EU Direct Tax Newsalert

European Commission presents EU Anti-Tax Avoidance Package

PwC's EU Direct Tax Group

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On 28 January 2016, the EU Commission (EC) presented its EU "Anti-Tax Avoidance Package (ATAP)", which consists of 7 parts:

- A proposed Anti-Tax Avoidance Directive ("draft ATA Directive");
- An EC Recommendation on the implementation of G20/OECD BEPS recommendations on tax treaty abuse and on permanent establishments (PEs);
- A proposed amendment to Directive 2011/16/EU on mandatory automatic exchange of information (AEOI) in the field of taxation to enable coordinated implementation of G20/OECD BEPS country-by-country reporting (CBCR) requirements;
- A general policy Communication on the ATAP and proposed way forward;
- A general policy Communication on an EU external strategy for effective taxation;
- An EC Staff Working Document; and
- A Study on Aggressive Tax Planning.

The **draft ATA Directive** addresses 6 international and BEPS-related elements of the Common Consolidated Corporate Tax Base (CCCTB), which have been discussed by the EC, Member States and stakeholders since the EC issued its 2011 CCCTB proposal. (NB: The EC still intends to issue a new two-step CCCTB draft Directive in the 4th quarter of 2016.) The draft ATA Directive largely reflects the Luxembourg EU Council Presidency Working Paper of 15 December 2015. The base erosion and profit shifting (BEPS) risks arising from several different areas are also picked up in response to the OECD BEPS project including hybrid mismatches, interest deductions and CFCs. Many of these rules reflect the proposals arising from the OECD's BEPS deliverables, however there are some areas where the rules in the draft ATA Directive differ from the corresponding BEPS proposals. The draft ATA Directive also includes rules on additional areas, such as exit taxation and a minimum level of taxation of third country income, which were not included in the OECD BEPS project. The draft ATA Directive stipulates minimum standards to be enacted; it does not prohibit other anti-avoidance rules designed to give greater protection to the corporate tax base.

Key provisions in draft ATA Directive:

- Deductibility of interest: A rule restricting net borrowing costs to the higher of EUR 1m or 30% of the taxpayer's EBITDA. There is also suggested wording for a group carve out, which differs from the potential group ratio rule suggested in OECD Action 4. There is a (temporary) exclusion for financial undertakings;
- Rules for exit taxation where a taxpayer transfers assets (between a head office and its PE, or between PEs) out of a Member State to another Member State or to a third country, or transfers its tax residence to another Member State or to a third country, or transfers its PE out of a Member State;
- A "switch-over" clause to ensure taxation of dividends and capital gains in respect of companies in a low tax third country. This clause also applies to low taxed PE profits from third countries. The test for 'low tax' has been set at 40% of the statutory tax rate in the Member State of the taxpayer (i.e. the company disposing of the shares/ receiving the distribution/holding the branch);
- A general anti-abuse rule (GAAR) allowing tax authorities to ignore arrangements where the essential purpose is to obtain a tax advantage that defeats the object or purpose of the tax provision and where the arrangements are not regarded as genuine;
- CFC rules dealing with entities subject to a low level of taxation (40% of the parent's effective rate) where more than 50% of the entity's income falls within specified categories (broadly, passive income). Where the CFC is resident in the EU/EEA, the rules only apply if the entity's establishment is wholly artificial or the entity engages in non-genuine arrangements with the essential purpose of obtaining a tax advantage;
- Rules addressing mismatches between Member States arising due to hybrid entities or hybrid instruments, whereby the characterization of the entity or instrument in the Member State where the payment has its source is followed by the other Member State which is involved in the mismatch.

To be adopted, the Directive requires unanimity in ECOFIN of all Member States. We understand that it is still an open question for Member States whether the draft ATA Directive should be negotiated in Council as an integral package or could be dealt with in separate parts, as was done with the EU Parent-Subsidiary Directive, i.e. some provisions could be fast-tracked and become effective quicker than others. Given the political momentum around BEPS and pressure on the EC on this dossier, the EC will aim to have the Directive adopted within the next 6 months so it might come into effect on 1 January or 1 July 2017, although this seems ambitious.

The EC furthermore issued a **Recommendation on implementation of measures to tackle tax treaty abuse.** The EC Recommendation urges Member States to implement the OECD BEPS proposals to address tax treaty abuse. Where Member States include in tax treaties a GAAR based on a principal purpose test (PPT) as suggested in the OECD's final report on BEPS Action 6 (Prevention of Treaty Abuse), the EC recommends that the rule should be modified to comply with EU case law such that genuine economic activity is not affected. Member States are also encouraged to amend treaty definitions of permanent establishment to reflect the OECD's proposed amendments to Article 5 of the OECD Model Tax Convention as set out in the OECD's final report on BEPS Action 7 (preventing the artificial avoidance of PE status). Member States are required to inform the EC on the measures taken to comply with the Recommendation, and the EC will publish a report on the application of the Recommendation within 3 years of its adoption.

Thirdly, the **EC proposes coordinated implementation within the EU of OECD BEPS Action 13 CBCR requirements** by extending the scope of the recently amended EU Directive on mandatory AEOI / tax rulings and advance pricing agreements (APAs) amongst EU tax administrations. We understand that since most of the EU Member States are also OECD members and have already approved and committed to implementing BEPS Action 13, this amendment could be adopted in Council within weeks, that is, if Member States do not raise any new technical issues. The Directive would enter into effect on 1 January 2017. NB: the EC will still issue a proposal and Impact Assessment for CBCR with public disclosure in spring 2016.

Fourthly, **in the general policy Communication the EC explains the rationale behind the ATAP**. The EC notes that the majority of businesses do not engage in aggressive tax planning and suffer a competitive disadvantage to those that do, in particular SMEs. The EC adds that Member States suffer significant revenue loss from this.

The EC hails the BEPS project but states the EU can and should go further to ensure that Member States develop a 'common standard' and level-playing field by implementing the ATAP in a coordinated manner, and with CCCTB clearly as the preferred holistic solution to profit shifting, transparency and effective corporate taxation in the EU. The EC claims to be on track to adopt the new CCCTB legislative proposal in autumn 2016. To placate business concerns, the EC states that the measures included in the ATAP have been designed so as to minimise the risk of double taxation and disputes. 'as much as possible'. The EC recalls that its work on an impact assessment on dispute resolution is progressing, with a view to presenting a new proposal in the summer.

Fifthly, the **Communication on an EU external strategy for effective taxation** sets out the EC's ideas for promoting tax good governance with non-EU countries, e.g. through a special clause in trade agreements, and assistance to developing countries on tax matters. Most importantly, the EC wants a common EU system for assessing, screening and listing third countries. The Communication does not, however, address the counteraction to be taken against listed countries. An update of the EC's controversial June 2015 list of non-EU country non-cooperative tax jurisdictions is published online in an interactive map.

Sixthly, the EC published a **new study on aggressive tax planning** (ATP) which it commissioned in order to identify indicators which facilitate ATP, and then reviews the corporate income tax systems of Member States against the ATP indicators, in order to identify tax rules and practices that result in Member States being vulnerable to ATP. Written by independent advisors and national tax experts, the study does not necessarily reflect the official opinion of the EC.

The study draws out the following general observations:

- results imply that scope exists for Member States to tighten their anti-abuse rules in order to counter base erosion by means of financing costs;
- nearly half (13) of Member States did not apply any beneficial owner test when accepting a claim for a reduction or exemption of withholding tax;
- half of Member States do not have CFC rules; and
- very few Member State have rules to counter the mismatching tax qualification of a local partnership or company by another state (typically the state of the owners); and
- although most (26) Member States have general or specific anti-avoidance rules, the study notes that it appears that the rules in place can be only partially efficient to prevent ATP structures.

Lastly, an **EC Staff Working Document accompanies the ATAP and is used to underpin the EC's economic and academic analysis** on the drivers and most common mechanisms which are linked to aggressive tax planning. The annex to this EC document also includes an overview of the 15 OECD BEPS Actions and corresponding EU actions.

More context and analysis will be provided in our forthcoming PwC Tax Policy Bulletin.