Attn Mr Gerassimos Thomas
Director General
DG TAXUD
European Commission
B-1049 Bruxelles

24 January 2024

Dear Mr Thomas,

Subject: PwC feedback to the European Commission's Proposal for a Council Directive "Business in Europe: Framework for Income Taxation" (BEFIT)

PwC International Ltd (PwC), on behalf of the PwC network, welcomes the opportunity to provide comments on the recently published Proposal for a Council Directive "Business in Europe: Framework for Income Taxation" ("the Directive").

PwC commends the policy goals of the European Commission to simplify and harmonise the business tax environment by introducing more common standards.

Executive Summary:

- We believe that simplification resulting in the kind of outcome desired by the Commission will not solely be achieved by the Directive. It is our view that the proposal does offer some simplification, but needs further consideration in light of the overall tax reform landscape.
- We think that the proposed implementation date in 2028 is too soon after the implementation of the Pillar Two rules and will not allow time for the impact and outcome of these rules to be fully understood.
- The Commission may wish to give further consideration to differences in the treatment of transactions or arrangements resulting from different financial reporting standards.

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- The Commission may wish to give further consideration to the allocation of profits to non-EU group members.

In the short Appendix to this letter, we outline some considerations which we feel require further thought at this stage of the legislative process. Our comments are influenced by our ongoing work with businesses and governments on the implementation of various tax reforms, particularly Pillar Two which represents the biggest tax change in a generation for both the business community and tax authorities. We observe businesses and tax authorities facing challenges with the Pillar Two rules and we are concerned that layering BEFIT on top of Pillar Two, very soon after the implementation of the latter, and without being able to fully understand the impact yet, may adversely impact the Directive's desired simplification outcomes.

We also acknowledge the public responses of three EU Member States with regard to the Directive - The Netherlands,[1] Sweden[2] and Finland[3] - and the reservations expressed by each jurisdiction in these publications.

We would welcome the opportunity to discuss these with you in further detail at your convenience.

Please reach out to me or Edwin Visser at the addresses below with comments or questions.

Yours sincerely,

William Morris
PwC Global Tax Policy Leader
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PwC IL is registered under number 60402754518-05 in the EU Transparency Register

[1] https://open.overheid.nl/documenten/dc837b31-4319-4913-b8cb-4e74e158c024/file
[2] https://www.regeringen.se/contentassets/e7970777eebc44e8a3c8420da088484c/direktiv-om-internprissattning-202324fpm9.pdf
[3] https://valtioneuvosto.fi/-/10623/hallitus-suhtautuu-varauksella-yritysten-tuloverotusta-euroopassa-koskevaan-befit-kehykseen

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Appendix

Simplification

The stated objective of BEFIT is to simplify the way in which large organisations compute and pay corporate tax in the EU. PwC agrees with the objective to reduce the tax compliance burden for businesses operating in the Single Market. It is our view that the proposal does offer potential simplification, but needs further consideration in light of the overall tax reform landscape.

To achieve this desired simplicity, we strongly believe that it will be necessary to ensure that BEFIT and the Pillar Two rules can coexist such that one set of rules does not produce results inconsistent with the other set of rules. The current challenge of implementing a series of complex Pillar Two rules is an ongoing concern among EU Member States. There is evidence of potential non-alignment in how the rules will be applied from jurisdiction to jurisdiction (through adoption of different policy choices, etc.). The Directive should ensure that BEFIT adjustments will not result in any increased Pillar Two top-up tax that is not already due under the Pillar Two rules (we understand it is suggested that a loss generated under the BEFIT rules could nonetheless be subject to a Pillar Two top-up tax in certain cases).

Also in relation to the goal of simplification, there is also uncertainty with regard to the formula related to profit allocation, as the Directive only provides for a pooling and allocation system during the 3-year period of the transitional phase. The review of the factors used and their weighting in the formula will only be possible after the transitional phase concludes, however there is a possibility that the transitional system becomes permanent. During the transitional phase the arm's length principle should be observed and safeguarded to ensure that the basis for pooling and allocation after the transitional phase ends is not vulnerable to scrutiny, given the potential upside of securing a maximum taxable result on a per country basis.

Timing

The release of this proposal coincides with the ongoing implementation of the Pillar Two rules across the EU Member States. Pillar Two represents a fundamental change in how business taxes by large organisations will be computed and paid. The new rules are incredibly complex for both businesses and tax administrations.

We believe that the proposed timeline of introducing BEFIT in January 2028 may be too soon, not leaving enough time for Pillar Two to be fully embedded across all Member States or for the full implication of those rules to be totally understood. The layering on of the proposed BEFIT Directive would only work if the proposed Directive, as noted above, can coexist with the Pillar Two rules, including in allowing local efforts to streamline business taxes. Streamlining the EU corporate tax system makes sense and would be helpful to businesses, but it needs to happen after Pillar Two has settled into the domestic tax systems of the Member States.

It is also important to note that there are currently five EU Member States who have elected to defer the execution of Pillar Two rules until 2030,[4] meaning that those tax authorities will not have had any experience with Pillar Two before the BEFIT rules are proposed to be effective in 2028. Additionally, the frequency with which businesses are expected to utilise the Pillar Two Transitional Country-by-Country Reporting safe harbour (indicative of the associated complexities with the rules) means that businesses will similarly not be fully applying the Pillar Two rules until 2027 at the earliest in many countries.

These two interlinked issues heighten our concerns regarding the timing of this proposal. Adding on a minimum of three years for businesses to file Pillar Two returns (18 months after the first relevant fiscal period) and allowing time for tax authorities to quantify the quantitative and qualitative impacts of the Pillar Two system (typically a year after returns filed, if not longer) leads us to believe that the implications of Pillar Two will not have become clear before BEFIT is proposed to be introduced. It would be hugely beneficial to evaluate the impact of Pillar Two first to better prepare for the implementation of BEFIT, and to hone in on the areas that require harmonisation.

<u>Accounting Framework Alignment</u>

We recommend considering whether the accounting frameworks that will underpin the BEFIT and Pillar Two proposals also require further alignment. There remain differences between IFRS and local generally accepted accounting principles (GAAPs) which will in turn result in different treatment of transactions and arrangements from a tax perspective once the tax system is pivoted to be closer aligned to the accounting treatment.

<u>Pricing transactions with non-EU group members</u>

The pricing of transactions with third countries poses the greatest challenge to simplification under this proposal. The traffic light system for risk assessing the arm's length nature of transactions with group members situated outside the EU, which derogates from the guidance laid down in the OECD transfer pricing guidelines, is extremely stringent and only leaves a narrow margin centred around the median of the range. Although the narrow margins should only be used as risk assessment, it will increase the scrutiny of taxpayers falling outside that range but inside an appropriate (full or interquartile) arm's length range, potentially leading to the unnecessary audit of those enterprises. While the intra-EU pricing under this proposal may lead to a degree of simplification, the increased disputes that will arise between the authorities of EU and third countries would create further complexity, uncertainty and increased costs for business.

[4] As confirmed by the Commission 12 December 2023, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C_202301536