Tax Policy Update

24 July – 18 August

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European Commission

Cyprus changes tax treatment of financing companies, Commissioner Vestager applauds – 21 July

Commissioner Vestager has applauded a recent tax reform in **Cyprus** which revises the tax treatment of intragroup back-to-back financing transactions. The new rules aim to ensure that the remuneration of financing companies is in line with the arm's-length-principle. In her statement, Commissioner Vestager emphasises that Member States must be "on board and review their national rules and practice" in order to ensure that all companies pay their "fair share of tax".

Council

New VAT derogation for Croatia published – 28 July

A new derogation from the **VAT Directive** for **Croatia** has been published for the attention of Member States. The derogation would authorise Croatia to grant a VAT exemption to taxable persons whose annual turnover does not exceed €45,000. The exemption would be valid from January 2018 until December 2020. All Member States must approve the derogation, although no major issues with this regard is to be expected.

Austrian EU Presidency To Prioritize Tax – 1 August

Austria will take up the responsibility of Council Presidency from Bulgaria for the second half of 2018. Reportedly, The Austrian Presidency will maintain the ongoing policy momentum on tax, and keep anti-tax evasion and -avoidance high on the agenda. The Finance Minister, **Hans Joerg Schelling**, revealed that he has already discussed a possible Presidency agenda with **Commissioner Moscovici**. The agenda would include the Common Consolidated Corporate Tax Base (CCCTB), addressing the question of the so-called "virtual permanent establishments", and introducing VAT to all mail order sales. The denomination of a virtual permanent establishment would apply to digital companies that are not considered to have a taxable presence in a given jurisdiction under the current definition of a 'permanent establishment', despite generating sales there. Austria has promised to deliver concrete proposals on the matter. Overall, Austria's commitment to continue the anti-tax abuse agenda well into 2018 demonstrates that the political momentum on tax is all but fading, despite significant progress at the EU-level.

France and Germany to step up tax cooperation – 7 August

France and **Germany** are stepping up their cooperation in an effort to accumulate EU-level support for major tax reforms. The countries are, reportedly, aiming to harmonise their corporate taxes in 2018 – with eurozone level corporate tax harmonisation as the ultimate objective. France itself has committed to lowering its corporate tax rate from the current 33% to 25%.

A second pillar of the Franco-German tax cooperation will be to target large technology firms and digital platforms such as Airbnb, Amazon, Facebook and many others, in order to ensure that they pay their taxes where profits are generated. France and Germany will introduce proposals to this effect at the next meeting of the EU Finance Ministers to be held in Tallinn, Estonia, on 16 September. The European Commission, for its part, has indicated its intention to present guidance to Member States on how to deal with such firms. The French Finance Minister, Bruno Le Maire, expressed impatience at the slow pace of progress at the OECD-level to address digital companies – hence the push for more direct action at the EU-level. This would not be the first time that the EU seeks to move ahead of OECD in the fight against tax avoidance, as evidenced by the debate around public Country by Country Reporting (CBCR).

Airbnb, for its part, is insisting that its business model is "fundamentally different" from other companies, hence why it pays less taxes in the EU. The company argues that most of the profits stay in the hands of local communities and individuals who rent out their own homes.

Member States considering options for sanctions regime against non-cooperative jurisdictions – 9 August

Member States are considering a variety of options for a sanctions regime to be applied on so-called EU list of **non-cooperative jurisdictions**, once the list has been finalised by the end of this year. The details stem from a Council document seen by Bloomberg. According to the document, four types of sanctions are under particular consideration: withholding taxes, new controlled foreign company rules, elimination of deductible costs (e.g. royalties), and participation exemption limitations. Member States are also considering under what conditions and with what degree of flexibility the various sanctions can be applied on a given non-cooperative jurisdictions.

Three options are on the table: a flexible approach, rigid approach, or toolbox approach. The Flexible approach would allow Member States to choose from a menu of sanctions which ones to apply against a jurisdiction. The rigid approach, in turn, would require a list of countermeasures adaptable to the national systems of all Member States and suitable for all listed jurisdictions. The toolbox approach, for its part, would involve the development of more targeted toolboxes of countermeasures that would be aimed at addressing specific issues such as levies on outbound royalty payments. According to Bloomberg, the Council document appears to emphasise the benefits of the toolbox approach – which might indicate that a priori this will be the preferred option. However, a tax attache from **Estonia** emphasised that it is possible that the sanctions regime will not be finalised before the final list of non-cooperative jurisdictions is ready.

International

White House and Congress Republicans close to agreement on Tax Reform – 27 July

The expected major **US** tax reform has taken further steps forward as the White House and Congress Republicans have agreed on the broad principles of the reform. These principles include, notably, lowering the corporate tax – albeit no agreement yet on the rate as White House has been calling for a 15% rate and Congress Republicans for 20%, and removing a number of business tax breaks. Interestingly, the so-called Border Adjustment Tax (BAT) will not be a part of the tax reform. This can be seen as a victory for White House, as Congress Republicans have been vocal in calling for a BAT, whilst President Trump's administration has remained sceptic. **Kevin Brady**, the Chairman of the powerful Ways and Means Committee, has estimated that the reforms could still be finalised by the end of this year, whilst more optimistic voices from the White House hint at November.

There has been little visible debate about a possible move to a so-called territorial tax system. However, a non-partisan US think-tank has recently warned that if badly designed, a territorial US tax system could prove overly complex, thus defeating one of the main purposes of the pending tax reform – simplification.

Overall, getting tax cuts through now seems to be the main target for reform, although with BAT gone there is uncertainty as to how the cuts would be funded. Still, according to a Bloomberg survey, a majority of economists expect Republicans to get tax cuts through before Congressional elections in November 2018. However, the economists are not convinced that the cuts would have any meaningful positive impact on the economy during 2018. Moreover, another survey by Deloitte found that the private sector does not believe that Trump will manage to cut the rate all the way to 15%. Almost 40% out of 3100 private sector respondents expect the rate to fall to 25%.

Either way, with the setbacks on healthcare reform, the Trump administration will now direct its fully energy to tax reform. A lot of scepticism and criticism remains, as some commentators blame the Republicans for being ambiguous on major issues such as tax deductions and moving to a territorial tax system, and pushing for mere tax cuts under the banner of 'tax reform'. Democrats, for their part, have already outlined their conditions for tax reform – some of which appear to be at odds with what the Republicans are pushing for.

Latvia Adopts Major Tax Reform – 3 August

The parliament of **Latvia** has adopted a major corporate tax reform under which company profits would not be taxed until or unless they are distributed. The tax rate on distributed profits would be set at 20% starting January 2018, whilst re-invested profits would not be subject to tax at all. Moreover, the reform would get rid of the current 23% flat tax on personal income and introduce a progressive system.

India sees increase in tax returns after reforms – 3/8 August

In **India**, tax authorities have reported a 25% increase in income tax returns following a set of measures by the government to improve tax compliance and increase the number of income tax paying citizens to 100 million. Reportedly, a major contributor to this was the government's decision from November 2016 to withdraw 86% by value of the cash in circulation, in a bid to make life more difficult for individuals with large amounts of illicit cash. Moreover, tax authorities were called to keep a particular eye on individuals and businesses depositing above a set limit of the old currency notes in their banks accounts. At the same time, economists have noted that the increase in the number of taxpayers has not brought about significant increases in the amount of tax collections.

The Indian government continues its fight against tax non-compliance through more innovative means. Reportedly, the country's tax authorities will soon begin to screen social media profiles in order to make sure that their activities and assets are in line with their declared taxable income.

Luxembourg opting for a new patent Box Regime – 11 August

The government of **Luxembourg** has proposed amendments to its IP regime in order to align it with the OECD's 'modified nexus' approach. The new regime would allow for a wider range of patents and copyrights on computer software, but trademarks and designs would be ineligible. Moreover, costs that are not directly related to the IP would be ineligible, along with costs related to real estate, interest and financing.

AUSTRALIA'S OPPOSITION CALLS FOR TAX TRANSPARENCY – 14 August

The Labour opposition of **Australia** has issued a call for greater tax transparency, as expressed notably in a statement published by the shadow assistant treasurer **Andrew Leigh**. The Labour party is calling for companies with a turnover exceeding $100 million to publish their tax information, as well as for businesses to disclose their activities in "tax havens" in government tenders and to commit to public Country-by-Country Reporting (CBCR).

Data published on 2016 Dutch environmental tax income – 15 August

According to the statistics agency of the **Netherlands**, the Dutch state received €25,3 billion of revenues from environmental taxes and charges in 2016. This amounts to a 3% increase in revenue from 2015. Households account for approximately 2/3 of the tax's revenue. At the same time, however, the share of environmental tax revenue in the overall tax revenue has been in decline in past year, falling from 17,1% in 2011 to 15,3% in 2016.

"German Prosecutors Investigating Swiss Tax 'Spies'" – 16 August

Germany's prosecutors are looking into suspected spying of the country's tax administrations by **Switzerland's** intelligence agency. One individual has already been arrested, and three more working for the Swiss intelligence agency are suspected of being linked to the case. The Swiss have allegedly been spying on efforts by German tax authorities to use stolen data to acquire further information on German taxpayers suspected of hiding their wealth offshore.

Slovakia amends tax credit for R&D – 17 August

Slovakia has introduced major changes to its R&D cost tax deductions. Currently, companies are eligible for a 25% deduction from R&D expenses, as well as an additional 25% deduction to R&D costs exceeding R&D spending from the previous year. The proposed new rules would increase both 25% deductions to 100%. The government is also planning to introduce a patent box regime. The amendments will enter into force from January 2018 onwards.

OECD

OECD report: Neutralising the tax effects of branch mismatch arrangements – 27 July

The OECD has published a new report on neutralising the effects of branch mismatch arrangements. The report sets out recommendations for branch mismatch rules that would bring the treatment of such structures into line with the treatment of hybrid mismatch arrangements as set out in the OECD BEPS Action 2 (neutralising the effects of hybrid mismatch arrangements). The OECD explains that branch mismatches arise where the ordinary rules for allocating income and expenditure between the branch and head office result in a portion of the net income of the taxpayer escaping the charge to taxation in both the branch and residence jurisdiction. Branch mismatches result from differences in the way the branch and the head office account for a payment made by or to the branch. The new report identifies five basic types of branch mismatch arrangements that give rise to one of three types of mismatches: deduction/no inclusion (D/NI) outcomes, double deduction (DD) outcomes, and indirect deduction/no inclusion (indirect D/NI) outcomes. It also includes specific recommendations for improvements to domestic law intended to reduce the frequency of branch mismatches as well as targeted branch mismatch rules which adjust the tax consequences in either the residence or branch jurisdiction. The objective is to neutralise the hybrid mismatch without disturbing any of the other tax, commercial or regulatory outcomes.

The Platform for Collaboration on Tax invites comments on a draft toolkit on the taxation of offshore indirect transfers of assets – 1 August

The OECD's Platform for Collaboration on Tax has published a draft toolkit designed to help developing countries tackle the complexities of taxing offshore indirect transfers of assets. The Platform is now seeking public feedback on its draft toolkit by 25 September 25. The aim is to release the final toolkit by the end of 2017.

The draft toolkit examines the principles that should guide the taxation of such transactions in the countries where the underlying assets are located. It emphasises extractive (and other) industries in developing countries, and considers the current standards in the OECD and UN model tax conventions, and the new Multilateral Convention. The toolkit also discusses economic considerations that may guide policy in this area, the types of assets that could appropriately attract tax when transferred indirectly offshore, implementation challenges that countries face, and options which could be used to enforce such a tax.

Public comments received on the draft contents of the 2017 Update to the OECD Model Tax Convention – 11 August

The OECD has published the public comments received on the draft contents of the 2017 Update to the OECD Model Tax Convention. A total of seven organisations provided comments, including the BEPS Monitoring Group, BIAC and the International Chamber of Commerce (ICC).

Nigeria signs the Multilateral BEPS Convention and the CRS Multilateral Competent Authority Agreement – 17 August

Nigeria has committed to the Multilateral Convention in tax Matters (MLI) as well as the CRS Multilateral Competent Authority Agreement (the CRS MCAA). Nigeria thus became the 71st jurisdiction to sign the MLI and the 94th jurisdiction to join the CRS MCAA.

The MLI is a legal instrument designed to prevent base erosion and profit shifting by multinational enterprises. It allows jurisdictions to transpose results from the BEPS Project into their existing networks of bilateral tax treaties in a quick and efficient manner. The CRS MCAA, in turn, is a multilateral competent authority agreement aiming to implement the automatic exchange of financial account information pursuant to the Common Reporting Standard (CRS), and to deliver the automatic exchange of CRS information between 101 jurisdictions by 2018.

State Aid

Commission requires Belgium and France to put an end to tax exemptions for ports – 27 July

The European Commission has ordered **Belgium** and **France** to abolish corporate tax exemptions granted to their ports, in order to align their tax regimes with EU state aid rules. The Commission states that profits by port operators must be taxed under normal national corporate tax laws to avoid distortions of competition. In particular, the Commission assesses that the tax exemptions do not pursue a clear public interest objective, such as the promotion of mobility or multimodal transport. Instead, the tax savings can be used by the port operators to fund any type of activity or to subsidise the prices charged by the ports to customers, to the detriment of competitors and fair competition. Both countries now have until the end of 2017 to take the necessary steps to remove the tax exemptions in order to ensure that, from 1 January 2018, all ports are subject to the same corporate taxation rules as other companies.

Ireland criticizes EU demand that Apple pAY IT €13 BILLION IN BACK TAXES – 17 August

Ireland has renewed its criticism of the European Commission's ruling ordering it to collect €13 billion in unpaid taxes. The new Irish Finance Minister, **Paschal Donohoe**, has stated that his country is not "the global tax collector for everybody else", and argues that most of Apple's European profits are taxable in the **US** instead.

Other News

New research on key role major economies play in global tax avoidance – 25 July

The civil society organisation Tax Justice Network has reported on a new study from the University of Amsterdam which appears to demonstrate the central role that European countries such as the **UK** and the **Netherlands** play in the global tax avoidance network. The study is based on data from over 77 million ownership relations, which form a network in which value flows from subsidiaries to shareholders. From the data, the researchers have extracted millions of global corporate ownership chains, thus enabling to not only see where value originates and ends up. Countries such as the UK, the Netherlands, **Ireland**, **Switzerland** and **Singapore** are one of the few so-called "conduit" Offshore Financial Centres (OFCs) – i.e. jurisdictions through which a disproportional amount of value moves to other OFCs where the value disappears from the economic system.

New tax complexity index published – 27 July

According to a new index ranking countries by the complexity of their accounting and tax compliance regimes, **Turkey** has the most complex tax system out of a total of 94 jurisdictions that were screened and compared on the basis of a set of specific criteria. **Italy** (3rd), **Greece** (4th) and **Belgium** (8th) top the list for EU countries.

MEP Questions & Answers

Gibraltar — Blacklist of non-cooperative tax jurisdictions – 17 July

The Council of the EU has replied to a question asked by the MEP **Enrique Calvet Chambon (ALDE/SPA)** with regard to the pending EU list of non-cooperative jurisdictions. In his question, Mr. Calvet Chambon asks the Council whether Brexit and the status of Gibraltar has been considered by Member States in the process of devising the blacklist. In its reply, the Council confirms that the prospect of including Gibraltar on the blacklist as a Brexit-related scenario has not been discussed.

Environmental taxation – 17 July

The European Commission has replied to a question asked by the MEP **Dubravka Šuica (EPP/CRO)** with regard to environmental taxation. In her question, Ms. Šuica asks the Commission how it will ensure that all Member States have similar environmental protection rules and, in particular, environmental taxes. In his reply, **Commissioner Vella** (environmental affairs) emphasizes that it is up to Member States to choose which tools – including taxation – they use to ensure environmental protection and sustainability. The Commission cannot interfere with Member States' tax systems as long as they are compliant with EU law. Moreover, he reminds that environmental taxes are only one tool in a larger toolbox of environmental measures. The Commission does, however, monitor national tax systems and provides recommendations for improvement where it sees appropriate in the context of the European Semester and in the Environmental Implementation Review.

Panama Papers — Madeira — administration by a public/private consortium – 20 July

The European Commission has replied to a question asked by the MEP **Louis Michel (ALDE/BEL)** with regard to **Madeira** and Panama Papers. In his question, Mr. Michel refers to a public-private consortium which is responsible for issuing licenses to companies based in the International Business Centre of Madeira in exchange for registration fees and annual license fees from all companies on the Madeira commercial register. This provides the consortium with an estimated annual income of between €4 and €5 million. Mr. Michel asks the Commission whether the consortium is legal, given that it has no incentives to properly supervise the Madeira free trade zone due to the license fees, thus potentially rendering Madeira into a 'tax haven'. In her reply, **Commissioner Vestager** states that in principle, it is possible to award a concession to a public-private partnership to administer a free trade zone. The

Commission is, however, currently examining if the concession contract to administer the Madeira free trade zone has complied with the necessary criteria and prerequisites.

VAT fraud – 4 August

The European Commission has replied to a question asked by the MEP **Andrey Kovatchev (EPP/BUL)** with regard to VAT fraud. In his question, Mr. Kovatchev states that the current VAT system is vulnerable to fraud and tax avoidance. Carousel fraud alone results in VAT revenue losses of approximately €50 billion in 2014. He asks the Commission whether it has taken "concrete steps" to access information exchanged between Member States with a view to preventing and combating carousel fraud, and whether it will require Member States to report cases of fraud and other types of irregularities. In his reply, **Commissioner Moscovici** re-iterates that the Commission will table a legislative proposal for the definitive VAT system "by the end of 2017", which should address current weaknesses in the VAT system. The Commission is also examining how to reinforce administrative cooperation between Member States, notably in terms of enabling a swifter and more efficient detection of cross-border fraud cases. A legislative proposal will also be submitted before the end of 2017. And finally, the Commissioner confirms that the Commission regularly collects information on information exchanges between Member States and the use made of the existing cooperation instruments to evaluate their effectiveness.

VAT on sports activities – 8 August

The European Commission has replied to a question asked by the MEP **Theodoros Zagorakis (EPP/GRE)** with regard to VAT on sports activities. In his question, Mr. Zagorakis asks the Commission whether it has comparative data on VAT for sports in Member States, and whether there is scope for reducing VAT rates in Europe for sports undertakings. In his reply, **Commissioner Moscovici** states that the Commission is not aware of any Member State collecting data on VAT revenues from sports activities. According to EU VAT law Member States can either apply the standard VAT rate or a reduced VAT rate to the use of sport facilities. However, reducing VAT rates for the use of such facilities falls under the responsibility of each individual Member State. The Commissioner, moreover, confirms that 16 Member States apply the standard rate to the use of sport facilities, whereas 12 Member States apply a reduced rate.

Capital gains tax in Portugal – 8 August

The European Commission has replied to a question asked by the MEP **Daniel Hannan (ECR/UK)** with regard to capital gains tax in **Portugal**. In his question, Mr. Hannan asks the Commission whether Portuguese domestic law on capital gains tax on properties now conforms with EU law. Previously, the tax was on 50% of the gain for residents, and 100% for non-residents – a system that the Court of Justice of the EU deemed incompatible with EU law (case code C-443/06). In his reply, **Commissioner Moscovici** confirms that Portugal did change its legislation, but there are doubts as to whether the amendments have remedied the situation. The Commission has, therefore, sent a letter of formal notice to Portugal in April 2017 to further inquire the matter.

Croatian Special Motor Vehicle Tax Act – 9 August

The European Commission has replied to a question asked by the MEP **Ruža Tomašić (ECR/CRO)** with regard to a motor vehicle tax in **Croatia**. In her question, Ms. Tomašić refers to Croatian special motor vehicle tax which has been in force since January 2017. On used vehicles, the law states that in lack of selling price data for Croatia, the customs office will determine the special tax balance by reference to a motor vehicle with broadly similar characteristics on the market in Croatia. This also means that the special tax charged on used vehicles from other Member States is based in part on motor vehicle prices on the Croatian market, rather than the price that the buyer actually paid for the vehicle. The tax rules could, therefore, dis-incentivise Croatian citizens to buy used vehicles in other Member States. She therefore asks the Commission whether the Croatian tax regime is in breach of EU law. In his reply, **Commissioner Moscovici** states that there are currently no indications that the Croatian law would be in breach of EU rules. Second-hand vehicles on the domestic market must be regarded as 'similar' to imported second-hand vehicles of the same type, characteristics and wear. Consequently, taxes on vehicles should be levied in such a way that they do not have the effect of promoting sales of domestic second-hand vehicles, thereby discouraging imports of similar second-hand vehicles. Therefore, a Member State is not necessarily precluded from introducing a car registration tax based on prices prevailing on the national market. However, the tax would violate EU law if, for instance, the tax levied on an imported second-hand car was higher than the residual tax of a similar car already registered on the national market.

The Spanish Constitutional Court's delayed response to the tax amnesty has prevented the Tax Agency from recouping EUR 5.3 billion – 11 August

The European Commission has replied to a question asked by the MEP **Ramon Tremosa i Balcells (ALDE/SPA)** with regard to a delayed response to a tax amnesty from **Spain's** constitutional court which has, allegedly, prevented the tax agency from collecting tax income. In his question, Mr. Tremosa i Balcells argues that a tax amnesty case from 2012 has cost public coffers €5,3 billion in tax income. He asks the Commission for tax fraud percentage in Spain, whether the tax amnesty law and judicial delay are in compliance with the Anti-Tax Avoidance Directive (ATAD), and whether the Commission took the missing €5,3 billion into account when calculating Spain's budget deficit. In his reply, **Commissioner Moscovici** states that the Commission has no data on tax fraud in Spain. However, the VAT compliance gap in Spain was estimated at 9% of the VAT liability in 2014. Furthermore, the Commissioner reminds that ATAD was not devised to fight against tax fraud. And finally, the amount mentioned was not included in the Commission's tax revenue projections, since its forecasts do not include revenue that could have been collected under hypothetical tax policy scenarios.

Evidence of tax avoidance and evasion by large European banks – 16 August

The European Commission has replied to a question asked by the MEP **Dimitrios Papadimoulis (GUE-NGL/GRE)** with regard to tax avoidance and evasion by large European banks. In his question, Mr. Papadimoulis refers to data from Oxfam which appears to demonstrate that 20 large European banks have reported unusually high profits in "tax havens", and asks the Commission whether the data is accurate, what is the state of play with the introduction of information exchanges between Member States to cross-check transfers of funds in countries with a very low or zero tax rate, and whether tax evasion by banks is permissible under EU law. In his reply, **Commissioner Moscovici** questions the validity of the data, since Oxfam uses its own definition of 'tax havens'. He, moreover, provides a timeline for the applicability of the various tax information exchanges provisions covering tax rulings and Country-by-Country Reporting (CBCR). And finally, the Commissioner points out that tax evasion often has only a domestic dimension and is addressed by EU Member States through national legislation. The Commission proposes EU-level legislation to assist them in identifying cross-border tax avoidance and evasion practices within the EU.

Events

- 07/09/2017, ***Current Issues in European Tax Law***, Estonian Presidency, Tallinn, Estonia. Source
- 13/09/2017, ***Taxation of the sharing economy***, EESC. Tallinn, Estonia. Source
- 27/09/2017, ***Commerce and Industry Group Annual Conference – tax***, CIOT, London. Source
- 12/10/2017, ***Future of VAT: Digitalisation is here!***, Accountancy Europe, Brussels. Source
- 21/11/2017, ***FairTax meets COFFERS: Joint Perspectives on Fair and Sustainable Taxation***, Umea University, Brussels. Source