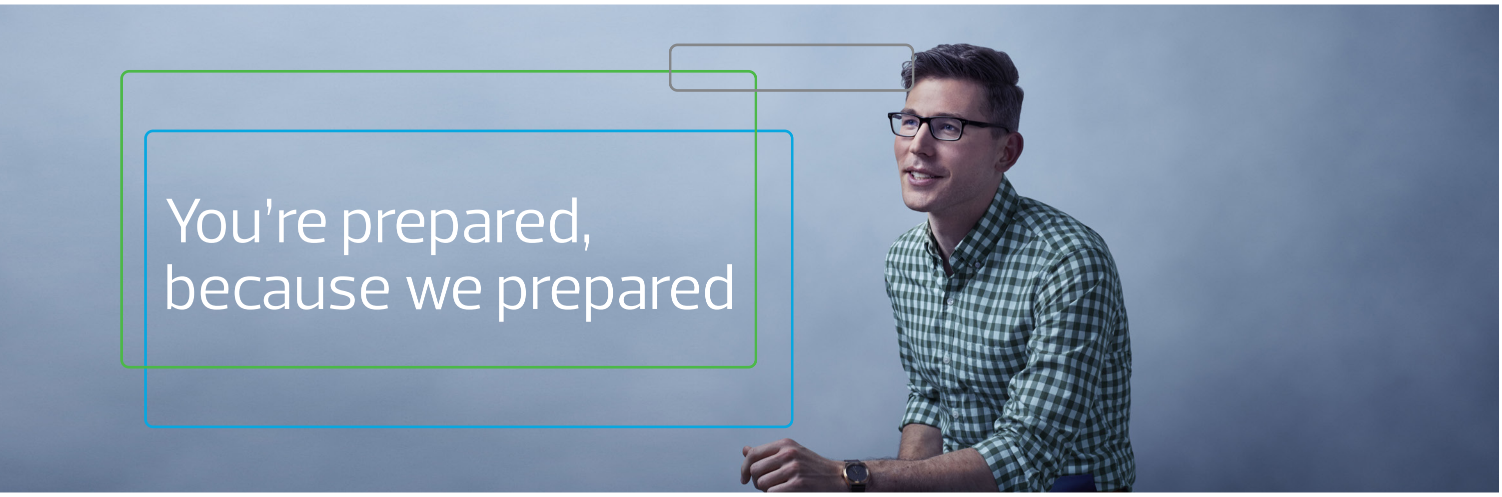

IMPORTANT TAX PROPOSALS ANNOUNCED BY THE EUROPEAN COMMISSION

The European Commission (EC) published an important communication on the re-development of Business Taxation for the 21st century in the European Union (EU) that includes a series of important legislative proposals.

Overview tax proposals

With the legislative proposals the EC promotes a robust, efficient and fair business tax system in the EU that at the same time sets out both a long-term and short-term vision to support Europe's recovery from the COVID-19 pandemic. Below we provide a short outline of all measures that have been proposed:

1. **European Corporate Income Tax**
   In 2023 the EC will present a new framework for business taxation in the EU (BEFIT). BEFIT should reduce administrative burdens, minimise tax avoidance opportunities, provide for fairer allocation of taxing rights between Member States and as such create a more business friendly environment in Europe. BEFIT aims to provide a single corporate income tax rulebook for the whole EU.

2. **EU Pillar I Directive**
   The Pillar I project of the OECD aims to provide jurisdictions a right to tax part of the profits of certain non-resident businesses (digitally operating businesses) by introducing a transfer pricing mechanism based on which taxation rights will be provided to the jurisdiction where the customers of a company are located. In order to ensure a consistent implementation of the Pillar I project in all EU Member States, the EC is going to propose a Directive for the implementation of Pillar I in the EU.

3. **EU Pillar II Directive**
   The Pillar II project of the OECD aims to guarantee a minimum level of effective taxation by providing rules to enable jurisdictions to top up the amount of tax paid by large multinationals to a minimum effective level. Pillar II sets a floor to excessive tax competition between jurisdictions and should limit tax avoidance opportunities. In order to ensure a consistent application within the EU and compatibility with EU law, Pillar II will be implemented through an EU Directive.

4. **Transparency rules on taxes paid by large companies**
   The EC will create a legislative proposal in 2022 for the annual publication of effective tax rates paid by large companies in the EU, using the methodology of Pillar II. Based on this legislation information will be provided to the public on the taxes paid over the amount of profits that are generated, and thus not over the amount of the taxable profits.

5. **ATAD 3 – Abusive use of shell companies**
   The EC will publish a legislative proposal in Q4 2021 targeting the abusive use of companies with no or minimal substantial presence and real economic activity (shell companies), which are created for the main purpose of reducing the tax liability or disguising improper conduct of the group or operations they belong to. The EC announces that the legislative proposal will encompass rules on the exchange of information to tax administrations, and rules for denying tax benefits linked to the existence or the use of abusive shell companies.

The EC also intends to take further steps to prevent royalty and interest payments leaving the EU from escaping taxation. These rules will most likely be part of ATAD3.

6. **Debt Equity Bias Reduction (DEBRA),**
The current tax framework encourages to finance investments through debt rather than equity, because it allows a tax deduction of interest on debt but not for the costs related to equity financing. The EC recognizes that this contributes to an excessive accumulation of debts, with potential negative effect for the EU as a whole. The EC will therefore make a proposal to address the debt-equity bias in corporate taxation, via an allowance system for equity financing, thus contributing to the re-equitization of companies. The proposal will incorporate anti-abuse measures to ensure it is not used for unintended purposes and is expected to be published in Q1 2022.

7. **Loss utilization rules**
The EC is adopting a recommendation to EU Member States on the domestic treatment of losses, to improve a fair competition between companies operating in the EU and to better support companies recovering from the COVID-19 crisis (loss utilization rules). The EC will also investigate whether a coordinated treatment of cross-border loss relief will be possible within the EU.

Our observations with respect to the announced measures:

The Communication provides an interesting insight into the EU's thinking and also shows a proactive approach with short-term planning as soon as Q4-2021 for combatting low-substance shell companies. This Communication should not be viewed as a standalone event. It is clear that governments all over the world are considering a revision of the international tax framework necessary for many different reasons of which budgetary reasons still remain one of the key considerations.

Our view is that although it is important to wait for further details on the upcoming plans, a change in mindset and behaviour should also be considered paired to an interactive approach outlining different scenarios on how internationally active companies should react and make sure to become a collaborative part of historical international tax changes.

Our observations in particularly entail:

1. The EU is determined to play a leading role in the revision of the international tax framework.
2. The EU has recognized the importance of taxation of the digital economy and the shortcomings of the current international tax framework in this area. Digital presence must clearly mean that internationally companies also have operational / business presence in jurisdictions without having physical presence.
3. It is interesting (and not surprising) to see that the EU emphasized the importance of the COVID-crisis and the countries' needs for further funding, but at the same time the EC recognizes that corporate income (business) taxation should play a more significant role compared to revenue generators such as labour taxes and VAT. Corporate income taxation and digital levies can ensure a more sustainable and fair European tax revenue.
4. Even more transparency is promoted whereby the use of shell and holding companies will continue to be scrutinized. Operational substance must be promoted and recognized.
5. New EU measures in the corporate tax field should make the corporate tax systems simple, reducing the need for anti-abuse measures and thus lowering administrative burdens and compliance costs for international business operating and investing in the EU.
6. Last but not least, the EU calls for a new Single Market taxation system (BEFIT) replacing the idea of a common consolidated tax base (CCCTB). This could lead to a departure of the arm's length principle for MNE's operating in the EU.

More information?

If you would have any questions with respect to these new measures, please feel free to contact your trusted RSM advisor.