantage is, in principle, sufficient to support the presumption that it is selective. The presumption of selectivity operates independently of the question whether there are operators on the relevant market in a comparable factual and legal situation. Only when examining an aid scheme it is necessary to identify whether the measure in question, notwithstanding the finding that it confers an advantage of general application, does so to the exclusive benefit of certain undertakings or sectors (Judgment of 4 June 2015, Commission v MOL, C-15/14 P, paragraph 60).

On the procedural arguments, the Court established that the Commission was entitled to initiate the formal examination procedure and did not breach the principles of equal treatment and good administration. As a result of this judgment the Commission will continue its investigation into the APAs issues by the Dutch tax administration from 2006 to 2015, establishing levels of royalty paid by the Nike/ Converse subsidiaries for use of the IP belonging to the group company for products sold in the EMEA regions.

EU Commission Appeals General Court Amazon State Aid Ruling

The European Commission lodged an appeal against the EU General Court's ruling in its dispute with Amazon concerning profit allocation and application of TNMM as transfer-pricing method, in Case T-816/17 *Luxembourg and Amazon v Commission*.

The General Court in its ruling found that the Commission did not prove the existence of State aid to the requisite legal standard and annulled the Commission decision. From a transfer-pricing perspective, the Court found that even if the 'arm's length' royalty should have been calculated using the Commission's designated group company as the 'tested party' in the application of the TNMM, the Commission still did not establish the existence of an advantage since the Commission did not take into account the evolution of the intangible assets and the cost sharing agreement, ie. the subsequent increase in value of said intangible assets.

The Commission will argue before the European Court of Justice that the General Court made a number of errors of law in its judgment, notably that the Court should have based its ruling on the profits recorded in Luxembourg by Amazon rather than looking at the US where it holds its intellectual property.

ECJ Sets Aside General Court Ruling in Belgian Excess Profits Case

The European Court of Justice issued its decision in the Belgian Excess Profit State aid case, C-337/19 *Commission v Belgium and Magnetrol International*, setting aside the decision of the General Court. The key issue in the appeal was whether the General Court rightfully held that the Commission had not demonstrated to the requisite legal standard the existence of a 'consistent tax administration practice in the contested decision'. In its judgment the General Court repealed the Commission decision on grounds of failure to state reasons as to the choice of advance rulings used, in particular why 6 examples chosen by the Commission were sufficiently representative of all 66 advance rulings under scrutiny. The Commission argued that the General Court incorrectly misclassified 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.

The Court of Justice in its decision held that the General Court misapplied the term 'act' in Article 1 by limiting its analysis of the conditions of Article 1(d) of Regulation 2015/1589 to only the acts referred to in recital 99 of the decision at issue, and that the General Court's conclusion that the Commission had not demonstrated the existence of a 'systematic approach' was incorrect in law, ordering that the General Court judgment be set aside. The Court of Justice referred back to the General Court the questions to assess the pleas in law, i.e. whether the advance tax rulings concerning the downward adjustment of profits constitute State aid, and subsequently, whether the recovery of the alleged aid infringes the principles of legality and of the protection of legitimate expectations.

Significantly, in paragraphs 157 to 167 of the judgment, in respect of arguments that the Commission exceeded its powers by using EU law on State aid in order unilaterally to determine matters falling within the exclusive tax jurisdiction of a Member State, the Court of Justice held that action by Member States in areas that are not subject to harmonisation by EU law is not excluded from the scope of the provisions of the FEU Treaty on the monitoring of State aid. The Court stated that "*Member States must exercise their competence in the field of direct taxation in compliance with EU law and, in particular, the rules established by the FEU Treaty on State aid. They must therefore refrain, in the exercise of that competence, from adopting measures which may constitute State aid incompatible with the internal market within the meaning of Article 107 TFEU*".

Accordingly, the Court of Justice held that the Commission "*could not be accused of having exceeded its powers when it examined the measures constituting the scheme at issue and when it ascertained whether those measures constituted State aid and, if so, whether those measures were compatible with the internal market within the meaning of Article 107(1) TFEU*" and that this could not be called into question on the basis of a lack of tax jurisdiction for the taxation of excess profits or national competence to adopt measures to avoid double taxation, as *"in exercising that competence, the Member States must refrain from adopting measures which may constitute State aid, the monitoring of which falls within the Commission's competence. The same is true of the adoption by the Member States, in the exercise of their powers in the field of taxation, of measures necessary to prevent double taxation situations"*.

ECJ Advocate-General Opinions in Fiat/ Ireland v Commission

Advocate General Pikamäe issued Opinions in Cases C-885/19 *P Fiat Chrysler Finance Europe v Commission* and Case C-898/19 *P Ireland v Commission*, proposing that the Court allows the appeal brought by Ireland and annul the Commission's decision declaring aid which Luxembourg granted to Fiat as being incompatible with the Single Market, and to dismiss the appeal brought by Fiat Chrysler Finance Europe against the said Commission decision.

The Advocate General suggests that Ireland's appeal should be declared acceptable in so far as the Commission's use of the arm's length principle is not a rule which is expressly codified in national law, therefore in breach of the Treaty provisions governing the division of competences between the European Union and the Member States and providing for a prohibition of harmonisation in the field of direct taxation.

Regarding Fiat's appeal, the Advocate-General suggests that the Court dismisses the appeal in its entirety. The General Court correctly held that the Commission was not required to take account of the intra-group and cross-border elements of the effects of the tax ruling when determining whether that ruling conferred an advantage, in accordance with applicable provisions of Article 107(1) of the Treaty, the Advocate General notes.

The opinions of EU Advocates General are of advisory character and are not binding for the European Court of Justice.

EU Tax Policy Report

Semester II 2021

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