CONFEDERATION FISCALE EUROPEENNE

Opinion Statement FC 3/2014 of the CFE

on the Recommendation C(2012)8806 on aggressive tax planning, an EU GAAR and double-non taxation

Prepared by the CFE Fiscal Committee

Submitted to the European Commission

in March 2014

CFE (Confédération Fiscale Européenne) is the umbrella organisation representing the tax profession in Europe. Our members are 32 professional organisations from 25 European countries (21 EU member states) with 180,000 individual members. Our functions are to safeguard the professional interests of tax advisers, to assure the quality of tax services provided by tax advisers, to exchange information about national tax laws and professional law and to contribute to the coordination of tax law in Europe.

CFE is registered in the EU Transparency Register (no. 3543183647-05).

Background

On 6 December 2012, the European Commission issued its Recommendation C(2012)8806 on aggressive tax planning (hereinafter: the Recommendation). This Recommendation to EU member states (MS) essentially consists of two elements:

- a subject to tax clause to be included in MS´ double tax treaties with other MS or non-EU countries and/or in their national law, to prevent that a company´s income is neither taxed in the state where it is generated, nor in the company´s residence state ("double non-taxation"), and
- a General-Anti-Abuse-Rule (GAAR), to be included in national laws.

The Recommendation only concerns direct taxes.

The European Commission has discussed this Recommendation with MS and member organisations of the *Platform for Tax Good Governance*. In this context, the Commission has prepared in January 2014 a discussion paper[i] on the Recommendation (hereinafter: the Discussion Paper), containing questions to the Platform. The observations below relate to the questions raised in this Discussion Paper.

I. Definition of aggressive tax planning

The Commission explains that *"Aggressive tax planning consists in taking advantage of the technicalities of the tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability"*[ii].

The CFE considers that this definition is not accurate.

The first part of this definition ("*consists in taking advantage of the technicalities of the tax system*") could well apply as "tax avoidance". Besides, "tax avoidance" has been accepted by the ECJ as one of the possible justifications for the restriction of the freedoms of the Treaty on the Functioning of the EU (Treaty).

Quite different is the second alternative *"taking advantage of (…) mismatches between two or more tax systems for the purpose of reducing tax liability"*. The origin of mismatches may well be the parallel exercise of the fiscal sovereignty by two MS, which has been recognised and admitted by the ECJ[iii]. We are not convinced that a use of tax laws, adopted in parallel exercise of taxing powers,

should be considered aggressive, whenever there is a real exercise of such freedoms (see below our remarks on point 4.2 of the recommended GAAR).

The CFE believes that the work of the Commission should not go beyond what is agreed on, and effectively implemented, at the OECD level (BEPS project). If the EU opts to take a narrower view, it risks placing itself in a disadvantageous position compared to other jurisdictions.

II. Double non-taxation

In the Discussion Paper, the Commission has asked the following questions to the Platform members:

1) Platform members are invited to report on the state of play and progress in including such a clause in double taxation conventions.

2) Do the Platform members foresee practical or administrative difficulties in applying this approach in practice? If so, how can these difficulties be addressed?

3) Do the Platform members see other double non-taxation issues that ought to be considered in relation to Double Taxation Conventions?

4) Do Platform members have suggestions on best practices to address non-taxation in Double Taxation Conventions?

CFE comments:

Question 2: Practical/administrative difficulties in applying the approach suggested by the EU

Definition of "*subject to tax*" (point 3.4 of the Recommendation):

In our view, the meaning of "*subject to tax*" should be further elaborated, since the proposed definition lacks clarity and effectiveness and may leave room for further conflict and disputes. Given that this definition only covers income that is *"treated as taxable by the jurisdiction concerned and is not exempt from tax, nor benefits from a full tax credit or zero-rate taxation"*, such rule can easily be circumvented by countries by applying a *de minimis* level of tax. We therefore believe that a workable definition of "subject to tax" cannot avoid a reference to the tax rate.

Question 3: Other double non-taxation issues that ought to be considered in relation to double taxation conventions

Solutions must not create further double taxation

Before including the subject to tax clause in the existing double tax treaties, it should be ensured that these double tax treaties effectively eliminate double taxation, both juridical and economic.

Solutions should be developed in the OECD context

Any action taken by the EU should also take into consideration the developments made at international level (BEPS Action Plan by the OECD – Action 2 "*to neutralize the effects of hybrid mismatches arrangements*") in order to avoid any competitive disadvantage for EU taxpayers. The OECD's deadline for the implementation of the aforementioned Action 2 has been scheduled for September 2014.

Solutions must respect the Member States´ sovereignty

The concept of "*double non-taxation*" in the Recommendation is particularly broad. The CFE suggests that a careful analysis and clarification of this concept be carried out, in particular, with regard to the type of situation occurring, i.e. whether this is due to mismatches (hybrid entities and hybrid instruments) or to tax competition (low taxation).

The CFE does not agree that double non-taxation is, *per se*, something bad. Many double tax treaties include clauses whose purpose is precisely that of facilitating double non-taxation in order to give an incentive to certain activities or types of income.

There cannot be a blanket assumption that countries or MS, by concluding double tax treaties, seek to exclude double non-taxation as well, unless the agreement expressly says so. There are examples of MS that have included subject-to-tax clauses in agreements only with some MS but not with others, although the agreements have been concluded by the same government, during the same period[iv]. It seems highly speculative to deduce any intention of parties to an agreement where these parties are jurisdictions which may have a different understanding of legal principles and may pursue different internal political objectives.
Therefore there cannot be an assumed "spirit" beyond the letter of double tax treaties. Neither can a subject to tax clause be in the assumed interest of a residence country. Residence countries may have reasons not to opt for a subject to tax clause, since such clause may oblige them to treat foreign income differently from domestic income. This will narrow the country´s discretion to grant tax incentives, as such incentives would distort competition. This could be incompatible with national laws.

As a conclusion, double non-taxation, where it is intended by states, should be accepted as the parallel exercise of taxing powers. Any analysis of the European Commission should draw this distinction.

Question 4: Suggestion of best practices

Improve cooperation and information exchange

Member States should increase tax cooperation and automatic exchange of information to potentiate early detection of aggressive tax planning schemes and to coordinate strategies and approaches to better address double non-taxation issues.
Further analysis and discussion should be devoted to cross-border cooperation in order to decide whether (and what) information should or should not be exchanged among MS.

Enable taxpayers to obtain a ruling

As it may be difficult for taxpayers to determine whether double non-taxation has been intended, there should be the possibility for the taxpayer to ask his residence MS for a ruling. Where confidentiality concerns can be solved by anonymisation of the ruling, such rulings should be published, to contribute to legal certainty and to ensure transparent and equal treatment of taxpayers.

III. A General Anti-Abuse Rule

In the Discussion Paper, the Commission has asked the following questions to the Platform members:

6) Platform members are invited to report on the state of play and progress in including a General Anti-Abuse rule in national legislation.

7) Do the Platform members foresee practical or administrative difficulties in applying this approach in practice? If so, how can these difficulties be addressed?

8) What are Platform members' views on the efficiency of such a General Anti-Abuse rule within the EU?

CFE comments:

The CFE recognises and supports EU efforts to tackle tax fraud and evasion, as well as MS´ efforts to properly address the gaps and loopholes that exist at the EU level. The CFE fully recognizes the advantage of having one clear set of anti abuse rules in order to avoid further difficulties when dealing with several national tax authorities.

The CFE supports the EU initiative to implement an EU GAAR aimed at preventing the implementation of wholly artificial arrangements, as long as:

- the agreed solution warrants an efficient implementation among MS;
- the new framework is clear and effective (limiting total discretionary interpretations);
- EU businesses are not negatively affected and the EU fundamental freedoms respected.

Question 6: State of play and progress in including a GAAR in national legislation

During the period of April-July 2013, the CFE drafted a questionnaire on GAARs among its member countries to establish to what extent GAARs are already in place in member countries. The main results are summarised in a separate (enclosed) document.

Question 7: Practical or administrative difficulties in applying this approach in practice and how these can be addressed

The CFE has editorial as well as technical comments that concern the wording and practical use of the proposed EU GAAR:

A concise EU GAAR

An EU GAAR must be carefully drafted to ensure that:

- it fits in all direct tax situations, in the context of different pieces of legislation, and
- it will not have to be amended on a frequent basis.

This suggests that a proposed GAAR should be concise rather than prescriptive. It should not include an enumeration of arrangements considered unacceptable, as new types of arrangements emerge constantly. It is a truism that the more prescriptive a law is, the more gaps it leaves.

We recognise the demand for guidance in the application of a GAAR but we consider that this should be better accommodated through a commentary issued by the Commission, which would contain examples like the points 4.3 to 4.7 of the Recommendation and reflect changes in the ECJ case law, rather than including as many examples as possible in the wording of the GAAR.
The Commission should continue monitoring the implementation of the Recommendation into national law, administrative practices and double tax treaties.

An EU GAAR in conformity with the Treaty

- Comments relating to point 4.2:

We agree with the Commission to the extent that artificiality should be the decisive criterion when judging whether an arrangement shall be accepted or disregarded for tax purposes. Artificiality is an objective criterion. If an arrangement lacks economic substance, its use fulfils no economic purpose and hence deserves no protection under the EU fundamental freedoms.

However, where there is substance and hence an exercise of Treaty freedoms, we do not see why the taxpayer´s intentions when setting up the arrangement should play a role. Moreover, we doubt that such criteria are workable in practice. Intentions are difficult to prove. A distinction whether an arrangement has been put into place for the essential, the main or the sole purpose of avoiding taxation cannot reasonably been drawn.

To determine whether an arrangement leads to a “tax benefit”, a comparison will have to be made. This implies that there would be a single “normal” or “reference” behaviour and tax outcome. This does not reflect reality where taxpayers have many different legal and business options to take into consideration.

- Comment relating to point 4.4:

As far as the examples for determining artificiality are concerned (point 4.4 b), we would suggest replacing the word “*reasonable*” by the word “*acceptable*”.

- Points to be added to the recommended GAAR / commentary:

Moreover, and in line with a number of national GAARs, the EU GAAR should set forth a provision granting the taxpayer the possibility to demonstrate the economic validity of his arrangements [e.g. "*valid economic reasons*" (as in the Italian tax system[v]), or "*relevant non-tax reasons*" (as in the German tax system[vi])]. The Commission´s commentary should include further explanations.

The CFE also suggests that the risk of double taxation in connection with the application of the GAAR be considered, in order to instruct MS on how to better avoid and solve the phenomenon of double taxation.

Question 8: Efficiency of a GAAR within the EU

Given the differences in the domestic legal systems and traditions in MS, the CFE is of the opinion that a uniform interpretation of any EU GAAR will not be easily achieved.

IV. Other measures against aggressive tax planning

In the Discussion Paper, the Commission has asked the following question to the Platform members: 9. Do Platform members have any other suggestions on how to address aggressive tax planning?

CFE comment:

The CFE, AOTCA (The Asia-Oceania Tax Consultants´ Association) and STEP (Society of Trust and Estate Practitioners) have presented a draft Model Taxpayer Charter in May 2013, intended as a blueprint for what a good tax system should include. We believe that such Charter will contribute to fostering a relationship of mutual trust and mutual responsibility between taxpayers and tax authorities, while promoting the fulfilment of taxpayers' duties, as well as the tax authorities' position *vis-à-vis* the rights of taxpayers.

MS should be encouraged to endorse these principles by referring to this Model Charter which is designed to have a global remit.

The CFE also welcomes and supports the European Commission´s intention to present an EU Taxpayer´s Code essentially based on the same principles.

On tax avoidance, Art. 28 of the draft Model Taxpayer Charter[vii] provides that:

> *1. Legislative measures directed towards denying tax effectiveness to otherwise legal transactions whose purpose is principally directed to the reduction of taxation liabilities of particular Taxpayers and that are artificial, blatant and contrived are appropriate measures to maintain the integrity of the taxation system.*
>
> *[explanatory note:] This provision affirms that tax-avoidance legislation, whether specific or general, is a valid approach to counter artificial, blatant and contrived tax-reduction arrangements. However, a reasonable balance is needed that the paragraphs below seek to achieve.*
>
> *2. Such measures need to recognise both that the purpose of many legal provisions that afford taxation relief to Taxpayers which enter into transactions acts as an incentive for them to do*

so, and the legitimacy, within clearly defined limits, of Taxpayer choice as to the form of transactions and business structures that the Taxpayer will adopt.

[explanatory note:] Tax-avoidance legislation should not deny a Taxpayer the benefit derived from incentives provided in the legislation or the benefit of reasonable choices among alternative transactions or business structures. The applicable doctrine of when a general anti avoidance rule will become actionable will vary from country to country. However, the threshold should be a high one, since the Taxpayer has otherwise complied with all requirements of the tax legislation.

3. Tax-avoidance legislation shall be drafted with sufficient clarity that its scope can be readily understood and discretion shall not be granted to Taxation Officers beyond the specific words of the tax-avoidance legislation.

[explanatory note:] What is most important in practical terms concerning tax-avoidance laws is that they be clear, well known, and not open to the discretion of the Tax Administration – or, worse yet, particular Tax Officers. Taxpayers are entitled to reasonable certainty in their tax affairs. Broadly worded tax-avoidance legislation that gives wide discretion in interpretation is unfair.

We would like to stress that the above-cited Art.28 (3) (clear drafting providing legal certainty) is particularly important in the context of the EU GAAR.

We will be pleased to answer any questions you may have concerning CFE's comments outlined above. For further information, please contact Mr. Piergiorgio Valente, Chairman of the CFE Fiscal Committee, at rreibel@cfe-eutax.org.

Sincerely yours,

Confédération Fiscale Européenne

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[i] DOC: Platform/006/2014/EN.

[ii] Discussion Paper on the follow-up of the Commission Recommendation regarding measures intended to encourage third countries to apply minimum standards of good governance" (DOC: Platform/005/2014/EN).

[iii] Decisions in cases C-513/04, *Kerckhaert and Morres*, paragraph 20; C-298/05, *Columbus Container Services*, paragraph 43; C-67/08, *Block*, paragraph 31, and other.

[iv] The Protocol of the Convention for the Avoidance of Double Taxation of Income and Capital and for the Prevention of Fiscal Evasion and Fraud between the Government of the French Republic and the Government of the Italian Republic, signed in 05.10.1989, in its Article 15 specifically include a "subject to tax clause": *"15. In the cases where, in accordance with the provisions of this Convention, income must be exempted by one of the States, the exemption shall be granted if and to the extent such income is taxable in the other State*" . The Convention between the Federal Republic of Germany and the Republic of Italy for the Avoidance of Double Taxation with respect of Income and Capital and for the Prevention of Fiscal Evasion, signed few days later (18.10.1989) does not include such provision.

[v] Art. 37- bis (1) of Presidential Decree No. 600/1973.

[vi] § 42 (2) AO (Abgabenordnung / General Fiscal Code), link.

[vii] Full text available in: http://www.cfe-eutax.org/sites/default/files/Model%20Taxpayer%20Charter,%20preliminary%20report,%20text.pdf.