The Commission re-launches its initiative for a CCCTB

IFA Belgium

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A shift in priorities?

- International taxation is facing **critical challenges**
- **Technological advancement** (in particular, the digital world in communications) gradually:
  - (i) led to globally integrated markets; &
  - (ii) changed multinational business models.
- The **crisis highlighted weaknesses** of the new normal and **questioned the functioning of certain fundamental principles** in international taxation.

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Way Ahead

- **Solution to the new stakes** should not result in building walls to protect our tax territory from erosion
- Need for action to **rectify** situations **where taxpayers did not pay their fair share of tax**
- Need for constant **support** and legitimate facilitation to the **business**

Tax Transparency

- Automatic exchange of info re financial account information (DAC 2 – Dec. 2014);
- Mandatory automatic exchange of info re cross-border tax rulings (DAC 3 – Dec. 2015);
- CbCR amongst tax authorities (DAC 4 – May 2016);
- Proposal for public CbCR (April 2016 - pending);
- Access to anti-money laundering info by tax authorities (DAC 5 – Nov. 2016);
- BEPS 12 – Intermediaries & Advisors involved in potentially ATP schemes – Public Consultation (ongoing).

Fair, Competitive & Stable Corporate Tax System

- Action Plan to modernise corporate taxation (2015);
- Anti-Tax Avoidance Directive (adopted – July 2016);
- Proposals for re-launching the C(C)CTB (Oct. 2016);
- Proposal on hybrid mismatches (ATAD 2 – Oct. 2016);
- Proposal for a Double Taxation Dispute Resolution Mechanism (Oct. 2016);
- EU list of non-cooperative jurisdictions for tax purposes – Criteria and Process (by end of 2017).

Re-launched Proposals for a Common Tax Base

{COM(2016) 685 final}

&

a Common Consolidated Corporate Tax Base

{COM(2016) 683 final}

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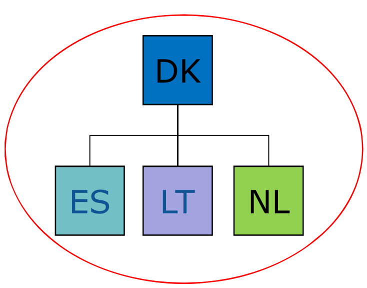
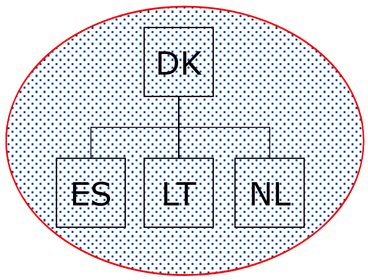
Calculation of the individual tax bases



ES, LT, NL and DK calculate their taxable revenues individually under the rules for a common tax base.

Consolidation Exercise



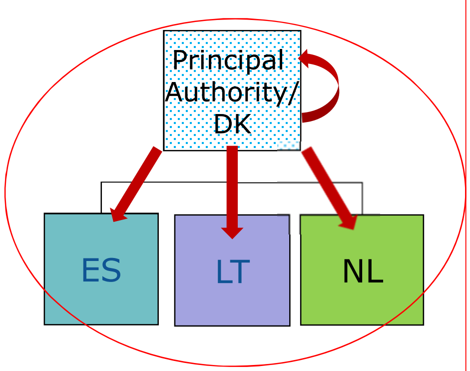
All results are added up together by DK (principal tax authority) to create a consolidated tax base for the group in the EU;

Loss-making results of one company are automatically set off against the taxable profits of others in the same group;

Tax return in one MS ('one-stop-shop');

No transfer pricing formalities within the group

Apportionment of the Consolidated Tax Base



DK, as principal authority, applies the formula to distribute the consolidated tax base across the group;

Taxable revenues are allocated to each company of the group based on the weight of the three factors: assets, labour (1/2 personnel & 1/2 payroll) and sales by destination;

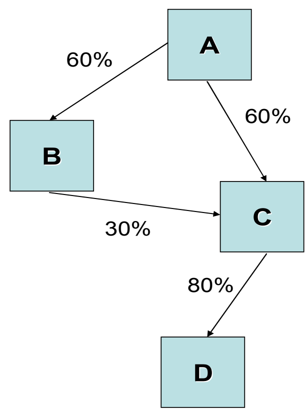
MS are free to set tax rates on their taxable shares individually.

Structure of Tax Base - Overview

- **Revenues**
  less
- **Exempt revenues**
- **Deductible expenses**
- **Deductions for depreciation**
- **Allowance for growth and investment (AGI)**
- **Non-deductible items – exhaustive list**
- **Limitation to the deductibility of interest**
- **Expenditure incurred for the benefit of shareholders in closed-end companies**

Consolidation (i) – Tests for Consolidation

- There is a **2-part test** for consolidation (Art. 5(1)) based on:
  - **Control** (more than 50% of voting rights) &
  - **Ownership or entitlement to profits** (more than 75% of capital or profit)
- Indirect participation (Art. 5(2)):
  - **Voting-right threshold**, if reached, counts for 100%;
  - **Capital holding or entitlement to profit** are calculated by multiplying at each tier.
- Intra-group transactions **shall not give rise to a profit/loss** for tax purposes (Art. 9).
- Absence of withholding taxes and source taxation within the group (Art. 10).



Consolidation (ii)

- Outcome of **adding up together the tax bases of all** group members:
  - ❖ The tax base is the result of **adjusting a company's P&L account to the common tax rules** - There is no Tax B/S.
  - ❖ Consolidation is effectively the **sum of the tax profits/losses** of all group members.
- **Intra-group** transactions:
  - ❖ No tax profit or loss - ignored.
  - ❖ No transfer pricing adjustments apply within the group (Art. 9).
- Member States may **adjust their share** where the **Directive explicitly permits** (pre-CCCTB losses) – Art. 44.

Formulary Apportionment

- A **formula** is used for apportioning a tax share to each group member (Art. 28-44).
- 3 equally-weighted factors (**Labour, Assets & Sales**);
- Safeguard clause (Art. 29);
- Treatment of intangibles;
- Sector-specific formulae for:
  (i) Financial Institutions (Art. 40);
  (ii) Insurance Undertakings (Art. 41);
  (iii) Oil and Gas (Art. 42); &
  (iv) Shipping, Inland Waterways Transport & Air Transport (Art. 43).

What is new since 2011?

- **Staged approach** outlined in 2 steps
- **Mandatory scope** for companies with a consolidated financial group revenue of more than EUR 750 million
- **ATAD/ATAD 2:** agreed anti-tax avoidance elements & the switchover clause feature in the framework of the common tax base with the necessary adjustments
- **Specific new elements**
- **Technical modifications** to reflect the outcome of discussions with Member States on specific topics since 2011

A staged approach

✓ **Consolidation remains the ultimate objective**

- **BEPS-related elements of the common tax base:** already dealt with through ATAD/ATAD 2 and the Directive on CbCR.
- **1st step - Common tax base:** a set of corporate tax rules for computing the tax base of companies applying the CCCTB (without consolidating individual tax results).
- **2nd step - Consolidation & apportionment:** individual tax results are added up together in a single tax base and distributed based on a formula of 3 equally-weighted factors.

Scope of the re-launch proposals

Differently from CCCTB (2011), the re-launch has both a **mandatory** and an **optional scope**

- **Mandatory scope:** primarily serves the objective for fairer taxation and countering tax avoidance – limited to those who have the means to engage in such practices - **threshold of EUR 750 million** of consolidated revenue for the financial accounting group.
- **Optional scope:** those not captured by the mandatory scope will still have the option to apply the common rules, provided that they fulfil certain conditions.
- Scope also involves **EU-located PEs** of third-country companies.

R&D costs

1. **Fully deductible** in the tax year that the expense is incurred, except for R&D costs related to immovable property which go to depreciation;

2. An **additional 50%** of the **R&D costs up to** the first **EUR 20 million** is deductible in the same tax year, **except** for the cost related to **movable tangible fixed assets**;

3. An **additional 25%** of the R&D costs for the amounts above EUR 20 million is deductible in the same year (the exception for movable tangible fixed assets also applies here).

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Example on R&D costs

- A company incurred R&D expenses of EUR 25 000 000 in year 1.
- Deductible amounts – Article 9(2) &(3):

  1) cost fully deductible in the tax year incurred **25 000 000**, except for amounts which concern immovable property;

  2) super-deduction: extra deductible amount equal to

     - 50% of 20 000 000 (= **10 000 000**) and
     - 25% of 5 000 000 (= **1 250 000**).

- The company is allowed to deduct a total amount of EUR **36 250 000**.

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R&D costs for start-ups

- For up to EUR 20 000 000 of R&D costs, **start-ups may deduct an extra 100%** (instead of extra 50%); for costs beyond EUR 20 000 000, the **mainstream extra 25%** applies.
- A **'start-up'** is:
  - an unlisted company;
  - with fewer than 50 employees;
  - an annual turnover and/or balance sheet up to EUR 10 000 000;
  - not registered for longer than 5 years;
  - not formed though a merger;
  - without associated enterprises.

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Example on R&D costs for start-ups

- A start-up company incurred R&D expenses of EUR 25 000 000 in year 1.
- Deductible amounts – Article 9(2) & (3):

  1) cost fully deductible in the tax year incurred **25 000 000**, except for amounts which concern immovable property;

  2) enhanced super-deduction: extra deductible amount equal to:
     - 100% of 20 000 000 (= **20 000 000**) and
     - 25% of 5 000 000 (= **1 250 000**).

- The company is allowed to deduct a total amount of **EUR 46 250 000**.

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Allowance for Growth and Investment (AGI)

- A defined yield on **increases** in the **'AGI equity base'** is deductible.
- **'AGI equity base':** difference between the equity of a taxpayer and tax value of participations in associates (in a tax year).
- **Increases:** difference between the 'AGI equity base' at present and on joining the common tax base; reference can go back up to 10 tax years & thereafter, moves forward by one tax year.
- **Decreases:** the defined yield on the decrease is taxable.
- **Defined yield:** Euro area 10-year government benchmark bond in Dec of preceeding year, increased by a risk premium of 2 percentage points.

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Example on AGI (i)

- 1.1.2019:
  A company with a participation in a subsidiary joins the common tax base
- 31.12.2018:
  Tax value of the taxpayer's participations : 400
  Equity: 1 000
  AGI equity base: 600
- 31.12.2019:
  Participations value: 400
  Equity: 1 200
  AGI equity base: 800
  Increase in the AGI equity base: **200** (= 800-600)
  Defined yield for deduction to be applied to 200

Example on AGI (ii)

- 31.12.2020:
  Participations value: 400
  Equity: 1 300
  AGI equity base: 900
  Increase in the AGI equity base: **300** (= 900-600)

- 31.12.2021:
  Participations value: 400
  Equity: 900 (due to a profit distribution or trade loss of 400)
  AGI equity base: 500
  Decrease in the AGI equity base: 100 (= 500-600)
  Defined yield for taxation to be applied to 100

Temporary Cross-Border Loss Relief (i)

- Taxpayers without own losses may ***temporarily*** deduct losses incurred in the same tax year by ***immediate qualifying subsidiaries*** or PEs in other MS.

- 'Qualifying subsidiaries' means companies in the same CCCTB group.

- The deduction will be:
  - for subsidiaries, **in proportion to the holding** of the taxpayer; and
  - for PEs, **fully**.

Temporary Cross-Border Loss Relief (ii)

- "Temporarily" means that:

  (i) There is a **recapture** once the subsidiary/PE becomes profitable or at the latest, in 5 years.

  (ii) The regime will be **available until** the **CCCTB** comes **into force.**

- "Recapture" means that the taxpayer will **add** any **subsequent profits** made by the subsidiary/PE **back to its tax base** up to the loss previously deducted.

- Losses will automatically be reincorporated in a number of circumstances and at the latest, after 5 years.

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Example on Cross-Border Loss Relief

- B Co and C Co are both immediate and wholly-owned subsidiaries of A Co.
- 31.12.2019:

  A Co generates profits of 100; B Co profits of 50; and C Co tax losses of 50.

  A Co can use the tax losses of C Co up to 50 and bring its tax base down to 50 for 2019.
- 31.12.2020:

  A Co generates profits of 100; B Co profits of 50; and C Co profits of 100.

  A Co is liable to add profits of 50 (previously deducted)
- 31.12.2024:

  If C Co losses remain wholly or partially unrelieved, the balance is reincorporated to A Co as profits after 5 years.

Anti-Tax Avoidance Directive

Council Directive 2016/1164/EU of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (OJ L 193, 19.7.2016, p. 1-14).

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Scope & Minimum Standard

- **All taxpayers** that are subject to **corporate tax** in one or more Member State;
- **Transparent entities** fall **outside the scope** of the Directive – unless treated as taxpayers under national law.
- Concept of **minimum standard**:
  - to provide a **minimum level of protection** to the internal market; and
  - to **strengthen the average level of protection** against aggressive tax planning in the EU.

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Interest Limitation (i)

- **Interest costs are generally deductible expenses for tax purposes**
- MNEs take advantage of the high mobility of debt to shift income – in the form of inflated interest payments - towards low-tax jurisdictions
- The group reduces its overall tax burden
- Both the **BEPS reports and CCCTB proposals** suggest introducing a method for limiting the deductibility of net interest expenses (**'exceeding borrowing costs'**)
- Response to *Lankhorst*: the rule applies across the board – no discrimination risks

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Interest Limitation (ii)

- Underlying principle: the **financial costs** of a company may only be **fully deductible** up to the amount of its **taxable financial revenues**
- **'Exceeding borrowing costs'**:
  - Limitation up to **30%** of (tax-adjusted) **EBITDA**; or
  - **Safe harbour** of EUR 3 million,

  whichever allows for higher deductibility.
- Concept of taxpayer extends to a **tax group**
- Possible additional deductibility within **accounting groups filing cons'd financial statements** – (not taken on board for the common tax base)

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Interest Limitation (iii)

- Possibility of **full deductibility** of interest:
  - Up to **safe harbour** of EUR 3 million;
  - The taxpayer is a **standalone** company.
- **Waivers** – exclusion from the scope:
  - **Grandfathering clause** for existing loans – without extension of the benefit in the event of subsequent modification;
  - **Loans for** long-term **public benefit** infrastructure in the EU;
  - **Financial undertakings** (also when part of an accounting cons'd group)

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Exit Taxation (i)

- **Transfers of assets or tax residence** out of the tax jurisdiction of a Member State; disposals of assets are not included in the scope.
- **Objective:** to prevent the **risk** whereby assets, expected to generate high income, are **moved to low-tax jurisdictions** to have their profits taxed **at a low level**.
- **Transfers** covered:
- **Assets** from Head Office in the EU to PE in another MS or 3rd country or from PE in a MS to the Head Office or another PE in another MS or a third country;
- The **entire business of a PE** intra-EU or to a third country;
- **Tax residence** to another MS or 3rd country.

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Exit Taxation (ii)

- **Within the EU/EEA:**
  - **Deferral** of the payment of tax by arranging instalments over 5 years (poss. interest, guarantee)
- **Prevention of double taxation:** destination MS shall accept the market value determined by MS of the taxpayer or PE as a starting tax value (as a matter of principle).
- **No obligation to apply exit taxation:**
  - **Tax exempt assets;**
  - **Financial assets:** no exit tax on temporary asset transfers and as long as the assets are due to revert to the departing MS.

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General Anti-Abuse Rule (GAAR)

- **Aim:** to tackle abuses that have not yet been dealt with through specifically targeted provisions – designed to cover gaps
- **Within the EU:**

  (a) Regardless of wording, application to be limited to 'wholly artificial arrangements' (non-genuine); use of term 'essential' purpose – **substance test**

  (b) Taxpayer should have the right to choose the most tax efficient structure for its commercial affairs
- **Indistinct application** domestically and cross-border

** The question of withholding tax.

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Controlled Foreign Company (CFC) Rules(i)

** Under the **CCCTB**, scope is **limited to third countries.**

- **Aim:** to discourage shifting large profits out of a highly-taxed parent company towards subsidiaries in low-tax jurisdictions
- Schemes often involve shifts of mobile passive income (e.g. royalties) within a group, based on transfers of intangible assets to CFCs
- **Outcome:**
  (a) to reduce overall tax burden of the group;
  (b) internal market is affected

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CFC Rules (ii)

- Common requirements for **establishing** that a **CFC** exists:
  (a) A **participation of more than** 50% in the controlled subsidiary, directly or indirectly;
  (b) **Low level of taxation** in the third country or Member State where the subsidiary is tax resident,

  i.e. actual corporate tax paid by the entity or PE is **lower than the difference** between the corporate tax that would have been charged on the entity or PE under the corporate tax system of the MS of the taxpayer and the actual corporate tax paid on their profits.

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CFC Rules (iii)

- To compute CFC income for re-attribution, rules may target:
  - (i) the **entire revenues** of a low-taxed subsidiary; or
  - (ii) specific categories of income (**'tainted' income**); or
  - (iii) income **artificially diverted** to the subsidiary
- In ATAD, MS may opt between options (ii) & (iii) for computing the income of a CFC;
- In the Common Tax Base, only (ii) has been retained.

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CFC Rules (iv)

- **Policy option (ii)**
  - **List of categories** that income is derived from;
  - Escape clause: **taxpayer may prove sufficient substance** in its economic activity to avoid the CFC charge – **vis-à-vis third countries**, no obligation for MS to give this right
  - **'Throw-out' clause:** MS **may**(ATAD)/**shall**(CTB) not treat an entity or PE as a CFC if:
  - **not more than 1/3** of the income falls within one or more of the listed types of income
  - **financial undertakings** earn not more than 1/3 of their income through associates

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CFC Rules (v)

- **Policy option (iii) – only ATAD**
  - Re-attributes to the MS of the parent income generated in the subsidiary from **assets and risks which are effectively managed through SPF in the parent's** MS;
  - Amounts beyond 'arm's length' are **wholly artificial;**
  - **Exemptions** apply to low accounting profits and low profit margin.

Hybrid Mismatches (under amendment)

- Like COM's proposal, **only mismatches within the EU**;
- COM's text was based on **mutual recognition** due to certain constraints related to EU law;
- **Agreed text follows the OECD principle** – covers DD and D/NI arising from mismatches related to entities and/or financial instruments;
- COM was invited in a Council Statement (accompanying the agreed Directive) to table a proposal on hybrids involving **third countries by October 2016.**

Transposition Article: adoption and publication of the implementation of the ATAD in national legislation

General date: **31st December 2018** at the latest.

Transposition Date for **exit taxation**: 31st December 2019 at the latest.

Transposition Date for interest limitation rule: option for certain Member States with **equally effective** national rules – depending on the agreement of a minimum standard between OECD members or at the latest, until 1st January 2024.

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Thank you!

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