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EU Tax Policy Report

Semester I 2022

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 2022.

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Highlights

In January, EU Finance Ministers began their first discussions concerning the European Commission proposal for an EU directive on global minimum level of taxation for multinational groups, adopted just prior to Christmas last year. The Directive will implement the OECD Pillar 2 agreement into European Union law, and follows on from the publication of the OECD Pillar 2 Model, which contains detailed rules to assist governments in the implementation of the minimum 15% tax rate as of 2023.

The French Presidency of the Council of the EU was eager for the Directive to be approved as quickly as possible in Semester 1 of 2022; alas, this was not to be. Although by March significant progress had been made, with a revised compromise text published which revealed some notable changes from the original proposal, the most significant of which being that the time limit for transposition has been changed to 31 December 2023, instead of 31 December 2022, agreement was not able to be reached under the French Presidency. Vetos invoked by Poland and subsequently by Hungary thwarted agreement on the file. The Czech Republic took over the rotating Presidency on 1 July and have vowed to continue pushing for a compromise.

In the meantime, the EU Commission was anything but idle in Semester I as these ECOFIN Council discussions on the most watched EU tax file took place, most notably holding public consultations on: the proposal for a directive on the misuse of shell entities, or unshell legislation in the EU-bubble jargon; policy options for a new EU-wide system for withholding taxes; the proposal for a directive laying down rules on a debt-equity bias reduction allowance and on limiting the deductibility of interest for corporate income tax purposes ("DEBRA"); and on the future of the VAT in the digital age.

To ensure that there was no shortage of work in the tax policy arena, the OECD also held a series of public consultations on a number of the 14 building blocks which make up Pillar 1 of the two-pillar solution to tax challenges posed by the digital economy. Discussions on some technical aspects of Pillar 1 are proving more time-consuming than anticipated at the Inclusive Framework, reflected in the EU postponing the planning for publishing a proposal on the implementation of the OECD global agreement on re-allocation of taxing rights from July 2022 to the fourth quarter of 2022.

Also in Semester II, a much-anticipated EU Commission consultation on the regulation of tax advisers who are involved in tax avoidance schemes is expected to take place, as well as legislative proposals on both VAT in the Digital Age and on addressing the VAT Gap in the EU. A proposal on withholding tax relief is expected in the fourth quarter of the year, following on from the recent consultation which took place. CFE will continue to monitor these developments and actively participate in all stakeholder processes.

Contents

EU Directive on Minimum Tax

01

EU Directive on Minimum Tax – Negotiations on Implementing Legislation Stall for Summer

In January, EU Finance Ministers began their first discussions concerning the European Commission proposal for an EU directive on global minimum level of taxation for multinational groups, adopted just prior to Christmas. The Directive will implement the OECD Pillar 2 agreement into European Union law, and follows on from the publication of the OECD Pillar 2 Model, which contains detailed rules to assist governments in the implementation of the minimum 15% tax rate as of 2023.

The EU Pillar 2 Implementation Directive 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 the intra-EU level.

The implementation of the Pillar 2 Directive will affect 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.

The French Presidency of the Council of the EU was eager for the Directive to be approved as quickly as possible in Semester 1 of 2022; alas, this was not to be. During initial discussions in January, several EU finance ministers expressed certain reservations, contending the EU proposal went beyond the OECD agreed rules, to the extent it extends to domestic companies, and urged caution about the speedy adoption of Pillar 2 without concurrent adoption of Pillar 1. Initially, Malta and Estonia expressed particular reservations about the Directive, and urged Member States to delay any introduction of the new rules until the beginning of 2025, rather than 2023, as was initially planned under the Directive.

In March, significant progress was made in relation to the EU Directive on the implementation of the OECD's Pillar 2 minimum corporate income tax. A revised compromise text published ahead of the meeting revealed some notable changes from the original proposal, the most significant of which being that the time limit for transposition has been changed to 31 December 2023, instead of 31 December 2022. Under the revised compromise text, the Directive would apply for fiscal years beginning 31 December 2023, instead of from the start of 2023. The Undertaxed Payments Rule would then accordingly apply from 31 December 2024. The revised compromise text also includes a provision that Member States with no more than 10 ultimate parent entities of groups in scope of the Directive can elect not to apply the Undertaxed Payments Rule and Income Inclusion Rule until the end of 2025.

In April, Poland invoked its veto, on the basis that it is not prepared to move forward on the implementation of Pillar 2 without it being "legally tied" to the implementation of Pillar 1. Poland's Finance minister Magdalena Rzeczkowska raised concerns that if Pillar 1 fails, the global minimum tax would burden international businesses in Poland and may cut revenues. The directive was again scheduled for a vote on 24 May however the French presidency removed the item last minute faced with Poland's veto, tabling the discussion for June.

At the ECOFIN meeting on 17 June, the European Union Member states again failed to reach a political agreement. Poland lifted its veto prior to the meeting, however Hungary reversed its support for the proposal last-minute. According to the Finance Minister, Mihaly Varga, Hungary was no longer able to support the deal due to the changed economic and fiscal climate arising from the war in Ukraine as well as inflation. This justification was disputed by Bruno Le Maire, the French Finance Minister, who said that Pillar 2 would on the contrary be helpful for the EU economy. France, as Presidency of the Council, maintained that they were hopeful of a last-minute deal during their Presidency, but agreement was not able to be reached. The Czech Republic took over the EU rotating Presidency on 1 July.

Adoption of Pillar 2 is also stalled across the Atlantic, where President Biden is struggling to pass the legislation through the US Congress. Despite the House adoption of the Build Back Better Act in December 2021, the Senate remains divided on this matter. It is therefore unclear whether the bill will be passed before the November US midterm elections.

CFE Tax Advisers Europe issued an Opinion Statement on the ongoing process that seeks to enact the Pillar 2 political agreement into the legal order of the EU and other states. CFE set out its reservations on the proposed EU Directive implementing Pillar 2, principally focused on the complexity, the ambitious implementation timeline and lack of opportunity for meaningful engagement with stakeholders in developing the model rules, on which the EU directive is based.

CFE in its statement set out that it finds it problematic that subsequent iterations of the EU Compromise text as discussed by the Member states representatives refers to subsequent OECD commentary as regards rules of interpretation. As discussed in more detail in CFE's statement, recourse to OECD guidance to interpret provisions of EU law is extremely problematic for reasons of legal certainty. CFE strongly suggests the directive should establish a link with the entering into force and effective implementation of Pillar 2 by most of the jurisdictions participating to the Inclusive Framework. In the opinion of CFE Tax Advisers Europe, the proposed directive should come into force and be effectively applicable only as of the year following that in which at least 2/3 of the members of the Inclusive Framework have effectively introduced the necessary legislation so as to apply the OECD Pillar 2 rules.

The issue of the future of Member states CFC legislation is being raised with the introduction of the Income Inclusion Rule in the EU legal order. As noted by the OECD, the Income Inclusion Rule is drafted with reference to the modus operandi of CFC rules. CFE would welcome a dialogue on the interaction of the CFC rules with ATAD/ ATAD3/ Unshell proposal given the interconnection of these rules and the same underpinning objective - taxation of shareholders as if an entity did not exist. In light of the above, CFE in its statement suggested further postponement of entry into force due to the inherent complexity and ambiguity of the OECD Model Rules on Pillar 2 and the need of taxpayers, advisers and tax administrations to get acquainted with these rules before they become operational. Few countries of the Inclusive Framework have the resources to implement these rules, and certainly they could not put in place these measures in the desired timeframe.

Regulation of the Tax Adviser Profession

02

EU Plans to Regulate Tax Intermediaries

On 25 April, the European Parliament's Permanent Subcommittee on Tax Matters, FISC, held a hearing concerning regulation of the provision of tax advice across the European Union, *"How to reinforce the regulation of intermediaries to create an intermediary sector that ensures a fair and user-friendly tax system?"*. The hearing was a follow-up to a hearing held in November 2021 concerning the Pandora Papers, tax evasion and tax avoidance. Members of the Subcommittee discussed the the role of tax intermediaries in tax avoidance and tax evasion and evaluated options to improve tax intermediaries' regulatory framework to deter them from playing any part in tax abusive activities.

During the hearing, Ms Jasna Voje from DG TAXUD at the European Commission participated in the discussion, and informed attendees that a public consultation would soon be launched exploring policy options being considered by the Commission to improve tax intermediaries' regulatory framework. Ms Voje explained that the Commission have in mind not to regulate the profession in terms of qualification requirements but instead to introduce a sort of behavioural monitoring measure; that the Commission want to establish standards which intermediaries must adhere to, an instrument setting out harmonised definitions of wrong-doing across the EU, with limits and consequences, to tackle the activities of intermediaries operating in the grey-zone of providing tax advice.

It now appears however that the European Commission will not propose amendments to the existing rules on professional regulation of tax advisers, according to reports from various events and meetings held in late June. Due to the complexity and diversity of the professional regulation among EU Member states, the EU will most likely opt for addressing issues only with enablers who are involved in tax avoidance schemes with third countries. The public consultation, which is now scheduled to be published in July, will clarify the proposed solutions for addressing any outstanding issues with 'enablers of tax avoidance', but it is very likely the proposed measures would not affect the majority of tax advisers.

The hearing before the European Parliament's Permanent Subcommittee on Tax Matters in April featured interventions by the Organized Crime and Corruption Reporting Project, KPMG and CFE Tax Advisers Europe. Aleksandar Ivanovski and Brodie McIntosh gave a presentation concerning the CFE Discussion Paper on An Ethics Quality Bar for All Advisers, which sets out a proposed Ethics Quality Bar for advisers to reflect on when giving advice, questioning whether there is manipulation and artificiality in tax planning. The CFE's Professional Affairs Committee prepared this paper based on its long-standing commitment to high professional standards in tax advice and to stimulate a discussion on how to tackle this problem among all who have an interest in how our tax systems function in Europe.

CFE set out that a 'one-size-fits-all' approach in regulating tax professionals is difficult to achieve in Europe, given the regulatory culture differs significantly among European states. It is also important to recognise the significant differences between tax intermediaries. Policymakers therefore need to ensure that all intermediaries operate to high standards, which calls for a holistic policy approach.

FISC also met on 27 June 2022 to discuss a study conducted by Prof. Dr. Emer Mulligan from the National University of Ireland Galway on "The regulation of intermediaries, including tax advisors, in the EU/Member States and best practices from inside and outside the EU ". It is likely the report will help inform the policy choices of the Commission in pursuing this issue further as part of its consultation process.

EU Unshell Legislation

03

EU Proposal on the Misuse of Shell Entities

In late December 2021, 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.

The 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.

In April, CFE Tax Advisers Europe issued an Opinion Statement on the EU proposal on fighting the use of shell entities and arrangements for tax purposes (Unshell or ATAD3 proposal). CFE in the statement highlighted the potential issues in practice raised by the proposed Directive, noting that the application of the existing anti-avoidance measures within the EU has become very complex in recent years, and expressing concerns about the manner in which this draft directive intends to achieve these objectives.

CFE is of the view the proposed Directive seems to ignore the fact that transfer pricing and CFC rules already deal with the very issues that it is purporting to address. Indeed, the past few years have seen the implementation of a trove of EU and broader international measures designed to counteract certain perceived abusive practices. These include the Multi-Lateral Instrument ('MLI'), limiting access to treaty benefits (PPT), EU Mandatory Reporting (via DAC6), as well as two EU anti-tax avoidance directives ('ATAD'), comprising rules on CFCs, interest deductibility, anti-hybrid arrangements, exit taxes and general anti-avoidance. The effectiveness of these rules is yet to be fully seen. In the opinion of CFE, the proposed directive seems to assume that abusive situations persist, without having allowed these measures sufficient time to prove their relevance.

CFE in the statement suggests a different approach in respect of addressing the outstanding issues raised by shell entities:

- Introduce another iteration of the DAC directive by way of enhancing transparency between Member states and taxpayers, limiting the proposed directive to exchange of information (i.e. by removing the proposed articles 11 and 12);
- Create a list of Member states that have introduced the Principle Purpose Test (PPT) in their respective double tax treaties;
- Invite the European Commission to use the powers conferred on it by Article 258 of the Treaty on the Functioning of the EU to enforce the compliance by Member states with their obligation to prevent the avoidance of EU legislation (i.e. ATAD) and to do so in a manner that is compliant with primary EU law and settled ECJ case-law.

CFE will monitor further developments on the proposal closely in Semster II of 2022.

EU Policy – Direct Tax Update

04

EU Commission Consults on a New EU System for Withholding Taxes

In late April, the European Commission has launched a public consultation questionnaire on a new EU-wide system for withholding taxes. Input received will feed into the upcoming legislative initiative planned for adoption in Q4 of 2022, which aims to introduce a common EU-wide system for withholding tax on dividend or interest payments. The draft legislation aims to remove barriers to cross-border investment and will also include a system for the exchange of information between tax authorities. This followed after a Plenary session of the European Parliament on 10 March 2022, at which the Parliament adopted a report requesting the EU Commission put forward legislation for an EU-wide withholding tax, ensuring payments are taxed before leaving the EU, and to create a standardised framework, reducing complexity and compliance costs.

The policy options being considered by the Commission for the new legislative proposal are as follows:

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 standardised 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.

In June, CFE issued an Opinion Statement in response to the consultation, setting out its strong preference for a harmonized relief at source system and for there to be a harmonized means to obtain via e-request a tax residence certificate, with swift online provision of the tax residence certificate, and a digitalised verification system. CFE believes that the ultimate goal should be that dividends should only be taxed once in the residence state, and thus not also in the source state, the only means to truly ensure that there is no double taxation. CFE also believes such a mechanism should be extended to interest/royalty payments. CFE is of the view that there are solid public policy arguments for Option 3 (enhancing the existing administrative cooperation framework to verify entitlement to double tax convention benefits) and extending this to third countries. It would obviously benefit financial intermediaries in third countries if the benefits of any directive was extended to them, for instance through a treaty. CFE will continue to closely follow this topic.

DEBRA: New Proposed EU Rules on a Debt-Equity Bias Reduction Allowance & Limiting Deductibility of Interest for Corporate Income Tax Purposes

On 11 May 2022, the European Commission published a proposal for a directive laying down rules on a debt-equity bias reduction allowance and on limiting the deductibility of interest for corporate income tax purposes ("DEBRA"). These measures seek to equalise the tax treatment of debt and equity by way of introducing an allowance on equity.

Under the proposal, the allowance on equity shall be deductible for 10 consecutive tax periods, from the taxable base of a taxpayer for corporate income tax purposes up to 30% of the taxpayer's EBITDA. If the deductible allowance on equity is higher than the taxpayer’s net taxable income in a tax period, Member States shall ensure that the taxpayer may carry forward, without time limitation, the excess of allowance on equity to the following periods. The taxpayers may carry forward, for a maximum of 5 tax periods, the part of the allowance on equity which exceeds 30% of EBITDA in a tax period. The proposal also introduces interest deduction limitations, whereby a taxpayer would be able to deduct from its corporate taxable base the exceeding borrowing costs up to an amount corresponding to 85% of such costs incurred during the tax period.

It is widely acknowledged in academic literature that the debt-equity tax bias is highly distortive of investment decisions. Interest as a return on debt is tax planning efficient, whereas similar tax benefits are ordinarily not in place for equity investment. As a result, companies often become highly leveraged for taxation purposes, which hinders innovative investment through equity whilst piling up debt. At present tax legislation of only six EU Member states includes some form of allowance on equity. Such an allowance could retain or limit the deduction for interest expenses but would add similar benefits for the normal return on equity.

The initial EU Commission inception impact assessment operated with the following options:

- Disallowing the deductibility of interest payments, or creating an allowance for equity (ACE) by enabling the tax deductibility of notional interest for equity;
- Introducing allowance for a notional interest deduction on all corporate equity, new corporate equity or corporate capital (equity and debt).

Commenting, EU Commission Vice-President Valdis Dombrovskis, said: “*Europe's companies should be able to choose the financing source that is best for their growth and business model. By making new equity tax-deductible, just as debt is at present, this proposal reduces the incentive to add to their borrowing and allows them to make financing decisions based on commercial considerations alone. As part of the EU's agenda to ensure a fair and efficient tax system, it will make financing more accessible for EU businesses, particularly start-ups and SMEs, and help to create a genuine single market for capital. This will be important for the green and digital transitions, which require new investments in innovative technologies that could be funded by increased equity*.”

A public consultation concerning the proposal was launched by the EU Commission, and feedback can be submitted until 29 July 2022. CFE is preparing an opinion statement for publication concerning the proposed directive.

Green Taxes: EU Targets Portion of Carbon Tax Revenues & OECD Pillar 1 to Finance Post-Pandemic Recovery

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.

EU Parliament & Council Reach Deal on Rules for Tracing Crypto-Assets

In late June, European Parliament and Council reached a provisional deal on legislation forming part of the 2021 EU anti-money laundering package that aims to ensure that transfers of crypto-assets can be traced in the same way as traditional money transfers. Under the legislation, the "travel rule" will now apply to crypto-assets, such that information on the source of an asset and its beneficiary is sent with a transaction and stored. Crypto-assets service providers will also be obliged to provide this information to competent authorities if an investigation is conducted into money laundering and terrorist financing.

Co-rapporteur on the file, MEP Ernest Urtasun, said of the agreement: *"This new regulation strengthens the European framework to fight money-laundering, reduces the risks of fraud and makes crypto-asset transactions more secure. The EU travel rule will ensure that CASPs can prevent and detect sanctioned addresses and that transfers of crypto-assets are fully traceable.This regulation introduces one of the most ambitious travel rules for transfers of crypto assets in the world. We hope* *other jurisdictions will follow the ambitious and rigorous approach the co-legislators agreed today."*

In April, the European Parliament voted on the legislation during their April plenary session, and confirmed the ECON and LIBE Committee decision to enter into interinstitutional negotiations with the EU Council. Parliament were successful in negotiating the removal from the draft legislation any minimum thresholds and exemptions for low-value transfers. They also called on the European Banking Authority to create a public register of businesses and services involved in crypto-assets that may have a high risk of money-laundering, terrorist financing and other criminal activities, including a non-exhaustive list of non-compliant providers.

AML: New FATF Anti-Money Laundering Standards

In March, the Financial Action Task Force (FATF) updated its Recommendations to add new definitions of "nominator" and "nominee shareholder or director", to strengthen the standards on beneficial ownership of legal persons, and recommended governments set up beneficial ownership registers where this is not already in place. These measures would reportedly be of use in identifying assets targeted by sanctions introduced by the international community following the Russian invasion of Ukraine. Other changes to the FATF Recommendations include:

- Combating the financing of the proliferation of weapons of mass destruction through the consistent implementation of targeted financial sanctions when these are called for by the UN Security Council.
- Improved transparency to make it harder for criminals and terrorists to conceal their identities or hide their assets behind legal persons and arrangements.
- Stronger requirements when dealing with politically exposed persons (PEPs).
- Expanding the scope of money laundering predicate offences by including tax crimes.
- An enhanced risk-based approach which enables countries and the private sector to apply their resources more efficiently by focusing on higher risk areas.
- More effective international cooperation including exchange of information between relevant authorities, conduct of joint investigations, and tracing, freezing and confiscation of illegal assets.
- Better operational tools and a wider range of techniques and powers, both for the financial intelligence units, and for law enforcement to investigate and prosecute money laundering and terrorist financing.

FATF is the global standard-setter for measures to combat money laundering, terrorist financing, and financing of proliferation. It is an intergovernmental organisation with 36 members and with the participation of over 180 countries through its global network.

EU Policy - Indirect Tax Update

05

EU Commission Consultation on "VAT in the Digital Age"

In early January, the European Commission published a call for evidence for an impact assessment, and simultaneously launched a public consultation on the future of the VAT in the digital age. The Commission Action Plan for 2022 envisages that 'VAT in the digital age' legislation will be published, which will cover:

- VAT reporting obligations and e-invoicing
- VAT treatment of the platform economy
- Single EU VAT registration.

According to the Commission, for digital reporting requirements, costs linked to the introduction of new reporting obligations are expected, but the reduction of 'fragmentation costs' related to differences in jurisdictions' data reporting requirements would benefit all businesses. This will require the highest level of new IT investments and may require a longer implementation period. Depending on the level of centralisation of the IT infrastructure to be built, implementation may run until 2030. However, Member States investing in their IT would benefit from a more efficient tool to fight against fraud and make good use of the data to provide better services to taxpayers. This would be a game changer in the fight against fraud, the Commission contends.

On 5 May 2022, CFE Tax Advisers Europe issued an Opinion Statement on the EU VAT in the Digital Age Consultation. CFE welcomed the work of the European Commission in seeking to review the appropriateness of current VAT rules in the EU in light of changes brought about by digitalisation of the economy, and set out that it is very concerned that the introduction of non-harmonised digital reporting requirements and e-invoicing is effectively fragmenting the single market. While the CFE does not consider that Member States should be required to implement such requirements, if they do decide to do so the CFE considers that it is highly desirable that the systems should be implemented in so far as possible in a harmonised manner. They should also be implemented in a manner that seeks to minimise the burdens on businesses and in particular SMEs, since such requirements can be particularly burdensome for them.

CFE also stressed in the statement that for reporting requirements to effectively address VAT fraud, they must be balanced against taxpayers' rights. Many taxpayers are wary of Member States goldplating any requirements, and requiring even further evidence than may be necessary under any common rules adopted, and being pursued unfairly by overly zealous tax authorities. CFE believes that the risks to taxpayers' rights could be balanced by ensuring that taxpayers have full access to the data which can be viewed by the tax authorities.

While CFE Tax Advisers Europe can see that there may be sectors where it is reasonable to have a presumption that everyone using a platform to sell goods and services is acting as a taxable person, it does have concerns about how far such presumptions should be taken. There are obvious issues as to input tax recovery and how to define this at an EU-level, as to who should recover input tax and to what extent. It is appropriate to have a rule governing this, but CFE is of the view that if one is considered a taxable person, one should have the right of recovery of input VAT. The volume of VAT registrations which may flow from such a rule should also be considered, in terms of compliance and oversight burdens for tax administrations.

CFE is also of the view that the OSS should be extended to supplies with installation with the final consumer and in chain supplies where extending it would be desirable. CFE is of the view that the IOSS should also be extended as the current financial threshold significantly limits the utility of the system. We also consider that there would be merit in extending the OSS to business to business supplies in cases where VAT is not accounted for using the reverse charge under Article 194 of the Directive.

The CFE also believes there ought to be a facilitation scheme available for supplies of greater value, although this would of course need to include customs requirements when the value of goods is over 150 Euro. However, CFE considers that it would be ideal if the system could incorporate both purposes, both customs and VAT requirements. CFE is of the view that this will benefit SMEs given the cost of compliance versus the volume of sales.

A legislative proposal concerning VAT in the Digital Age is expected later this year and CFE will participate in the further stakeholder consultation processes at that stage.

EU Extends VAT Reverse Charge Mechanism as Definitive VAT Regime Negotiations Continue

The European Commission in the first semester of 2022 also extended the application of the optional reverse charge mechanism in relation to supplies of certain goods and services susceptible to fraud and of the Quick Reaction Mechanism against VAT fraud. The Directive extends the application of the mechanism until the end of 2055.

The Explanatory Memorandum to the Directive notes that negotiations in the Council concerning the definitive VAT system are ongoing, and that it will not be possible for the system to enter into force by July 2022, and that an extension until the end of 2055 was required to allow for the negotiations and to prolong the anti-fraud measures.

The European Parliament also adopted a resolution concerning the EU VAT Gap, noting that progress to reduce the VAT Gap in the EU reversed in 2020 and that additional challenges have been posed by the exponential growth of e-commerce since the corona pandemic began, demanding new strategic policy options now be adopted.

The Parliament in the resolution noted that failure at the EU Council level to agree on the proposed definitive VAT regime "is delaying important decisions on adapting VAT for the challenges we will face during the EU's economy recovery and whereas the absence of action means loopholes that could allow the VAT gap to grow have not been closed".

The Parliament in the resolution called for a range of legislative action to be taken by the Commission and by the EU Council to progress reaching solutions fit for the issues posed by VAT fraud to the EU economy. A proposal on this is anticipated from the Commission later in 2022.

EU Blacklist & Code of Conduct Update

06

EU Council Updates 'Blacklist' of Non-Cooperative Jurisdictions

On 24 February the Council of the EU, sitting as ECOFIN, reviewed its List of Non-Cooperative Jurisdictions for Tax Purposes ("Blacklist"). No jurisdictions were added to the list during the review. The Blacklist is reviewed twice per year, and will next be reviewed in October 2022.

The following jurisdictions remain on the Blacklist: American Samoa, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands and Vanuatu. The state of play in Annex II of the Blacklist also details steps taken by various jurisdictions to undertake reforms in order to comply with tax good governance standards. More detail on this can be found in the Code of Conduct (Business Taxation) report to the Council of the EU.

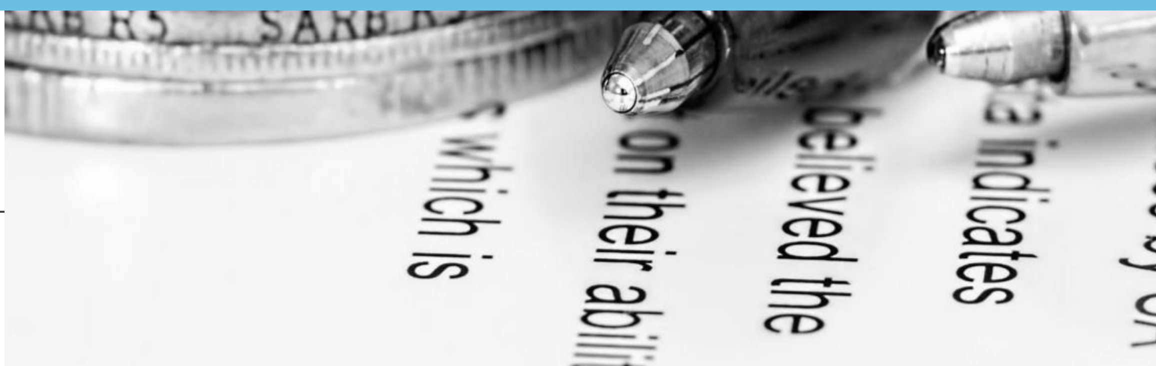
Updates to the list in late 2021 were called 'grotesque' by some European Parliament members and other critics, in light of the Pandora Papers revelations on the role of certain off-shore jurisdictions. The EU Parliament renewed criticism of the EU Blacklist following the publication of the Pandora Papers, adopting a Resolution at its plenary session in Strasbourg on 6 October 2021 calling 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.

The Council of the EU's Code of Conduct Group on Business Taxation work programme for the first semester of 2022 during the French Presidency of the Council of the European Union prioritised: 1) Monitoring of standstill and the implementation of rollback; 2) Monitoring the implementation of agreed guidance; 3) Links with third countries. Under the third aspect of the work programme, the Group continued to monitor third country jurisdictions and updated the EU list of non-cooperative jurisdictions for tax purposes.

In addition, the Group worked on the coordination of defensive measures towards non-cooperative jurisdictions, the future criterion on the exchange of beneficial ownership information, follow-up actions to the Pandora Papers, as well as reviewing possible impacts of the international agreement that was reached on a minimum effective taxation (OECD Pillar 2) on its work, including on the EU listing criteria.

International Tax Policy Updates

08



OECD Developments: Public Consultations on Pillar 1 Draft Rules & GloBE Model Rules Guidance & Framework

In February, the OECD hosted a Tax Talks webinar concerning recent and upcoming developments in the OECD's international tax agenda, the first update of its kind in almost a year, particularly focusing on updates on the two-pillar solution to tax challenges posed by the digital economy.

During the introduction to the Tax Talks update, Director of the Centre for Tax Policy and Administration at the OECD, Mr Pascal Saint-Amans informed attendees that consultations would be launched in the coming months on the 14 building blocks which make up Pillar 1, namely:

- Revenue Sourcing & Nexus
- Tax Base
- Scope Test
- Exclusions - Extractives
- Exclusions - Regulated Financial Services
- Tax Certainty for Amount A
- Tax Certainty for Issues Related to Amount A
- Elimination of Double Tax
- Marketing and Distribution Profits
- Safe Harbour
- Withholding Taxes
- Administration
- Segmentation
- Unilateral Measures

Members of the Inclusive Framework aimed to agree a multilateral convention by mid-2022, but this proved impossible. Over the course of the first six months of year, consultations were held concerning Revenue Sourcing & Nexus, Tax Base, Scope Test, Exclusions – Extractives, Exclusions - Regulated Financial Services, Tax Certainty for Amount A and Tax Certainty for Issues Related to Amount A. Further consultations will follow in the second half of 2022.

The revenue sourcing rules will allow in-scope MNEs to identify the relevant market jurisdictions from which revenue is derived, and to apply the revenue-based allocation key. Under the OECD agreement reached in October 2021, revenue is sourced to the end market jurisdictions where goods or services are used or consumed. The consultation document notes that *"input will be most helpful where it explains the additional guidance that would be needed to apply the rules to the circumstances of a particular type of business, as well as input on whether anything is missing or incomplete in the rules"*.

The purpose of the tax base determinations rules is to establish the profit (or loss) of an in-scope MNE that will be used for the Amount A calculations to reallocate a portion of its profits to market jurisdictions. The rules determine that profit (or loss) will be calculated on the basis of the consolidated group financial accounts, while making a limited number of book-to-tax adjustments. The rules also include provisions for the carry-forward of losses.

As to Draft Model Rules for Domestic Legislation on Scope under Amount A of Pillar One, the consultation states that *"the purpose of the scope rules is to determine whether a Group will be in scope of Amount A. The rules are designed to ensure Amount A only applies to large and highly profitable Groups and have been drafted to apply in a quantitative manner, such that they are readily administrable and provide certainty as to whether a taxpayer is within scope. The Draft Rules for the Exclusions for Extractives and Regulated Financial Services will be released for public consultation at a later date."*

The consultation document on the Financial Services Exclusion sets out that:

The Regulated Financial Services Exclusion will exclude from the scope of Amount A the revenues and profits from Regulated Financial Institutions. The defining character of this sector is that it is subject to a unique form of regulation, in the form of capital adequacy requirements, that reflect the risks taken on and borne by the firm. It is this regulatory driver that generally helps to align the location of profits with the market. The scope of the exclusion derives from that requirement, meaning that Entities that are subject to risk-based capital measures (and only those) are excluded from Amount A.

There are six types of Regulated Financial Institution defined in this document: Depositary Institution; Mortgage Institution; Investment Institution; Insurance Institution; Asset Manager; a Mixed Financial Institution. A seventh category is added, for a limited type of service entity that exclusively performs functions for a Regulated Financial Institution (RFI Service Entity). The definition for each type of Regulated Financial Institution generally contains three elements, all of which must be satisfied: a licensing requirement; a regulatory capital requirement; and an activities requirement. These conditions recognise the uniquely regulated nature of financial services. Where the conditions are met, the revenues and profits of the Entity are wholly excluded from Amount A.

However, commentators should note that this does not reflect the final or consensus views of the Inclusive Framework and that some members hold the view that reinsurance and asset management ought not to be excluded from Amount A.

In March, the OECD also published a detailed technical Commentary and Illustrative Examples setting out guidance on the operation and intended outcomes of the Global Anti-Base Erosion Rules. Also as part of the OECD two-pillar solution to reform the international tax framework in response to the challenges of digitalisation of the economy, the OECD held a consultation and public meeting on developing the Implementation Framework needed for the Detailed Implementation Plan.

OECD Public Consultation on a Crypto-Asset Reporting Framework

In March, the OECD published a public consultation document concerning amendments to the Common Reporting Standard (CRS) and a new global tax transparency framework to provide for the reporting and exchange of information with respect to crypto-assets. According to the OECD, the new framework will cover the collection and exchange of tax-relevant information between tax administrations, with respect to persons engaging in crypto-transactions. It is proposed that individuals and entities that provide services to exchange crypto-assets against other crypto-assets apply the due diligence procedures to identify their customers, and then report the aggregate values of the exchanges and transfers for such customers on an annual basis to revenue administrations.

Thereafter, the OECD held a hybrid public consultation meeting on 23 May 2022 concerning its consultation process on establishing a Crypto-Asset Reporting Framework & Amendments to the Common Reporting Standard. The meeting focused on the questions in the consultation document and the issues identified in the written input provided by interested parties as part of the consultation process.

On 29 April 2022, CFE issued an Opinion Statement on the OECD public consultation on a Crypto-Asset Reporting Framework and Amendments to the Common Reporting Standard. CFE recognises the need to understand and meet the challenges presented by the crypto revolution. For this reason we are supportive of the OECD efforts to establish global transparency but are of the view there is a clear need to focus on how this framework is implemented. CFE is concerned about the scope and nexus rules of the framework, and believes a tax framework for e-assets should be developed prior to a system for exchange of information.

CFE is of the view that existing tax legislation establishes canons of taxation that have the capacity to deal with crypto assets and that what is needed is convertability which enables ready adaptation. Acccordingly it should be no surprise that in our view amendment to the Common Reporting Standard (CRS) is a necessary precursor for this to happen and we are wholly supportive of the OECD proposals in this respect. We are not sure, at this stage, that the proposal for the development of a CARF, which underlies this consultation, has the necessary structural foundations to enable implementation and, therefore, risks substantial untargeted and unmatched overreporting if introduced in haste.

Release of an early CARF, which we think will not be globally accepted, will act as a disincentive for the economic and prosperous development of the sector in mature tax environments. It will act as a driver for crypto activity to develop in countries which make clear their intention not to introduce regulation and reporting in accord with a CARF.

CFE wonder whether a country by country implementation is necessarily the way to progress and think it far too early to form a view one way or another. That said, we reiterate our support both for a clear enunciation of a global taxation framework which includes crypto-assets, signposted by the Common Reporting Standard, and further research into what a Crypto Asset Reporting Framework which has global connectivity and matched reporting could look like.

CFE welcomes the work of the OECD in seeking to establish a crypto-asset reporting framework and exchange of information in this field in light of the development of new financial technologies, and will participate in any further stakeholder consultation processes.

Forum on Tax Administration: Inventory of Tax Technology Initiatives

The OECD's Forum on Tax Administration has published an Inventory of Tax Technology Initiatives. The inventory contains information on digital solutions implemented by 76 tax administration through the world. The inventory will be expanded in the future to include case studies and links to supporting materials, in order to provide developing countries with a one-stop-shop on digitalisation initiatives in tax administration.

Director of the OECD Centre for Tax Policy and Administration, Pascal Saint-Amans, said of the new initiative: *"This new web-based inventory, developed in a unique global collaboration, is an important tool for tax administrations globally, helping to identify opportunities for significantly reducing both tax gaps and administrative burdens. It is underpinned by the recently published Digital Transformation Maturity Model which allows administrations to understand their current level of digital development and supports the further development of digitalisation and digital transformation strategies."*

OECD to Establish New Inclusive Framework on Carbon Pricing

During the OECD's Tax Talks webinar on 21 February, Pascal Saint-Amans, Director of the Centre for Tax Policy and Administration at the OECD, announced that the OECD is launching a new inclusive framework on carbon pricing. This framework will address variety of issues, some of which were touched on in the policy paper released recently on the topic of decarbonising the economy by the OECD.

Mr Saint-Amans noted that a further Tax Talks Webinar will be held in the near future concerning the new inclusive framework and the particular focus of work it will undertake.

State Aid & Case Law Updates

09

ECJ Decision on Spanish Obligation to Provide Tax Information: *Commission v Spain* – C788/19

In February, the European Court of Justice handed down its decision in case C-788/19 *Commission v Spain* (Form 720), on the lack of proportionality of the consequences derived from the failure to provide information concerning assets or rights held in other Member States of the European Union or the EEA. The case was referred to the ECJ by the European Commission, which had commenced infringement proceedings against Spain in February 2017 after receiving a large number of complaints by taxpayers in relation to the legislation. In May, the CFE ECJ TaskForce issued an Opinion Statement concerning this decision.

In its decision, the Court held that the Kingdom of Spain had failed to fulfil its obligations under articles 63 TFEU and 40 of the EEA Agreement by imposing disproportionate measures on the failure to duly comply with the obligation to provide information concerning assets and rights located abroad. The Spanish legislation provided for very serious economic consequences, such as the taxation of the value of not duly declared assets and rights as unjustified capital gains with no statute of limitations period. The legislation also provided for a proportional fine of 150% of the tax calculated on amounts corresponding to the value of those assets or those rights, which could be applied concurrently with flat-rate fines. At the same time, such flat-rate fines were much higher than the penalties imposed in respect of similar infringements in a purely national context, not being capped by any amount. *Commission v. Spain* is an important case as it addresses a number of relevant issues regarding the limits that the Member States must respect when implementing measures to counteract international tax avoidance and evasion.

Proportionality plays an important role in ensuring the compatibility of the measures designed by the Member States to counteract tax evasion and abuse, and in particular, its scope, extent, consequences and intensity. However, a more precise analysis of the proportionality principle would require one to distinguish the reaction against those situations that can be considered tax evasion from those that can only imply abuse of rights or tax avoidance instead of taking an overall approach and analysis.

This is an important case for the recognition of rights derived from the EU fundamental freedoms limiting the discretionary and broad exercise of taxing powers by the Member States to counteract potential tax evasion and abuse. The CFE stresses the need to ensure the effectiveness of the rights enshrined by the TFEU and the EEA Agreements, by promoting decisions within a shorter period of time and by reinforcing the access to domestic remedies available to restore the primacy of EU Law in infringements by the Member States. Limitation periods, restrictions, and legal constraints under domestic legislation to use available remedies may hamper the aphorism *ubi ius ibi remedium*.

It is justified to guarantee the effectiveness of tax controls and to provide tax administrations with the necessary legal mechanisms to combat tax evasion and abuse, but this must be done with full respect for the fundamental rights and freedoms of taxpayers.

Spain was ordered to pay the Commission's costs in bringing the application, and must now amend its legislation in line with the ECJ decision.

AG Opinion in Belgian DAC6 Legal Privilege Challenge Case: C-694/20 – *Orde van Vlaamse Balies*

The Advocate General Opinion in Case C-694/20 *Orde van Vlaamse Balies,* concerning whether or not the obligations under the Directive on Administrative Cooperation infringes upon the right to privacy and the right to a fair trial under Articles 7 and 47 of the Charter of Fundamental Rights of the European Union, respectively, was handed down on 5 April 2022.

The Advocate General Rantos in his opinion held that the requirement to notify another intermediary of the reporting obligations does not form part of any legal proceedings and therefore does not constitute a breach of the right to a fair trial. In relation to the right to privacy, AG Rantos held that should the identity of the intermediary be made known in fulfilment of the reporting requirement, this could constitute a breach of the right, but that the breach would not occur should the name of the intermediary not be disclosed.

AG Rantos accordingly concluded in his Opinion that the ECJ should hold that Article 8ab(5) of DAC6, by requiring a lawyer who acts as an intermediary and who, by relying on his professional secrecy, has a declaration waiver to notify without delay to another intermediary the reporting obligations incumbent upon it under paragraph 6 of this Article, does not infringe upon the right to respect for private life guaranteed by Article 7 of the Charter of Fundamental Rights of the European Union, provided that that the name of this lawyer is not disclosed to the tax authorities in the context of the performance of the obligation to declare provided for in Article 8bisb, paragraph 9, second subparagraph, and paragraph 14, of that Directive.

The decision of the Court is expected in the coming months.

Court of Justice of the European Union Decision on Disclosure of Information in *Airbnb* Case C-974/20

The Court of Justice of the European Union has handed down its decision in case C-974/20 *Airbnb Ireland UC vs Région de Bruxelles-Capitale* concerning the sharing of customers' details with Brussels' regional authorities, which would enable tax authorities to be able to identify individuals who owe regional taxes on accommodation used for tourism purposes, finding this requirement does not contravene the prohibition in Article 56 of the TFEU.

The Court held in its ruling that:

1. *A provision of the tax legislation of a Member State requiring intermediaries, in respect of tourist accommodation establishments that are located in a region of that Member State and for which they act as intermediary or carry on a promotion strategy, to provide the regional tax authorities, on the latter's written request, with the particulars of the operator and the details of the tourist accommodation establishments, as well as the number of overnight stays and of accommodation units operated during the past year, must be regarded as being indissociable, as regards its nature, from the legislation of which it forms part and, accordingly, falls within*

the 'field of taxation' which is expressly excluded from the scope of Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market ('Directive on electronic commerce').

2. *Legislation which imposes an obligation on providers of property intermediation services, irrespective of their place of establishment and the manner in which they mediate, in respect of tourist accommodation establishments that are located in a region of the Member State concerned and for which they act as intermediary or carry on a promotion strategy, to provide the regional tax authorities, on the latter's written request, with the particulars of the operator and the details of the tourist accommodation establishments, as well as the number of overnight stays and of accommodation units operated during the past year, does not contravene the prohibition laid down in Article 56 TFEU.*

EU Tax Policy Report

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