EU tax proposals seek to harmonise corporate tax bases, apply formulary apportionment, further address hybrid mismatches and improve tax dispute resolution

23 November 2016

In brief

The European Commission (EC) published four new draft European Union (EU) Directives on 25 October 2016 with proposals to:

- harmonise corporate tax bases across each of the EU Member States, including a super-deduction for R&D costs and notional interest deduction for equity financing (Allowance for Growth and Investment), in the form of a **Common Corporate Tax Base (CCTB) Directive**
- consolidate the results of entities in a corporate group in the EU under a single filing and apportion the aggregate profits to individual Member States according to labour, assets and sales by destination via a **Common Consolidated Corporate Tax Base (CCCTB) Directive**
- introduce measures to address certain hybrid mismatches partly in relation to non-EU countries but partly more broadly by updating the Anti-Tax Avoidance Directive (ATAD), an amending document which we might call **ATAD II (hybrids)**, and
- extend existing double taxation dispute resolution mechanisms in the EU so that a taxpayer may ask its national court to set up an Arbitration Committee to deliver a binding decision within a fixed time frame under a **Dispute Resolution Directive**.

There are a number of detailed requirements that potentially could impact companies and groups. The CCTB and CCCTB Directive will be mandatory only for large groups. Others will be able to opt-in to the consolidation and single filing approach.

The CCTB may have different implications for individual companies and groups, as well as for Member States, in terms of revenue generation. However, Member States retain sovereignty to adjust their tax rates to compensate for lost revenue. The impact assessment and separate economic modelling suggest that the CCCTB could lift investment in the EU by up to 3.4% and growth by 1.2%.

The EC quotes estimates that businesses could cut their overall compliance time by 8% and costs by 2.5%, including, in particular, reducing time spent setting up subsidiaries by 62-67%.

In detail

A package of documents and communications

The four proposed Directives and their respective annexes were supplemented by additional documents and communications published on 25 October 2016. These encompassed a number of items on the package as a whole as well as more segmented elements.

Package as a whole:

- Overview: Corporate Tax Reform Package
- EC press release: Commission proposes major corporate tax reform for the EU
- Chapeau communication: Building a fair, competitive and stable corporate tax system for the EU
- Questions and Answers on the package of corporate tax reforms
- Fact sheet: Corporate tax reform – pro-business; anti-avoidance #FairTaxation

Additional CCTB/ CCCTB communications:

- CCTB/ CCCTB impact assessment (158 pages) and CCTB/ CCCTB summary impact assessment (4 pages)
- Video: CCCTB – it's good for Europe

Additional ATAD II (hybrids) communications:

- Commission Staff Working Document (partial impact assessment) as regards hybrid mismatches with third countries

Additional dispute resolution communications:

- Overview: Resolution of double taxation disputes in the European Union
- Dispute resolution impact assessment (135 pages) and Dispute resolution summary impact assessment (4 pages)

It is no coincidence that three new related background working papers were also published on the same day. The findings of these studies are reflected in the impact assessment on CCTB/ CCCTB:

- Taxation paper No 66: modelling corporate tax reform in the EU: New calibration and simulations with the CORTAX model written by Joint Research Center of the European Commission – IPTS
- Taxation paper No 65: The Effects of Tax Reforms to Address the Debt-Equity Bias on the Cost of Capital and on Effective Tax Rates written by Centre For European Economic Research (ZEW) Gmbh
- Taxation paper No 64: The Impact of Tax Planning on Forward-Looking Effective Tax Rates written by Centre For European Economic Research (ZEW) Gmbh

Economic perspective and background

The importance of tax certainty in promoting investment and growth has recently been recognised by the G20 leaders, and has become the new global focus. This is reflected in EC comments in a number of the documents.

The EC sets the package against a backdrop of the need for corporate taxation that:

- provides stable revenues for public investment and growth- friendly policies
- ensures that all businesses enjoy a level playing field, legal certainty and minimal obstacles when operating cross-border, and
- is part of a wider tax system in which citizens have confidence, because it is fair and meets society's socio-economic needs.

The EC describes the package as a more holistic, longer-term framework for corporate taxation in the EU. It suggests that elements of the package will help create a more predictable environment for business. However, there is a strong anti-avoidance message, which wasn't present when the CCCTB was first discussed more than a decade ago.

The EC formally proposed a Directive for a CCCTB in 2011, but that has since been pending in Council. The Directive aimed to provide companies and groups with the option for a single set of corporate tax rules for doing business across the internal market. This would include a single filing in one Member State and automatic loss offsets in one Member State with profits in another Member State. Council discussions have shown that the 2011 CCCTB Proposal, amended to incorporate some key anti-avoidance measures, would not likely be adopted in its entirety without a staged approach. A summary of the main differences between the 2011 proposals and the current proposals is in the appendix to this document.

In the EC's 2015 Communication on an Action Plan for a Fair and Efficient Corporate Tax System in the EU, the EC advocated a step-by-step approach. The first step could be regarded as the adoption of the Anti-Tax Avoidance Directive (ATAD) in July 2016. The adoption of rules for a

CCTB that is mandatory for large groups but optional for others is the second step. Third is the adoption of the CCCTB, the EC's ultimate goal in this regard. Again, the CCCTB would be mandatory for large groups but optional for others. Key differences between the CCTB and the CCCTB, which only arise with the CCCTB in the final step are:

- the cross-border consolidation of profits and losses
- the elimination of intra-group transactions (and the need for transfer pricing in transactions between Member States), and
- the 'one-stop shop' element of being able to file a single tax return for all EU activities.

The 2011 CCCTB Proposal is withdrawn with the EC's adoption of the new CCTB and CCCTB proposals. Note that, whereas the ATAD is a minimum standards Directive, the current CCTB and CCCTB proposals are more prescriptive and set absolute rules.

Although described as a package, the four Directives put forward on 25 October are all potentially standalone pieces of legislation, with different proposed time lines. The CCTB is seen by the EC as a step towards a CCCTB. However, it is not inconceivable that Member States may agree to the former but then reject the latter. Our network of EU firms has indicated informally that, in their States, there appears to be greater expectation that a form of CCTB may be adopted than that there will be significant backing for a CCCTB.

CCTB Directive

The proposal is for the introduction of a common tax base, effective 1 January 2019 (Article 70). That is one year earlier than had been discussed in the run up to the draft's publication.

Article 4 contains a number of definitions that apply in determining scope, principles and specific content.

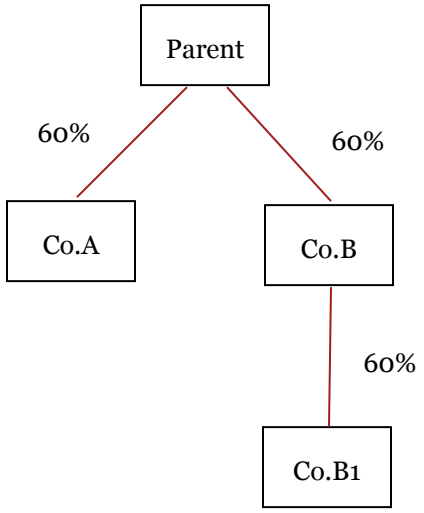
Rules on entering and leaving the system of the tax base (Articles 43-52) apply to any transition on introduction of the regime or for the movement of particular companies.

Scope

The CCTB would be mandatory for a company (of the form listed in Annex I) that is established in any Member State provided it is subject to a corporate income tax (of the type listed in Annex II) and is a member of a large group. It also applies to a permanent establishment (PE) in the EU of a similar type of company established outside the EU that is a member of a large group. The size criterion for this purpose is a 'consolidated group for financial account purposes' (as defined by reference to IFRS or national GAAP) with annual turnover in excess of €750m, irrespective of the size of its EU operations. The definition of a PE in the EU here largely follows the BEPS definition, with the 'auxiliary or preparatory' exclusion applicable to each of the 'exempt activities' (Article 5 - the third-country dimension for PEs is thus left to be dealt with in bilateral tax treaties and national law). A group, defined by reference to a parent company and qualifying subsidiaries, refers to (Article 3):

- entitlement to exercise more than 50% of voting rights (establishing such level of rights over an intermediate subsidiary enables 100% of its voting rights in its subsidiaries to be counted in this test as regards the lower-tier subsidiary), and
- ownership of more than 75% of capital or rights to profits (multiplying out indirect holdings).

For example, consider the following structure. If the 60% relates to voting rights, Parent is regarded as entitled to exercise 60% of the voting rights in Co.B1. If the 60% relates to ownership of capital, Parent is regarded as owning only 36% of Co.B1.



A company that falls within the mandatory criteria is required to notify the competent authority of the Member State in which it is tax resident or in which its PE is situated that it is within scope.

All other companies could opt-in to the CCTB for an initial five-year period. This option is automatically renewed for successive five-year periods unless the taxpayer opts out. However, the taxpayer would have to prove it is still within Annex 1 and II as a 'company' subject to a listed corporate income tax (Article 65).

Principles of the tax base and timing

Items are to be recognised on an accruals or incurred basis, unless specifically stated (Articles 15-28). Rather than relying on accounting principles, there are prescriptive rules for when matters are accrued or incurred and valuation (including mark-to-market for financial assets and liabilities held for trading). There are also specific measures for a

number of items such as stocks and work-in-progress, long-term contracts, pension deductions (with Member State flexibility), bad debt deductions, hedging, etc.

The tax base is broadly defined as 'revenues' less (Article 7):

- 'exempt revenues'
- 'deductible expenses' (including the R&D super-deduction), and
- 'other deductible items', mainly different tax depreciation amounts (see below),

Although there are then specific provisions, also considered in more detail below, which:

- exclude certain items as 'non-deductible expenses'
- include the 'Allowance for Growth and Investment', and
- limit the deductibility of interest (in a slightly different way than described in ATAD).

Subject to particular exceptions, the calculation would be performed for each 12-month period on a consistent basis with items measured individually and recognised only when realised (Article 6).

Revenues – Includes monetary and in-kind receivables, net of VAT and other duties collected on behalf of government agencies, but not equity raised by the taxpayer or debt repaid to it.

Exempt revenues - The list of exemptions (Article 8) comprises only five items. The main items provide a dividend and capital gains participation exemption at the 10% shareholding/voting rights level and exclude PE profits (regardless, it seems, of whether the PE is in an EU or non-EU country) in the head office state. However, notwithstanding failure to reach consensus on its inclusion in ATAD, there is a switchover clause (Articles 53, 54) to prevent exemption and apply instead a tax credit relief method where the tax rate of the host third (non-EU) country is less than 50% of the statutory tax rate that the company would have been subject to in the home country on such foreign income. The mechanism for PEs is not clear as the derogation from exemption mentioned refers only to points (c) and (d) of Article 8 which relate to profit distributions and share disposals.

Deductible expenses – Decreases in net equity, other than distributions, are limited to those incurred in the direct business interest of the taxpayer with few exceptions (Article 9). A Member State has the option to allow gifts and donations to charitable bodies. In a slightly odd formulation of the rules, this article also deals with the super-deduction for R&D costs (as further discussed below). Also, there are specific items which are stated as 'non-deductible expenses' (see also below).

Research and development (R&D)

On top of the amounts already deductible for R&D, an extra 50% of R&D costs each tax year may be deducted for amounts up to €20m. For R&D costs at €20m or above, taxpayers will be able to deduct 25% of any costs above this threshold. Furthermore, an enhanced 100% super-deduction for R&D costs up to €20m is granted for start-up companies (non-listed companies that have been registered for no longer than five years, have no associated enterprises, employ fewer than 50 people and have an annual balance sheet total not exceeding €10m).

R&D is defined by reference to basic research, applied research and experimental development, largely consistent with existing frameworks in the EU.

Allowance for Growth and Investment

An 'Allowance for Growth and Investment' (AGI) grants deductions for increases in equity, within limits, to avoid abuses and tax planning (Article 11).

AGI is defined as the difference between a taxpayer's equity and the tax value of its participation in the capital of 'associated enterprises', as defined by reference to participation in management or, at the 20% level, in, control or capital (Article 56). An amount equal to the notional yield on the AGI equity base increase will be deductible from the taxpayer's taxable base under certain conditions (the yield rate would vary on European Central Bank figures but, as an example, the proposal indicates that a current rate might be 2.7%). Should the AGI equity base decrease, an amount equal to the notional yield of the AGI equity decrease shall become taxable.

These rules aimed at the debt-equity bias in most EU Member States appear inspired by Italy's and other States' notional interest systems, with anti-abuse measures to focus on intra-group loans and loans involving associated enterprises; transfers of participations; re-categorisation of old capital as new capital through liquidations; and the creation of start-ups or subsidiaries and acquisitions of businesses held by associated enterprises.

After the first ten tax years, the reference to the amount of AGI equity base that shall be deductible against the AGI equity base at the end of the relevant tax year shall annually move forward by one tax year.

The cost of introducing AGI would be considerable and tax administrations may wish to consider carefully the revenue loss. The rationale is still not universally accepted. Purely looking at

the jurisdiction in which an investment is made, it appears logical and potentially attractive to encourage equity rather than borrowing. But at the investor level, interest is generally taxed whereas dividends are, in many cases, exempt or carry some form of credit. Therefore giving credit for equity may provide a mismatch in treatment between the investor and investee. This may be more pronounced in highly leveraged areas such as private equity and real estate where interest limitation rules are likely to be significant.

Interest limitation rule

The main thrust of the rules (Article 13), which would allow the deduction of 'borrowing costs' and the limitation of 'exceeding borrowing costs' is similar to that set out in ATAD. However, it is in particular more prescriptive (without the flexibility currently allowed for Member States) and there is no group ratio rule. Note that 'expenses incurred by the company for the purpose of deriving income' that is exempt under the participation exemption and PE profits, mentioned above, would not be deductible. It is unclear whether this would extend to all financing costs.

The rules propose a specific deduction for borrowing costs, defined by reference to interest on various forms of debt and other economically equivalent costs (including the AGI) up to the amount of the interest or other taxable revenues from 'financial assets' received by the taxpayer. Defining financial assets by reference to investments, including those in associated enterprises and own shares in certain circumstances, ought to suffice for determining net interest expense. However, by way of duplication but potentially introducing different interpretations, 'exceeding borrowing costs' is separately defined. That is the amount by which the deductible borrowing costs of a taxpayer exceed taxable interest revenues and other taxable revenues that the taxpayer receives and which are economically equivalent to interest revenues.

Those exceeding borrowing costs are then subject to the similar limitation expressed in ATAD but in a more straightforward fashion as deductible in the tax year in which they are incurred up to the higher of 30% of EBITDA or €3m.

Carryforwards of unused excesses are unlimited, but there is no carry back nor provision for unused capacity.

The rules would still reference the limitation applying to a whole group where an entity is permitted or required to apply rules on behalf of a group (now as defined in relation to the rules of a national group taxation system rather than according to national tax law). However, the rules would no longer reference similar treatment for an entity in a group which is not required to consolidate its members' results for tax purposes.

A stand-alone company (no longer a stand-alone entity, an entity now defined as any legal arrangement to carry on business through either a company or a structure that is transparent for tax purposes), which is not part of a 'consolidated group for financial accounting purposes' and has no associated enterprises or PEs, would have no restriction on deducting its exceeding borrowing costs. Consolidation would now mean for the purposes of IFRS or a national financial reporting system (with apparently less flexibility for Member States to allow reference to other accounting standards).

Also, 'financial undertakings' would not be subject to the interest limitation rules and no longer left to the discretion of Member States, as currently provided.

Tax depreciation

Tax depreciation rules (Articles 30-40) include requirements that assets on which a deduction is claimed must be properly registered and depreciable and must not constitute 'financial assets' (see interest above). Buildings qualify, which is not currently the case throughout the EU. Assets like land, art, antiques, and jewellery are subject only to exceptional write-offs and adjustments.

Tax depreciation would be calculated at 25% per year on a reducing balance basis for a main pool of assets. The pool comprises all qualifying assets that are not separately depreciated. This is similar to the previous proposal, but medium-life fixed tangible assets have been removed from the pool system to be depreciated individually. Acquisition or construction costs and asset improvement costs would be added to the depreciation base; the proceeds of an asset disposal and any compensation received for an asset loss or destruction would be deducted.

The following are separately depreciated on a straight-line basis over the periods specified:

- industrial buildings and structures: 25 years
- other immovable property, including commercial, office and other buildings: 40 years
- other long-life fixed tangible assets: 15 years
- other medium-life fixed tangible assets: 8 years;
- fixed intangible assets: the period for which the asset enjoys legal protection or for which the right has been granted or, where that period cannot be determined, 15 years.

Second-hand assets are treated similarly, although the period is reduced for assets with shorter useful lives, etc.

A taxpayer may not disclaim tax depreciation (unlike certain regimes, such as in the UK).

There are rules that identify who may claim the depreciation and when, what happens when assets are directly replaced, and how to deal with subsidies, gifts, etc.

'Non-deductible expenses'

There would be a category of expenses specifically referred to as 'non-deductible expenses' listed in Article 12:

a) profit distributions and repayments of equity or debt

b) 50% of entertainment costs, up to an amount that does not exceed [x] % of revenues in the tax year

c) the transfer of retained earnings to a reserve that forms part of the company's equity

d) corporate tax and similar taxes on profits

e) bribes and other illegal payments

f) fines and penalties, including charges for late payment, that are due to a public authority for breach of any legislation

g) expenses incurred by a company for the purpose of deriving exempt income

h) most gifts and donations

i) acquisition or construction costs or costs connected with the improvement of assets attracting tax depreciation, and

j) losses incurred by a PE in a third (non-EU) country.

Exit taxation

An amount equal to the market value of transferred assets, at the time that the assets exit, less their value for tax purposes, would be treated as accrued revenues (Article 29) to the same extent as is the case under ATAD.

However, there is no proposed deferral and payment in instalments as there is under paragraph 2 of Article 5 to ATAD.

Losses

If a company incurs a tax loss in a particular year (or has a PE in the EU that does so), the loss may generally be carried forward and deducted in subsequent tax years but may not create a loss for that year (Article 41). Losses are used on a first-in, first-out (FIFO) basis.

Under the CCTB (as a temporary measure pending the CCCTB) there is provision for a mechanism of cross-border loss relief within the EU with subsequent recapture (Article 41). This only applies in relation to a company and a loss in its immediately qualifying subsidiary (as per the scope above) or its PE. The wording is currently unclear as to whether 'situated in other Member States' refers only to PE or also to an immediate subsidiary; however, the EC's communications suggest it is only a cross-border relief. The Q&A document in particular states:

"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."

A company has to deduct its own losses first. This reduction of a taxpayer's tax base may never lead to a negative amount. The recapture takes place after five years or earlier as and when the subsidiary/ PE has profits or that entity is sold (or certain other events).

There is no provision in the CCTB Directive for any kind of tax consolidation or group relief other than this cross-border element. So there is no specific reference to domestic relief between one group company and another in the same Member State. However, it is understood that the EC's view is that existing domestic provisions in this regard would continue where they exist. The CCTB directive stipulates that "A company that applies the rules of this Directive shall cease to be subject to the national corporate tax law in respect of all matters regulated by this Directive" (Article 1). It is uncertain whether this would suffice to let Member States continue allowing their domestic provisions. There is reference to the treatment of an entire group as a taxpayer in relation to interest limitation where one company acts on behalf of a group, but there is no corresponding provision here.

There is also an anti-abuse provision regarding the purchase of loss-making companies. Carryforward losses cannot be relieved if the taxpayer becomes a qualifying subsidiary of another company and there is a major (60%) change in its activities and turnover.

Transfer pricing and attribution of profit to PEs

There are very brief but specific references (Article 57) that bring into question the positioning of the CCTB in relation to the OECD standards on transfer pricing and profit attribution.

"Where conditions are made or imposed in relations between associated enterprises that differ from those that would have been made between independent

enterprises, any income that would have accrued to the taxpayer but because of those conditions has not so accrued, shall be included in the income of that taxpayer and taxed accordingly."

Enterprises are associated for this purpose in the same way as for AGI, i.e., by reference to participation in management or, at the 20% level, in, control or capital. This has particular significance where existing benchmarks currently in place are based on a 50% threshold.

"Income attributable to a permanent establishment is what the permanent establishment would be expected to earn, in particular in its dealings with other parts of the same taxpayer, if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the functions performed, assets used and risks assumed by the taxpayer through the permanent establishment and through other parts of the same taxpayer."

GAAR, CFC and hybrid rules

A General Anti-Abuse Rule (GAAR) is included, allowing tax authorities to ignore arrangements where the essential purpose is to obtain a tax advantage that defeats the object or purpose of the tax provision and where the arrangements are not regarded as genuine (Article 58).

The GAAR is supplemented by a switch-over clause (as noted in relation to exempt revenues) and CFC rules similar to (but not the same as) the ATAD CFC rules (Article 59).

Hybrid and tax residency mismatch rules apply to mismatches between Member States and mismatches involving a third (non-EU) country (Article 60). They target differences in legal characterisation of financial instruments or entities, tax residency, and the treatment of a commercial presence as a PE. In brief, the provisions establish rules whereby one of the two jurisdictions party to a mismatch shall deny the deduction of a payment or ensure that the corresponding income is included in the corporate tax base.

CCCTB Directive

The EC proposes that Member States apply the CCCTB from 1 January 2021. The CCCTB is an approach to apportioning to EU Member States, according to a formula based on sales, people and assets, the consolidated results for companies in a group across the EU as a whole. The CCCTB would be mandatory for large companies (MNCs with turnover in excess of €750m), and optional for other companies. This approach would automatically offset losses and profits within the group, make transfer pricing unnecessary for transactions between them and provide a single point of tax administration.

Making it mandatory for large groups rather than providing optionality as with the 2011 CCCTB Proposal will help to create a more predictable environment, the EC states, though it also mentioned maximising its potential as an anti-avoidance tool. It would remain optional for other, smaller companies and groups, thus, they claim, making it easier to grow in the EU. The EC also refers to the consultation with Member states, businesses, civil society and the European Parliament which resulted in:

"bolstering the pro-business elements … to help cross border companies cut costs, red tape and to support innovation".

Taxpayers are likely to be divided over the potential advantages and disadvantages of such a move. Tax administrations would benefit from fewer dealings with transfer pricing issues and a reduced number of cases to the extent that a company's tax affairs are mainly handled by the administration of the Member State where the parent resides. On the other side, as long as the CCCTB is not mandatory for all firms, national administrations will experience additional compliance costs due to the required maintenance of two parallel systems.

The impact assessment notes that the proposal's expected economic benefits are positive. It further says that the CCCTB would lead to an increase in investment and employment of up to 3.6% and 0.5%, respectively. Overall, the EC claims that growth would increase by up to 1.3%. Compliance costs would, the EC expects, decrease (10% in compliance time and 2.5% in compliance costs). The cost of setting up a subsidiary would decrease by up to 67%, making it easier for companies (including SMEs) to go abroad. The EC suggests that

"based on these time reductions, one could endeavour a rough calculation of the order of total cost savings that would result under the CCCTB - if 5% of medium-sized companies expand abroad, a one-off cost saving of around EUR 1 billion could be expected. If all multinational entities apply the CCCTB recurring compliance costs could go down by about EUR 0.8 billion."

Rules on entering and leaving the system of the tax group (Articles 11-21) apply to any transition on introduction of the regime or to the movement of certain companies. In particular, pre-consolidation trading losses will be carried forward to offset its apportioned share. When a company leaves the group, no losses incurred during the consolidation period will be allocated to it.

Scope

The scope of the CCCTB is the same as the scope of the CCTB, above. Broadly, it would be mandatory for an EU company, or a PE in the EU of a non-EU company, that is a member of a large group for accounting consolidation purposes with a turnover in excess of €750m, irrespective of the size of its EU operations (Article 2).

A group (for CCCTB tax consolidation purposes) comprises broadly those companies that are EU 'resident taxpayers', or PEs situated in the EU of companies where one is the parent and the others are its qualifying subsidiaries or they are qualifying subsidiaries of a common third (non-EU) country parent. (Article 6).

An equivalent two-part test for a qualifying subsidiary, based first on control (more than 50% of voting rights) and second on ownership (more than 75% of equity) or rights to profits (more than 75% of rights giving entitlement to profit) determines the extent of the consolidated tax group (Article 5 – see also for CCTB). Article 8 covers the timing of the tests. In particular, taxpayers must meet these thresholds throughout the tax year. Otherwise, the failing company will leave the group immediately. Furthermore, taxpayers must meet these thresholds for at least nine consecutive months as a minimum requirement. Failing this, a taxpayer shall be treated as if it had never been a group member, in order to tackle taxpayer manipulations of the tax results.

Many business segments will want to closely examine the definition of the group for this purpose. For example, formulary apportionment applied to a wide range of investments by funds, etc., where one investment's tax position is impacted by the activities of another would potentially give rise to commercial considerations. It will be interesting to see whether the EC could specifically recognize this as it has been discussed in relation to interest deductibility.

Tax residence

A resident taxpayer would be subject to corporate tax on a global basis while a non-resident taxpayer would be subject to corporate tax on all income from an activity carried on through a PE in a Member State (Article 3). In this case, residence is defined by reference to registered office, place of incorporation or place of effective management subject to treaty, and a dual residence tie-breaker that uses place of effective management.

Effects of consolidation

Aggregation for apportionment

The tax bases of all group members would be added together into a consolidated tax base. Any positive amount would be apportioned to those members in accordance with the prescribed formula (Article 7). If the consolidated tax base is negative, the loss would carry forward and offset the next positive consolidated tax base. An interest limitation rule applies to the group as it would a single taxpayer, with the sole compromise of substituting the €3m threshold for one of €5m (Article 69). There are consequential adjustments to the switch-over, CFC and hybrid mismatch rules when applying them to the group (Articles 72-74).

Intra-group transactions

Groups would have to apply a consistent and adequately documented method for recording intra-group transactions, so that profits and losses arising from intra-group transactions could be ignored when calculating the consolidated tax base (Article 9). Any change in method could be applied from the beginning of a tax year, but only for valid commercial reasons.

Withholding taxes

No withholding taxes or other source taxation will be imposed on intra-group transactions (Article 10). The proceeds of withholding taxes charged on interest and royalty payments would be shared according to the formula apportionment of that tax year (Article 26). Withholding taxes charged on dividends would not be shared since, contrary to interest and royalties, dividends are distributed after-tax and do not lead to any previous deduction borne by all group companies.

Administration

The 'principal taxpayer', usually the EU parent of a group or designated subsidiary of a non-EU parent but potentially a single PE, would file the consolidated tax return of the group with the 'principal tax authority', which is its home tax administration by residence. The various processes proposed would hinge on that relationship (Article 46-68). This one-stop-shop approach would apply to the various reporting requirements when a group is formed, through to court appeals, debt enforcement provisions, etc. The principal tax authority co-ordinates activities including the audit initiations, although any competent authority may initiate an audit. In exceptional circumstances, relevant Member States may collectively override the group's designation of the principal company. Member States would be bound by secrecy with regard to information under the CCCTB Directive in the same way as they would for similar information under domestic law, with some specific references to use of the information. The EC may decide in due course on the form of filing, including whether it is electronic.

Apportionment

The consolidated tax base for each tax year would be apportioned to the members of the group.

Equal weight would generally be given to the factors of sales by destination, labour and assets. The labour factor is itself split equally according to payroll and number of employees (Article 28). An alternative method can be used if the principal taxpayer and affected competent authorities agree (Article 29). The Member State of the principal tax authority would then have to inform the EC about the alternative method used.

There are rules to determine the composition and allocation of each of the three factors (Articles 32-38):

- The **number of employees**, as defined by domestic law, would be determined at the year end and includes quasi-employees. **Payroll costs** would be the amounts deductible for salaries, wages, bonuses and all other employee compensation, including related pension and social security costs borne by the employer.
- The **asset** factor would include the average of the tax written-down value of all fixed tangible assets owned, rented or leased, giving preference to economic ownership over legal ownership.
- **Sales** would mean the proceeds from all sales of goods and supplies of services after discounts and returns, excluding value added tax, other taxes and duties. The rules would give preference to the group member located in the Member State where the dispatch or transport of the goods to the person acquiring them ends.

When a company joins or leaves a group during the tax year, its factor in the apportionment is reduced pro-rata to reflect the number of months it has been in the group during that year (Article 30).

Business reorganisations

A business reorganisation, undefined except by reference to a series of specific measures, is to be largely tax-neutral except as set out below (Article 22). Where a business reorganisation (or a series of transactions within a two-year period) results in the transfer of substantially all the assets of one group member to another, they remain in the transferring company's asset factor rather than the transferee's for up to five years. This is subject to conditions, including a group member continuing to be the economic owner of the assets.

Contrary to the 2011 CCCTB proposal, in reorganisations where more than one company has to leave a loss-making group, the rules introduce a fixed threshold to determine the conditions under which companies will no longer leave a group without losses. Instead the rules allocate a loss across the consolidated group (Article 23).

ATAD II (hybrids) Directive

The EC proposes that revised anti-hybrid rules will apply effective 1 January 2019. This amending Directive (essentially a single substantive article) would replace the existing definition of 'hybrid entity' in paragraph (9) of Article 2 ATAD and the counter action in Article 9 ATAD. This would extend the scope of ATAD including bringing third (non-EU) country circumstances into scope. This would broadly align it with the recommendations under the BEPS Action 2 report.

Remember that ATAD's 'hybrid mismatch' meaning was restricted to a double deduction or deduction without inclusion involving a taxpayer in one Member State and an associated enterprise in another Member State, or a structured arrangement between parties in Member States. The counter action was then extremely brief:

"1. To the extent that a hybrid mismatch results in a double deduction, the deduction shall be given only in the Member State where such payment has its source.

2. To the extent that a hybrid mismatch results in a deduction without inclusion, the Member State of the payer shall deny the deduction of such payment."

The EC would replace the meaning of 'hybrid mismatch' with a new definition. This definition would reference a situation between a taxpayer and an 'associated enterprise' or a 'structured arrangement' between parties in different tax jurisdictions where any of a set of listed outcomes is attributable to differences in the legal characterisation of a financial instrument or entity, or in the treatment of a commercial presence as a PE. The Directive would extend the listed outcomes to refer, for PEs, to non-taxation without inclusion. There would be a specific carve-out for amounts that give rise to matched income. Thus, a hybrid mismatch would arise only to the extent that the same payment deducted, expense incurred or loss suffered in two jurisdictions exceeds the amount of income that is included in both jurisdictions and which can be attributed to the same source. In addition, transferring a financial instrument under a structured arrangement that results in deduction -- without inclusion of the derived income or double withholding tax relief -- would also be regarded as a hybrid mismatch.

The term 'structured arrangement' was not originally defined in ATAD.

This would change to refer to pricing the mismatch into its terms or designing it to produce a hybrid mismatch outcome, unless the taxpayer or an associated enterprise could not reasonably have been expected to know about the hybrid mismatch, and did not share in the hybrid mismatch's tax benefit.

The definition of 'associated enterprise' (in paragraph (4) of Article 2 ATAD) is effectively extended to include, for financial accounting purposes, an entity that is part of the same consolidated group as the taxpayer. This is similar to the definition used for CCTB/ CCCTB, exception that here it refers to *the* national GAAP rather than *a* national GAAP. However, a Member State may allow a taxpayer to use other accounting standards. Furthermore, either the taxpayer would have a significant influence in the enterprise's management or the enterprise's management would have a significant influence in the management of the taxpayer.

The counter action now refers to rules which broadly would:

- for a double deduction, deny the deduction in the:
  - taxpayer's Member State, if the arrangement is with a third (non-EU) country that has not already denied the deduction, or
  - Member State which is not where the payment is sourced (or the expenses incurred or the losses suffered), if the arrangement involves two Member States, or
  - taxpayer's Member State, if the taxpayer makes the payment to an associated enterprise which results in an 'imported mismatch' involving two third (non-EU) countries, which have not already denied the deduction.
- for a deduction without inclusion, deny the deduction or include the income as follows:
  - deny the deduction in the payer's Member State, if the arrangement involves two Member States, or
  - deny the deduction in the Member State if that is the payer's state under an arrangement with a third (non-EU) country or, if that country is the payer and has not already countered, include the income in the Member State, or
  - deny the deduction in the taxpayer's Member State for a payment to a third (non-EU) associated enterprise, if the payee can offset, via an imported mismatch, a corresponding payment without it being included income (unless a third (non-EU) country has already denied a deduction for that corresponding payment).
- for PE non-taxation without inclusion, include income in the tax base:
  - of the head office (as the residence of the taxpayer) rather than adjusting the non-taxation in the host state, if the arrangement involves two Member States, or
  - of the head office (taxpayer), if the arrangement involves a PE in a third (non-EU) country.

If a mismatch on a transferred financial instrument provided withholding tax relief to more than one party, the taxpayer's Member State would be required to limit the benefit in proportion to the resulting net taxable income.

Where there is a mismatch involving an entity that is dual resident in a Member State and a third (non-EU) country, the Member State should deny the deduction of a payment to the extent that the payment offsets an amount that is not treated as income under the laws of the other jurisdiction (i.e., against income that is not dual inclusion income). New Article 9a ATAD would stipulate:

"To the extent that a payment, expenses or losses of a taxpayer who is resident for tax purposes in both a Member State and a third country, in accordance with the laws of that Member State and that third country, are deductible from the taxable base in both jurisdictions and that payment, those expenses or losses can be set-off in the Member State of the taxpayer against taxable income that is not included in the third country, the Member State of the taxpayer shall deny the deduction of the payment, expenses or losses, unless the third country has already done so."

Dispute Resolution Directive

The EC proposes that Member States should be required to bring these new dispute resolution procedures into force by 31 December 2017.

The EC notes that "One of the biggest tax obstacles to the Single Market is double taxation." It quotes estimates of 900 double tax disputes ongoing in the EU worth €10.5bn. If Member States don't agree how to resolve a cross-border dispute, the EC proposes allowing the taxpayer to ask its national court to create a committee to arbitrate a decision. This overcomes existing problems by virtue of being:

- broader than the transfer pricing/ PE cases that currently are potentially within the Arbitration Convention
- final and binding, and
- within a fixed timeframe.

The mechanism would apply to any EU-resident taxpayer or to any PE situated in the EU, in relation to the business income taxes listed in Annex I (Article 1).

Any taxpayer subject to 'double taxation' – whether additional tax, an increase in liabilities or reduction – would be able to request, within three years from receipt of the first notification of the action resulting in double taxation, the resolution by each of the Member States concerned (Articles 2 and 3). The taxpayer could still pursue the remedies available in the national law of any of the Member States concerned. The relevant tax authorities have, from the date of complaint:

- one month to acknowledge the complaint with the taxpayer and other Member States
- two months to request additional information from the taxpayer beyond the basic information that it must initially supply; this information includes details of the domestic and treaty rules applicable
- six months to inform the taxpayer and other Member States of the complaint's admissibility (appealable to national courts in each State).

Member States may reject the claim on a number of grounds (Article 5). If only one State rejects it, the relevant tax authorities would be required to set up an Advisory Commission within 50 days. They would have six months to judge the claim's applicability, otherwise it would be deemed to be rejected (paragraphs 1 and 2 Article 6). The Advisory Commission should include a chair and two representatives from each tax administration, plus an independent from an appointed panel of 'experts' from an EC list and a reserve. The taxpayer may refer any failure to appoint experts to a national court (Articles 7 and 8).

If the Member States accept the claim directly, they would then endeavour to eliminate the double taxation by mutual agreement procedure (MAP) within two years of notification from the last Member State involved. This time period could be extended by six months if all agree (Article 4). If the Advisory Commission accepts it, the two years runs from their decision. If the MAP fails to reach a decision, the competent authorities must specify the reasons why.

If the MAP fails, the Member States could, in order to judge the elimination of the double taxation, establish either:

- an Advisory Commission, as above (paragraph 3 Article 6), or
- an Alternative Dispute Resolution Commission to apply conciliation, mediation, expertise, adjudication or any other dispute resolution processes (Article 9).

Each body has 50 days to agree 'Rules of Functioning' (Annex II) and a date, no longer than six months hence, for reaching a decision (Article 10). There are rules for cost-sharing by the States (the taxpayer bears its own) and evidence, hearing, etc. (Articles 11-13). From the date the written opinion is given, the States have six months to agree an alternative resolution, otherwise the opinion will stand (Article 14). The states have an additional 30 days to inform the taxpayer.

The States would be required to publish the final decision or, if the taxpayer objects, an agreed abstract which excludes any commercially sensitive information (Article 16).

The takeaway

Some companies and multinational groups will see many potential benefits in this tax package. The estimated incremental growth across the EU would be welcomed, but this may not be evenly spread across Member States. Many of the MAP elements would be developments that businesses may warmly receive, although there may be some reluctance to enter into the new MAP where there is an obligation to publish the arbitration results. The prospect of simpler compliance with a single tax return, automatic loss offset and other longer-term compliance savings like transfer pricing work may be attractive to some multinationals and tax administrations. However, others may be wary of the immediate compliance impact of adapting to a new tax base and the effects of a formulary apportionment methodology, which could create new interpretational issues and uncertain tax liabilities.

There remains a strong undercurrent of anti-avoidance in many of the proposals. The Q&A document suggests that the mandatory nature of the CCTB/ CCCTB for large companies is aimed at those with the greatest capacity to carry out aggressive tax planning. The proposal will lead to unequal treatment of companies above and under the threshold; some tax administrations may be concerned about the resources required to maintain these two alternative methodologies for the CCTB and the national tax system. Consideration will be necessary to determine whether the proposal could also impact a Member State's national tax system on the basis that non-

discrimination rules may not allow a more advantageous domestic system.

For those applying the regime, rudimentary rules would replace well-developed case law and guidance on things like when to report a profit for tax purposes, when to realise a profit and when to take losses into account. Well-developed and sophisticated participation regimes would be replaced by a more basic standard (generally with a higher threshold). There would be considerable uncertainty and lack of clarity. In addition to basic implementation costs, businesses and tax administrations may also incur costs for arguing interpretation issues in potential disputes and through the courts to the ECJ. Consideration will be necessary to determine whether this is proportionate to the anti-avoidance objectives and whether the subsidiarity principle is really being followed. Specifically, taxpayers will need clarity for domestic fiscal unity regimes and the resulting questions about the recognition of internal transfers/ transactions in the fiscal unit and the filing of tax returns for each of those entities.

On a practical level for those analysing the proposals, the documents claim that the anti-abuse measures in the CCCTB mirror ATAD, but there are differences. This appears potentially to further divide the EU and the OECD, which rejected outright the formulary apportionment as part of the BEPS programme. This could, therefore, put the EU out of sync with the rest of the world. Whether the CCCTB will prevent or reduce future disputes is uncertain, but still the CCCTB will not cover many cases. Such cases include, e.g., transfer pricing between a group entity within and outside the EU, smaller companies and groups which don't opt-in, and the periods before implementation.

From a policy perspective, applying the CCTB/ CCCTB may yield additional benefits. These may be more widely considered in the future, and may include:

- a greater consistency in the rules between countries, thus providing reduced complexity for business and tax administrations (although there may be agreement within what is proposed – more harmonised than standardised)
- rules not prone to regular changes, making administration and compliance easier for taxpayers and tax administrations (these often occur in short-term policy changes made by changing national governments and leaders), and
- Member States refocusing resources, avoiding harmful tax competition by scrutinizing mobile tax bases and preferential rulings (thus competition for foreign direct investment (FDI) is would not be based only on tax).

We notice that the current ATAD2 draft directive doesn't provide any grandfathering or transitional rules. Many US multinationals that invest in the EU use a hybrid entity structure in combination with specific US rules to realise US corporate income tax deferral on the non-US profits. While EU unilateral action in this respect may seriously impact the future location decisions of US multinationals, the absence of grandfathering or transitional rules may directly impact the level of investments in the EU.

Factors considered in investment decisions are a key focus at the moment for the EU, G20 and the OECD. Therefore, we encourage businesses to complete an OECD survey on business certainty so that the OECD may gather information on how direct and indirect tax systems affect business behaviour. The aggregated and anonymised survey results will, it is stated, be included in analysis and presented to the G20 in 2017.

Let's talk

For a deeper discussion of how these issues might affect your business, please call your usual PwC contact. If you don't have one or would otherwise prefer to speak to one of our global specialists, please contact one of the below:

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Appendix

Comparison CCCTB 2011, CCTB 2016 and CCCTB 2016

	CCCTB (2011)	CCTB (2016)	CCCTB (2016)
Scope	**Article 1:** The CCCTB would be available for all company sizes ; MNEs would receive relief certain tax obstacles in the single market and the fact that SMEs would incur less compliance costs if they expand commercially to another Member State. The system is optional. Since not all businesses trade cross-border, the CCCTB will not force companies that don't expand beyond their national territory to bear the cost of shifting to a new tax system. (p. 5) *Article 1* This Directive establishes a common base system for the taxation of certain companies and groups of companies and creates rules for calculating and using that base. (p. 15)	**Article 2:** *Unlike* the 2011 proposal, which established an optional system for all, this Directive would be mandatory for companies that belong to groups exceeding a certain size. The criterion for fixing a size-related threshold would refer to the total consolidated revenue of a group that files consolidated financial statements. Furthermore, to reach a degree of coherence between the two steps (that is, the common corporate tax base and the CCCTB), companies would be required to meet the consolidation conditions in order to fall within the mandatory scope of the common base. This will ensure that all taxpayers under the common base rules will automatically move into the CCCTB scheme once the full initiative materialises with adoption of consolidation and apportionment formulas.. These common rules will also be available, as an option, for companies that do not meet these conditions.	**Article 2:** *Unlike* the 2011 proposals, which established an optional system for all, this proposal would be mandatory for groups of companies exceeding a certain size. The criterion for fixing a size-related threshold would refer to the total consolidated revenue of the group that files consolidated financial statements to which a company belongs. In addition, the common rules would be available, as an option, to a wide scope of groups that fall short of the size threshold. (p. 9) *Article 2* (c) belongs to a consolidated group with total consolidated group revenue for financial accounting purposes that exceeded EUR 750 000 000 during the financial year preceding the relevant financial year; (p. 17)
Definition of groups	**Article 4 (7):** Eligibility for consolidation (group membership) would be determined by a two-part test based on (i) control (more than 50% of voting rights) and (ii) ownership (more than 75% of equity) or rights to profits (more than 75% of rights		**Article 3 (22):** (unchanged compared to the proposal of 2011) Eligibility for the consolidated tax group would be determined by a two-part test based on (i) control (more than 50 percent of voting rights) and (ii) ownership (more than 75

	giving entitlement to profit). Such a test ensures a high level of economic integration between group members, as indicated by a relation of control and a high level of participation. The two thresholds must be met throughout the tax year; otherwise, the company would have to leave the group immediately. There would also be a nine-month minimum requirement for group membership. (p. 13) See also *Article 54 and 55 and Article 58 (2)*		percent of equity) or rights to profits (more than 75 percent of rights giving entitlement to profit). The two thresholds for control and ownership or profit rights must be met throughout the tax year; otherwise, the failing company would have to leave the group immediately. There would also be a minimum requirement of nine consecutive months for establishing group membership. (p. 9) *See also Article 5 and 6 and Article 8 (2)*
Definition of permanent establishment (PE)	**Article 5:** In this Directive, the PE concept is closely aligned with the post-BEPS PE definition recommended in the OECD Model Tax Convention.	**Article 5:** In this Directive, the PE concept is closely aligned with the post-BEPS PE definition recommended in the OECD Model Tax Convention. *Unlike* the 2011 proposal, the revised definition covers only PEs situated within the Union and belonging to a taxpayer who is resident within the Union for tax purposes. The intent is to ensure that all concerned taxpayers share a common understanding and to exclude the possibility of a mismatch due to divergent definitions. Proposing a common definition for PEs situated in a third country, or in the Union, but belonging to a taxpayer who is resident for tax purposes in a third country was not viewed as essential. The Article leaves it to bilateral tax treaties and national law to deal with the third-country definition.. (p. 9)	
Taxable revenues	**Articles 10-14:** Taxable revenues would be reduced by business expenses	**Articles 7-10:** Taxable revenues would be reduced by business expenses	

	and certain other items. Deductible business expenses would generally include all costs relating to sales and expenses linked to the production, maintenance, and securing of income. Deductibility would be extended to R&D costs and costs incurred in raising equity or debt for business purposes. There would also be a list of non-deductible expenses. (pp. 12-13)	and certain other items. The new proposal for a common corporate tax base would also replicate, with some necessary adjustments to ensure consistency, the list of non-deductible expenses that was featured in the 2011 proposal. To support innovation in the economy, this re-launch initiative would introduce a super-deduction for R&D costs into the already generous R&D regime included in the 2011 proposal. That proposal's baseline rule for deducting R&D costs would continue to apply; thus, R&D costs would be fully expensed in the year incurred (with the exception of immovable property). In addition, taxpayers will be entitled, for R&D expenditure up to EUR 20,000,000, to a yearly extra super-deduction of 50%. To the extent that R&D expenditures exceed EUR 20,000,000, taxpayers may deduct 25% of the excess amount. Considering that one of the key policy initiatives relating to the functioning of the single market is to support small and innovative entrepreneurship, the re-launch proposal for a common corporate tax base would grant an enhanced super-deduction for small starting companies that are particularly innovative and do not have associated enterprises (a category that would notably cover start-ups). In that context, taxpayers who qualify, according to the Directive, may deduct 100% of their R&D costs up to EUR 20,000,000, provided that these taxpayers	

		do not have any associated enterprises. (pp. 9-10)	
Depreciation	**Articles 32-42:** Fixed assets would be depreciable for tax purposes, subject to certain exceptions. Long-life tangible and intangible assets would be depreciated individually, while others would be placed in a pool. Depreciation in a pool simplifies matters for both the tax authorities and taxpayers since it avoids the need to establish and maintain a list of every single type of fixed asset and its useful life. (p. 13)	**Articles 30-40:** The rule determining which fixed assets would be depreciable for tax purposes, subject to certain exceptions, remains the same as the 2011 proposal. However, more assets will now fall within the scope of individual depreciation as medium-life fixed tangible assets have been removed from the pool system. (p. 10)	
Losses	**Article 43:** Taxpayers would be allowed to carry losses forward indefinitely, but no loss carryback would be allowed. Since the carry forward of losses is intended to ensure that a taxpayer pays tax on its real income, there is no reason to place a time limit on carryforwards. Loss carrybacks are relatively rare in the practice of the Member States, and lead to excessive complexity. (p.13)	**Article 41:** Consistent with the 2011 proposal, taxpayers are allowed to carry losses forward indefinitely without restrictions on the deductible amount per year. The Directive draws a link between the interest limitation rules and the tax treatment of losses. A policy choice was thus made to draft a highly effective interest limitation rule, to the effect that any amounts qualifying as a loss reflect the outcome of trading activity. The rule has also been reinforced with an anti-abuse provision to discourage attempts to circumvent the rules on loss deductibility through purchasing loss companies. (p.10) **Article 42:** Temporary loss relief with recapture: in order to partially make up for the absence of the benefits of cross-border consolidation during the 'first	**Article 71:** 1. Article 42 of Directive 2016/xx/EU (CCTB) on loss relief and recapture shall automatically cease to apply when this Directive comes into force. 2. Transferred losses that have not yet been added back when this Directive enters into force shall remain with the taxpayer to which they have been transferred. (p. 42)

		step', it would be possible to consider, under strict conditions, losses incurred by an immediate subsidiary or PE situated in other Member States. This relief would be temporary since the parent company would add back to its tax base, considering the amount of losses previously deducted, any subsequent profits made by its immediate subsidiaries or PEs. Furthermore, if the parent does not add back the losses within a certain number of years, they would be added back automatically. (pp.10-11)	
Business reorganisations & taxation of losses and unrealised capital gains	**Article 70 & 71:** Rules on business reorganisations should be established to protect the taxing rights of Member States in an equitable manner. When a company enters the group, pre-consolidation trading losses would be carried forward to be offset the taxpayer's apportioned share. When a company leaves the group, no losses incurred during the period of consolidation would be allocated to it. An adjustment may be made for capital gains when certain assets are disposed within a short period after entry to or exit from a group. The value of self-generated intangible assets would be assessed on the basis of a suitable proxy, such as R&D, marketing and advertising costs over a specified period (p. 13)		**Article 22 & 23:** (unchanged compared to the 2011 proposal) The proposed framework mainly involves the treatment of losses and unrealised capital gains upon entering and leaving the group. When a company enters the group, **pre-consolidation trading losses** would be carried forward to offset its apportioned share. When a company leaves the group, no losses incurred during the period of consolidation would be allocated to it. This proposal comes forward with a refinement of the 2011 rule: for more extensive reorganisations, where more than one company has to leave a loss-making group, a threshold is fixed to determine under which conditions companies would no longer be leaving a group without losses and instead, there would be a loss allocation across the consolidated group. There are rules to deal with **unrealised capital gains** that have

			accrued to fixed assets where the assets are disposed of within a short period after their entry into, or exit from, a group. A Member State (in the case of an entry into a group) or the group (in the case of an exit from a group) are able to tax the underlying capital gains to the extent they were created in their taxing territory. Moreover, the tax treatment of capital gains engrained in self-generated intangible assets calls for a customized approach, which would involve assessing them on the basis of a suitable proxy, such as R&D, marketing and advertising costs over a specified period. (p. 9)
Withholding taxes	**Article 60 & 77:** When a taxpayer withholds taxes on interest and royalty payments, the proceeds of such taxes would be shared according to the formula of that tax year. When a taxpayer withholds taxes on dividends, the proceeds of such taxes would not be shared since, contrary to interest and royalties, dividends have not led to a previous deduction borne by all group companies. (p. 13)		**Article 10 & 26:** (unchanged compared to the 2011 proposal) Taxes withheld on interest and royalty payments would be shared according to the formula of that tax year. Taxes withheld on dividends would not be shared since, contrary to interest and royalties, dividends are distributed after-tax and did not result in a previous deduction borne by all group companies. (p. 9)
Switch-over clause	**Article 73:** Article 11(c), (d) or (e) shall not apply where the entity which made the profit distributions, the entity the shares in which are disposed of or the PE were subject, in the entity's country of residence or the country in which the permanent establishment is situated, to one of the following:	**Article 53:** 1. By way of derogation from points (c) and (d) of Article 8, a taxpayer shall not be exempt from tax on foreign income that the taxpayer received as a profit distribution from an entity in a third country or as proceeds from the disposal of shares held in an entity in a third country where that entity is subject to a statutory corporate tax rate in its country of tax residence lower	**Article 72:** For the purposes of this Directive, the reference to the statutory corporate tax rate that the taxpayer would have been subject to in the first subparagraph of Article 53(1) of Directive 2016/xx/EU (CCTB) shall not apply and shall be replaced by the average statutory corporate tax rate applicable amongst all Member States instead.

	(a) a tax on profits, under the general regime in that third country, at a statutory corporate tax rate lower than 40% of the average statutory corporate tax rate applicable in the Member States; or (b) a special regime in that third country that allows for a substantially lower level of taxation than the general regime. The Commission shall publish annually the average statutory corporate tax rate applicable in the Member States. It shall be calculated as an arithmetic average. For the purpose of this Article and Articles 81 and 82, amendments to the rate shall first apply to taxpayers in their tax year starting after the amendment. (p. 43)	than half of the statutory tax rate that the taxpayer would have been subject to, in connection with such foreign income, in the Member State of its tax residence. The first subparagraph shall not apply where a convention for the avoidance of double taxation between the Member State in which the taxpayer is tax resident and the third country where that entity is tax resident does not allow switching from a tax exemption to taxing the designated categories of foreign income. 2. When paragraph 1 applies, the taxpayer shall be subject to tax on the foreign income with a deduction for the tax paid in the third country from its tax liability in the Member State where it is tax resident. The deduction shall not exceed the amount of tax, computed before the deduction, which is attributable to the income that may be taxed. 3. Member States shall exclude losses from the scope of this Article in the event of a disposal of shares in an entity that is resident in a third country for tax purposes. (pp. 45-46)	
Preventing circumvention of tax exemptions	**Article 75:** Income consisting of dividends, proceeds from the disposal of shares in a company outside the group, and the profits of foreign PEs would be exempt. To provide relief from double taxation, most Member States exempt dividends and proceeds from the disposal of shares because		**Article 24:** (unchanged compared to the 2011 proposal) The tax exemption favouring disposals of shares would be disallowed if this is illegitimately extended to sales of assets other than shares. This occurs if assets are moved within the group, without tax implications, to a group member that is then

	it avoids having to compute a credit for the tax paid abroad, in particular where such computation must consider the corporate tax paid by the company distributing dividends. The exemption of income earned abroad meets the same need for simplicity. (p. 12)		sold out of the group. The assets would benefit, under the cover of a sale of company, from the tax exemption for share disposals. A similar treatment exists for intra-group transfers of assets that are then sold out of the group within the current or following tax year. In this case, an adjustment would be made to treat the asset as having left the group from the Member State where it was initially located, that is, prior to the intra-group transfer. (p. 10)
General anti-abuse rule	**Article 80:** Artificial transactions that taxpayers carry out for the sole purpose of avoiding taxation shall be ignored for the purposes of calculating the tax base. The first paragraph shall not apply to genuine commercial activities where the taxpayer is able to choose between two or more possible transactions that have the same commercial result but produce different taxable amounts. (p. 46)	**Article 58:** **1**. For purposes of calculating the tax base under the rules of this Directive, a Member State shall disregard an arrangement or a series of arrangements which, having been put in place for the essential purpose of obtaining a tax advantage that defeats the object or purpose of this Directive, are not genuine, considering all relevant facts and circumstances. An arrangement may comprise more than one step or part. 2. For purposes of paragraph 1, an arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put in place for valid commercial reasons that reflect economic reality. 3. Arrangements or a series thereof that are disregarded in accordance with paragraph 1 shall be treated, for the purpose of calculating the tax base, by reference to their economic substance.	
Deductibility of interest	**Article 81:**	**Article 13:**	**Article 69:**

	1. Interest paid to an associated enterprise resident in a third country shall not be deductible where there is no agreement on the exchange of information comparable to the exchange of information on request provided for in Directive 2011/16/EU and where one of the following conditions is met: (a) the general regime in the third country provides for a tax on profits at a statutory corporate tax rate lower than 40% of the average statutory corporate tax rate applicable in the Member States; or (b) the associated enterprise is subject to a special regime in that third country which allows for a substantially lower level of taxation than that of the general regime. 2. The term 'interest' means income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment shall not be regarded as interest. 3. Notwithstanding paragraph 1, interest paid to an entity resident in a third country with which there is no agreement on the exchange of information comparable to the exchange of information on request provided for in Directive 2011/16/EU shall be	This is a new rule (absent from the 2011 proposal), featured in the ATAD and analysed in detail as part of the BEPS initiative. It limits the deductibility of interest (and other financial) costs to discourage profit shifting to low-tax countries. The rule would allow the full deductibility of interest (and other financial) costs to the extent they can offset taxable interest (and other financial) revenues. Any excess interest costs would be subject to deductibility restrictions, determined by reference to a taxpayer's taxable earnings before interest, tax, depreciation, and amortisation (EBITDA). (p.10)	1. For the purposes of this Directive, a group shall be treated as one single taxpayer under Article 13 of Directive 2016/xx/EU (CCTB). The principal taxpayer shall represent the group. 2. Where paragraph 1 applies, the excess borrowing costs and EBITDA shall be calculated at the group level and include the results of all group members. The amount of EUR 3,000,000 referred to in Article 13 of Directive 2016/xx/EU (CCTB) shall be increased to 5,000,000. 3. The Commission may adopt delegated acts in accordance with Article 75 to implement more detailed anti-fragmentation rules for the deductibility of excess borrowing costs. (p. 42)

	deductible in an amount not exceeding that which would be stipulated between independent enterprises, where one of the following conditions is met: (a) the interest amount is included in the tax base as income of the associated enterprise in accordance with Article 82; (b) the interest is paid to a company whose principal class of shares is regularly traded on one or more recognized stock exchanges; or (c) the interest is paid to an entity engaged, in its country of residence, in the active conduct of a trade or business, This is defined as an independent economic enterprise carried on for profit and in which officers and employees carry out substantial managerial and operational activities. (pp. 46-47)		
Controlled foreign companies (CFCs)	**Article 82:** 1. The tax base shall include the non-distributed income of an entity resident in a third country where the following conditions are met: (a) the taxpayer by itself, or together with its associated enterprises, holds, directly or indirectly, more than 50% of the voting rights, or more than 50% of capital, or is entitled to receive more than 50% of the profits of that entity; (b) under the general regime in the third country, profits are taxable at a statutory corporate tax rate lower than 40% of the	**Article 59:** 1. An entity, or a PE whose profits are not subject to tax or are exempt from tax in the Member State of its head office, shall be treated as a CFC where the following conditions are met: (a) when an entity, the taxpayer itself, or together with its associated enterprises, holds, directly or indirectly, more than 50% of the voting rights, or more than 50% of capital, or is entitled to receive more than 50% of the profits of that entity; and	**Article 73:** For the purposes of this Directive, the scope of CFC legislation under Article 59 of Directive 2016/xx/EU (CCTB) shall be limited to relations between group members and entities that are resident for tax purposes, or PEs that are situated, in a third country. (p. 43)

	average statutory corporate tax rate applicable in the Member States, or the entity is subject to a special regime that allows for a substantially lower level of taxation than that of the general regime; (c) more than 30% of the income that the entity accrues falls within one or more of the categories set out in paragraph 3; (d) the company's principal class of shares is regularly traded on one or more recognized stock exchanges. 2. Paragraph 1 shall not apply where the third country belongs to the European Economic Area (EEA) Agreement and there is an agreement on the exchange of information comparable to the exchange of information on request provided for in Directive 2011/16/EU. 3. The following categories of income shall be taken into account for the purposes of point (c) of paragraph 1, if more than 50% of the entity's income comes from the following transactions with the taxpayer or its associated enterprises: (a) interest or any other income generated by financial assets (b) royalties or any other income generated by intellectual property (c) dividends and income from the disposal of shares (d) income from movable property	(b) the actual corporate tax the entity or PE pays on its profits is lower than the difference between the corporate tax that would have been charged on the profits of the entity or PE in accordance with the rules of this Directive and the actual corporate tax paid on those profits by the entity or PE. For the purposes of point (b) of the first subparagraph, in computing the corporate tax that would have been charged on the entity's profits according to the rules of the Directive in the taxpayer's Member State, the income of any PE of the entity that is not subject to tax or is exempt from tax in the jurisdiction of the CFC shall not be taken into account. 2. Where an entity or PE is treated as a CFC under paragraph 1, non-distributed income of the entity or PE shall be subject to tax to the extent that it is derived from the following categories: (a) interest or any other income generated by financial assets (b) royalties or any other income generated from intellectual property (c) dividends and income from the disposal of shares (d) income from financial leasing (e) income from insurance, banking and other financial activities, or (f) income from invoicing companies that earn sales and services income from goods	

	(e) income from immovable property, unless the Member State of the taxpayer would not have been entitled to tax the income under an agreement concluded with a third country, or (f) income from insurance, banking and other financial activities (p. 47).	and services purchased from and sold to associated enterprises and add no or little economic value. The first subparagraph shall not apply to a CFC that is resident or situated in a Member State or in a third country that is party to the EEA. Agreement where the CFC has been set up for valid commercial reasons that reflect economic reality. For the purposes of this Article, the activity of the CFC shall reflect economic reality to the extent that commensurate staff, equipment, assets and premises support that activity. 3. An entity or PE shall not be treated as a CFC, as referred to in paragraph 1, where one third or less of the entity or PE's income falls within categories (a) to (f) of paragraph 2. Financial undertakings shall not be treated as CFCs under paragraph 1 where one third or less of the entity or PE's income from categories (a) to (f) of paragraph 2 comes from transactions with the taxpayer or its associated enterprises. (pp. 48-49)	
Formulary apportionment	**Articles 86-97:** The formula for apportioning the consolidated tax base would comprise three equally weighted factors (labour, assets and sales). The labour factor would be computed on the basis of payroll and the number of employees (each item counting for half). The asset factor would consist of all		**Articles 28-41:** (unchanged compared to the 2011 proposal) It would comprise three equally weighted factors (labour, assets and sales by destination). This combination reflects a balanced approach to distributing taxable profits amongst eligible Member States. The labour factor would

	fixed tangible assets. Intangibles and financial assets would be excluded from the formula due to their mobile nature and the risks of circumventing the system. These factors give appropriate weight to the interests of the Member State of origin. Finally, sales would be taken into account to ensure fair participation of the Member State of destination. Those factors and weightings should ensure that profits are taxed where they are earned. As an exception to the general principle, where the outcome of the apportionment does not fairly represent the extent of business activity, a safeguard clause provides for an alternative method. (p. 14)		be divided into payroll and the number of employees (each item counting for half) to account for differences in the levels of wages across the Union and thereby allow for a fairer distribution. The asset factor would consist of all fixed tangible assets. Intangibles and financial assets would be excluded from the formula due to their mobile nature and the risks of circumventing the system. These factors and weightings should ensure that profits are taxed where they are actually earned. As an exception, where the outcome of the apportionment does not fairly represent the extent of business activity, a safeguard clause would provide for an alternative method of income allocation. As the general scheme of the formulary apportionment cannot address the specificities of certain industries, there would be rules on adjusted formulae, in order to better fit the needs of sectors such as financial services and insurance, oil and gas, as well as shipping and air transport. (p. 10)
Administrative procedures	**Articles 104-110:** Groups of companies would be able to deal with a single tax administration ('principal tax authority'), which would be that of the Member State in which the parent company of the group ('principal taxpayer') is resident for tax purposes. This Directive would also establish procedural rules for the administration of the system. It would also provide for an advance ruling mechanism. The principal tax authority would initiate and		**Articles 46-56:** *Unlike* the 2011 proposal, the common administrative rules are limited to the consolidated group. As a matter of principle, single taxpayers, who opt to apply the rules under the 'first step' (CCTB), continue to fall within their national administrative provisions. Groups would deal with a single tax administration ('principal tax authority') in the EU; this is also referred to as the 'one-stop-shop'. This would be based in the Member

	coordinate audits, but the authorities of any Member State in which a group member is subject to tax may request the initiation of an audit. The competent authority of the Member State in which a group member is resident or established in may challenge a principal tax authority's decision concerning the notice to opt or an amended assessment before the courts of the Member State of the principal tax authority. An administrative body that is competent to hear appeals at first instance according to the law of the Member State of the principal tax authority would deal with disputes between taxpayers and tax authorities. (p. 14)		State where the parent company of the group ('principal taxpayer') is resident for tax purposes. The principal tax authority would initiate and coordinate audits. The national authorities of any Member State in which the profits of a group member are subject to tax may request the initiation of an audit. The competent authority of the Member State in which a group member is resident or established may challenge a principal tax authority's decision concerning the notification that there is a group or an amended assessment. For this purpose, an action would be brought before the courts of the Member State of the principal tax authority. An administrative body that is competent to hear appeals at first instance according to the law of the Member State of the principal tax authority would deal with disputes between taxpayers and tax authorities. (p. 10)
Hybrid mismatches		**Article 61:** Given that national differences in the legal qualification of certain types of entities or financial payments generate mismatches, they should normally not occur amongst companies that apply the common rules for calculating their tax base. Since, however, mismatches are likely to persist in the interaction between the framework of the common base and national or third-country corporate tax systems, this Directive establishes rules whereby one of the two jurisdictions in a	**Article 74:** For the purposes of this Directive, the scope of the rules on hybrid mismatches under Article 61 of Directive 2016/xx/EU (CCTB) shall be limited to relations between group members and non-group members that are associated enterprises, as referred to in Article 56 of Directive 2016/xx/EU (CCTB). (p. 43)

		mismatch deny the deduction of a payment or ensure that the corresponding income is included in the common base. (p. 11)	
Deductibility of equity		**Article 11:** Allowance for Growth and Investment (AGI): The re-launch initiative intends to tackle the asymmetry whereby taxpayers can deduct from their common base interest paid on loans (subject to some limits) but not profit distributions. The outcome is a definitive advantage in favour of financing through debt as opposed to equity. Given the risks that such a situation entails for the indebtedness of companies, the re-launch proposal for a common corporate tax base would include a rule against debt bias, to neutralise the current framework that discourages equity financing. Taxpayers would be given an allowance for growth and investment, which would allow taxpayers to deduct increases in their equity from their taxable base subject to certain conditions, such as measures against potential cascading effects and anti-tax avoidance rules. As part of the review of the common tax base, the Commission shall give specific consideration to the functioning of the AGI as a basis for considering adjustments to its definition and calibration. (p. 10)	