European Commission - Fact Sheet

Questions and Answers on the package of corporate tax reforms

Strasbourg, 25 October 2016

Why has the Commission presented a new package of corporate tax reforms?

One of the Commission's top political priorities is to make taxation fairer and more effective in the EU, as set out in the June 2015 Action Plan. Over the past two years, the Commission has advanced an ambitious agenda to achieve this, in particular through the fight against tax evasion and avoidance. There have already been some landmark achievements. Member States have agreed to new transparency rules for tax rulings and reports on multinationals' tax-related activities. They have adopted binding anti-abuse measures against some of the most common forms of tax avoidance and have started work on a new EU list of third countries that refuse to respect tax good governance standards.

Other transparency measures proposed by the Commission are now being negotiated, including public country-by-country reporting requirements for the EU's largest companies. In addition, the Commission's work in the state aid area is addressing unfair tax advantages that some Member States have given to certain companies.

For the longer term, a more holistic reform of corporate taxation in the EU is needed. There needs to be the right balance between implementing the reforms necessary to make taxation fairer and providing a predictable, growth-friendly tax environment for businesses. This package offers the EU a forward-looking framework for corporate taxation, which meets the 21st century needs of businesses, Member States and the economy as a whole.

What are the initiatives in this package?

There are three separate initiatives in today's package:

I. The Common Consolidated Corporate Tax Base (CCCTB)

The Commission has improved and re-launched the Common Consolidated Corporate Tax Base (CCCTB), which is perhaps the most ambitious corporate tax reform ever proposed in the EU. The CCCTB will provide Member States with an entirely new system for taxing multinationals, in a way that will make the EU more business-friendly while also eliminating the main channels of profit-shifting.

II. Improved mechanisms to resolve double taxation disputes

Double taxation is one of the most serious tax obstacles for businesses in the Single Market. The Commission has today proposed better procedures for resolving double taxation disputes in the EU to bring greater certainty for businesses.

III. Measures to tackle tax loopholes with non-EU countries

This proposal builds on to the Anti-Tax Avoidance Directive, which was agreed in July, with measures to stop companies from exploiting differing rules or 'mismatches' between the tax systems of Member States and those of non-EU countries.

1. **THE COMMON CONSOLIDATED CORPORATE TAX BASE**

What is the CCCTB?

The CCCTB is a harmonised system to calculate companies' taxable profits in the EU. It offers one set of rules for companies to determine their tax base, rather than multiple national ones. It will enable businesses to file a single tax return for all of their EU activities. Companies in the CCCTB system will also be able to offset losses in one Member State against profits in another, thereby enjoying the same treatment as purely domestic companies. The CCCTB will make it easier, cheaper and more attractive for companies to operate across the Single Market.

The CCCTB is also a potentially powerful instrument against tax avoidance. Common rules for taxing companies in the EU will remove the loopholes and mismatches in the current corporate tax frameworks which enable aggressive tax planning. They will boost transparency and reduce harmful tax competition.

(See Annex for more details)

What are the benefits of the CCCTB?

The CCCTB will improve the Single Market for businesses

The CCCTB will greatly reduce administrative burdens, compliance costs and tax obstacles for cross-border companies in the EU. They will be able to use a single EU system to compute their taxable income, rather than having to deal with multiple national rulebooks. They will also be able to file their tax return for all of their EU activities through a "One Stop Shop" system, meaning that they only have to deal with one administration, just as purely domestic companies do. The CCCTB will enable companies to offset profits in one Member State against losses in another, which is particularly important for smaller and start-up companies. The CCCTB will be a stable, transparent EU-wide system, enshrined in EU law. This will provide companies with much greater legal certainty and reduce tax obstacles such as double taxation. With the CCCTB, time spent on annual compliance activities should decrease by 8% while the time spent for setting up a subsidiary would decrease by up to 67%, making it easier for companies, including SMEs, to set up abroad.

The CCCTB will help to combat tax avoidance

The CCCTB will have a major impact in the fight against corporate tax avoidance. The Commission has proposed to make it mandatory for the largest groups in the EU, which have the greatest capacity to carry out aggressive tax planning. The CCCTB will eliminate mismatches and loopholes between national systems, which companies currently can exploit to avoid taxation. Consolidation will remove the need for complex transfer pricing, which is one of the main vehicles for profit shifting within groups. In addition, the common base will create complete transparency on the effective tax rate of each Member State, by removing any opaque and preferential tax regimes that currently exist in national systems. As such, it should reduce harmful tax competition within the EU. The CCCTB also contains robust anti-abuse measures, to defend the Single Market against base erosion and profit shifting to non-EU countries. These are in line with those in the Anti-Tax Avoidance Directive (ATAD), which Member States agreed in July 2016.

The CCCTB will support growth, jobs and investment in the EU

The CCCTB directly supports the EU's wider economic priorities. The CCCTB can lift investment in the EU by up to 3.4% and growth by up to 1.2%. It will offer companies predictable rules, a level-playing field and reduced compliance costs. This will make the EU a more attractive market to invest and do business in. It will incentivise R&D spending, which is crucial for future growth. It will remove the current debt-bias in corporate taxation, thereby contributing to a strong Capital Markets Union and greater financial stability in the EU.

In addition, the CCCTB will mean that revenues currently lost to tax avoidance will be channelled into the public purse for productive investment, as aggressive tax planning is curtailed by the CCCTB.

Why has the Commission decided to re-launch the CCCTB now?

Four years of technical discussions in Council have shown that the 2011 CCCTB proposal was not going to be adopted in a single step. While there was progress and support on some important areas, discussions faltered on more difficult aspects, notably consolidation. In addition, it became clear that the original proposal needed to be adjusted to be truly effective in tackling tax avoidance and to respond to other challenges such as the need to incentivise R&D.

There has been broad support from businesses, many Member States, the European Parliament and stakeholders for this re-launch of the CCCTB.

What are the new features in the re-launched CCCTB compared to the original proposal?

One of the main features is that the re-launched CCCTB is split into two proposals which can be implemented in two stages. Member States will be able to agree on the common base first, before working on the more complex consolidation aspect. This should make the negotiation process more manageable, facilitating more constructive discussions and quicker agreement, without reducing the overall level of ambition.

The improved CCCTB can better meet new and emerging corporate tax challenges, in particular because:

1. The CCCTB will be mandatory for the largest companies

The CCCTB will be mandatory for all groups with global consolidated revenues of more than EUR 750 million. This should help to maximise its potential as an anti-avoidance tool. Large groups will not be able to opt out of the watertight CCCTB system simply to continue aggressive tax planning. Companies that fall below the threshold will still be able to opt in to the CCCTB, in order to avail of the greater simplicity, certainty and cost-savings it will bring.

The mandatory aspect also means that the businesses concerned will know where they stand when it comes to the EU's anti-abuse rules and will not have to make unnecessary adjustments. As such, it will help to create a more predictable environment for businesses in the EU.

2. The CCCTB will support Research and Development (R&D)

A new R&D incentive has been included to encourage companies in the EU to invest in research and innovation, which are key drivers of growth. Companies will be given a super-deduction for their R&D costs [see separate section]. To support small and innovative companies that decide to opt-in to the CCCTB, an even more generous super-deduction will be given to start-up companies which will be allowed to deduct up to 200% of their R&D costs, under set conditions.

3. The CCCTB will remove the incentive for debt accumulation

The CCCTB will address the current debt-bias in taxation, which allows companies to deduct the interest they pay on their debts but not the costs of equity. This debt-bias distorts financing decisions, makes companies more vulnerable to bankruptcy and undermines the stability of the overall economy. Therefore, the CCCTB introduces an 'Allowance for Growth and Investment' (AGI), which will give companies equivalent benefits for equity as they get for debt. This will reward companies for strengthening their financing structures and tapping into capital markets. This initiative chimes with the Commission's plan for a Capital Markets Union which seeks to give businesses access to alternative, more diverse sources of funding.

How will the CCCTB work in practice?

In the re-launched CCCTB, Member States will have the possibility to agree on and implement the common base first, with consolidation coming as a second step, ideally soon afterwards. In terms of how the system works:

The common base provides the single set of rules to decide how a company's profit will be taxed, once various exemptions and deductions have been accounted for. For example, the common base will ensure that all Member States allow the same rate of depreciation for a particular asset or allow the same particular expense to be tax-deductible. This means that companies will only have to refer to one set of rules when calculating their taxable profits and the calculation will be uniform throughout the EU.

Consolidation will allow a group to add up all the profits and losses of its constituent companies in different Member States, to reach a net profit or loss for the entire EU. Based on this net figure, the rules in the common base will be used to decide the group's final amount of profits that should be taxed.

Once the tax base of the company has been established, the company's taxable profits will be shared out between the Member States in which the company is active using an **apportionment formula** (see below). Each Member State can then tax their share of the company's profits at their own national rate.

How will the apportionment formula work?

Once a company's consolidated tax base has been established (see above), each Member State in which the company has activities will have the right to tax part of this base. The proportion of the company's base that a Member State can tax will be decided based on 3 equally weighted factors:

- The **assets** the company has in that Member State (e.g. buildings, machinery).

- The **labour** the company has in that Member State (i.e. the number of employees and employment costs).

- The **sales** that the company made in that Member State. The sales factor will be calculated on the basis of destination (i.e. where the goods are sold/dispatched to or where the service is carried out).

Is it possible to have the common base on its own, until consolidation is introduced?

The full benefits of the CCCTB will only come about when both the common base and consolidation are implemented. Nonetheless, the common base can be applied while consolidation is being negotiated and will already bring some important improvements to the EU's corporate tax environment.

The common base sets down common rules for companies to calculate their taxable profits. It will therefore remove the need for companies to deal with many different national rules when they operate cross-border in the EU. This will considerably reduce compliance costs and administrative burdens.

The common base will also make corporate taxation in the EU more transparent and efficient. It would no longer be possible for Member States to have hidden elements in their tax bases, such as preferential rulings, which can lead to harmful tax competition and profit shifting. The CCCTB would also remove the mismatches and loopholes between national tax systems, which are frequently exploited by aggressive tax planners.

Nonetheless, consolidation remains a firm goal and should be taken up by the Council as soon as the common base is agreed. Businesses need consolidation for the cross-border loss offset and to be able to file a single EU tax return through the One Stop Shop system. Member States need consolidation to eliminate the complex and cumbersome transfer pricing system as a key channel for profit shifting. They also need the apportionment formula in consolidation to ensure a fair link between where companies make their profits in the EU and where they are taxed.

What is cross-border loss offset, and how does it fit with the CCCTB?

One of the main attractions for businesses in the CCCTB is the capacity to offset losses in one Member State against profits in another. This is particularly important to support start-ups and business expansion in the Single Market, as it would ensure that their cross-border activities enjoy the same loss offset treatment as purely national activities. However, this benefit is tied to consolidation and will only apply in the second step of the CCCTB, i.e. when consolidation has been implemented.

Therefore, the Commission has proposed a temporary system of cross border offset, which will apply until consolidation is in force. With cross-border loss offset, a parent company in one Member State will be able to receive temporary tax relief for the losses of a subsidiary in another Member State. Once that subsidiary becomes profitable, the Member State in which the parent company is established will "recapture" the taxes that it relieved during the loss phase. As such, no Member State would have to carry the long-term burden of an unprofitable company in another Member State.

What is the R&D incentive in the CCCTB and how will it work?

Research and Development is a key driver of growth. However, the current average level of investment in R&D in the EU is below that of some other advanced economies. The CCCTB will support innovation in Europe by allowing the costs of R&D investment to be tax deductible. All companies that invest in R&D will be allowed to deduct the full cost of this investment plus an additional percentage of the costs, depending on how much they spend. The full cost of R&D will be 100% deductible, while an additional 50% deduction will be offered for R&D expenses of up to EUR 20 million. An additional 25% deduction will be allowed for R&D spending over EUR 20 million

Start-ups will be able to deduct even more. In addition to being able to deduct their full (100%) R&D costs, they will be allowed to deduct a further 100%. This should give a boost to young, innovative companies that are an important source of job-creation and help create more dynamic, competitive markets.

Example

A company spends €30 million on R&D in a given year. It will be allowed to:

Deduct the full costs from its taxable income	=	€30 million
An additional 50% for the first €20 million	=	€10 million
An additional 25% for the remaining €10 million	=	€2.5 million

In total, the company can deduct €42.5 million from its tax base, due to its R&D spending.

What is the Allowance for Growth and Investment (AGI) in the CCCTB and how will it work?

Currently, almost all national systems allow interest payments from debts to be deducted, but do not have a similar benefit for equity. This encourages companies to take on debt, which can make them more vulnerable to shocks and more prone to bankruptcy. This goes against the goals of the Capital Markets Union and makes the overall economy less resistant to shocks.

The Allowance for Growth and Investment aims to redress this debt-bias. It will allow a tax deduction for companies that choose to increase equity for financing (e.g. by issuing new shares or retaining profits) rather than take on debt (e.g. a loan).

The deduction will be calculated by multiplying the change in equity by a fixed rate, which is composed of a risk-free interest rate and a risk premium. Under current market conditions, the rate would be 2.7%. Companies will generally be allowed to continue these deductions for 10 years. This should encourage companies to seek diversified sources of financing and to tap capital markets. The Allowance is particularly beneficial for smaller companies that sometimes struggle to secure loans.

Example

A company starts using the common base in January of year X.

In the same year it issues €10 million worth of new shares to invest in new premises.

The AGI rate for the year X is 3% (the rate will change from year-to-year).

That year, the company can deduct an AGI allowance from its tax base of €300 000 = €10 million multiplied by 3%.

The company will also get additional allowances for the following 9 years after issuing this equity. The exact amounts of this allowance will depend on how the equity value develops.

Is the CCCTB a first step towards the harmonisation of tax rates?

No. The CCCTB is not about tax rates. Member States will continue to decide their own corporate tax rates, as is their sovereign right. What the CCCTB will do is create more transparency with regard to the effective corporate tax rate in Member States, thereby creating fairer tax competition within the EU.

2. DOUBLE TAXATION DISPUTE RESOLUTION MECHANISM

What is double taxation and what is its impact?

Double taxation occurs when two or more countries claim the right to tax the same income/profits of a company. It can occur, for example, due to a mismatch in national rules or different interpretations of a bilateral tax treaty with regards transfer pricing arrangements. There are estimated to be around 900 double taxation disputes ongoing in the EU today between Member States, under the current dispute resolution mechanisms. Double taxation is a major obstacle for businesses and can be very damaging. It creates uncertainty, high administrative and legal costs and cash-flow problems, particularly for smaller companies. It also undermines the fairness of the tax system if companies end up paying tax on the same income twice.

Why is the Commission proposing to improve the way double tax disputes are resolved?

Double taxation disputes are growing in both size and magnitude. There are mechanisms in place to deal with double taxation disputes, in particular the EU Arbitration Convention and bilateral tax treaties between Member States. However, the current mechanisms to provide binding resolutions have limited scope, covering mainly transfer pricing disputes. Fixed timeframes for resolving disputes are not always respected, and there is generally a need to improve the efficiency, effectiveness and legal certainty of the mechanisms in place today.

How is the Commission proposing to improve dispute resolution mechanisms?

The Commission has proposed a number of important changes to current mechanisms that should ensure that companies can rely on timely and decisive resolutions to double tax disputes. The proposal expands the scope of cases that will be covered by the dispute resolution mechanism. Companies will be allowed to access it when they have problems with double taxation for all corporate tax issues. It also sets clear deadlines for Member States to resolve double taxation disputes, to prevent companies from suffering long periods of uncertainty. Finally, it provides a way for taxpayers to move cases forward when they are blocked or prolonged. Member States will have to take conclusive and enforceable decisions under the improved dispute resolution mechanism, so that companies are guaranteed a solution to their double tax dispute.

How will it work in practice?

The company subject to double taxation can initiate a procedure whereby the Member States in question must try to solve the dispute amicably within two years.

If at the end of this period, no solution has been found, the Member States should set up an Advisory Commission to arbitrate on the case. If the Member States fail to do this, the taxpayer can ask the national court to do so. This Commission will be comprised of 3 independent members and representatives of the competent authorities in question. It will have 6 months to deliver a final, binding decision. This decision will be immediately enforceable and must eliminate the double taxation. Any company faced with double taxation of its profits, including SMEs, will be able to benefit from this improved dispute resolution mechanism.

How does this fit with international work on double taxation?

The approach proposed by the Commission today responds to the OECD recommendations on base erosion and profit shifting (BEPS), which call on countries to resolve double taxation disputes in a timely, effective and efficient manner. The OECD has set down minimum standards on mutual agreement procedures for double taxation disputes, which will be subject to peer reviews. This minimum standard does not, however, include a mandatory binding dispute resolution mechanism, and the OECD intends to develop that as a later step. The improved EU system proposed today can be an example of best practice in this respect.

3. ADDRESSING MISMATCHED RULES WITH NON-EU COUNTRIES

What are hybrid mismatches and why are they a problem?

Hybrid mismatches occur when countries treat the same income or entities differently for tax purposes. Companies can take advantage of these mismatches to deduct their income in both countries or to get a tax deduction in one country on income that is exempt from tax in the country of destination. Hybrid mismatches are frequently exploited by aggressive tax planners to minimise their tax bills.

What has the Commission proposed on hybrid mismatches?

The Anti Tax Avoidance Directive (ATAD), agreed in June 2016, deals with hybrid mismatches between Member States. The new rules mean that companies can no longer take advantage of mismatches in tax rules in different Member States to deduct their income in both countries or to get a tax deduction in one country on income that is exempt from tax in the country of destination.

Today's proposal tackles hybrid mismatches between Member States and non-EU countries. If a hybrid mismatch with a third country leads to double non-taxation, the company may have to pay tax on certain payments in the EU which it normally would not have to or may no longer be able to deduct certain payments.

ANNEX

CCCTB: An acronym explained

Common Corporate Tax Base – One single set of EU rules to decide how much of a company's profit will be taxed, once various exemptions and income deductions have been accounted for.

Example:

Member State A may allow assets to be depreciated over 10 years, for tax purposes, while Member State B might allow it as quickly as over five years. Or Member State A might allow all entertaining expenses to be tax deductible, whereas Member State B might not.

A common corporate tax base would mean that these rules would be the same throughout the EU, and companies only need to do their calculations based on one set of tax rules.

Without consolidation, the company would need to do a separate calculation and tax return for each Member State in which it has a taxable presence. However, this would still be easier than today, as the rules for this calculation would be uniform across all Member States.

Consolidation – All profits and losses from the companies of a group in different Member States would be added up, to reach a net profit or loss for the group's entire EU activity. Based on this net figure, the common rules would be used to decide the final tax base of the group.

Example:

A group consists of companies A, B, C and D, each in a different Member State.

Companies A and B have profits equal to €10 million each;

Company C has profit equal to €5 million;

Company D has a loss equal to €8 million.

The consolidated tax base (net profit) for this group is A+B+C-D = €17 million.

This tax base (i.e. the company's taxable profits) would then be shared out between the Member States in which the company is active, according to an agreed formula. Each Member State would tax their share of the profits at their own national rate

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Attachments

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