The European Commission’s Anti-Tax Avoidance package

A brief Oxfam analysis of key points
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Proposal for an Anti-Tax Avoidance Directive

- **Interest limitation rule**: Consultations by the OECD and the UN committee of experts on taxation have found that tax avoidance via excessive interest deductions is of particular concern for developing countries. The European Commission proposes to cap interest deduction at 30% while the OECD has recommended a ratio between 10% and 30%. By selecting the weakest option, the European Commission chooses the lowest common denominator.

- **Controlled Foreign Company legislation**: Controlled Foreign Company (CFC) rules are a crucial measure against profit-shifting into low-tax jurisdictions. If the income of a subsidiary abroad is taxed at a low effective rate, or not taxed at all, then CFC rules apply and the home country’s tax authority taxes the income of the foreign subsidiary. The Commission proposes a 40% home country tax rate threshold, i.e. tax authorities can tax profits of a foreign-based subsidiary if the tax rate paid there is lower than 40% of the home country tax rate. In the case of Bulgaria, which has a 10% corporate income tax rate, even at a tax rate as low as 4% in countries where subsidiaries are based, CFC rules would not apply.

- **Hybrid mismatches**: Hybrid mismatches involve legal entities or instruments that are treated differently under the rules of different countries, e.g. an entity could be a partnership or a company, while a financial instrument could be a loan or an equity contribution. Rules against hybrid mismatches can benefit developing countries by making it more difficult to shift profits out of their territory and into the EU in such a way that profits remain untaxed. The current proposal only covers hybrid mismatches between EU member states. This makes it very weak, as mismatches with third countries are common.

- **Permanent establishment**: Criteria defining a permanent establishment, i.e. a fixed place of business, are essential to determine the taxable presence of a foreign company. While the objective of the Anti-tax avoidance directive is to implement OECD recommendations regarding BEPS, the recommendation concerning permanent establishment (Action 7 of the OECD/BEPS project) is only mentioned in a non-binding recommendation on tax treaty abuse. In December, discussions at
Council level actually referred to ‘artificial avoidance of permanent establishment status’. This is very worrying – without a strong common definition of what a permanent establishment is, multinationals will still be entitled to artificially avoid declaring a subsidiary and shift their profit.

Proposal for a Directive implementing the G20/OECD Country-by-Country Reporting (CbCR)

The European Commission proposes to adopt OECD rules for country-by-country reporting by reforming the Directive on Administrative Cooperation (DAC4). This way, only tax administrations will know where multinationals generate profit and where they pay taxes. Additionally, the current proposal applies only to multinationals groups with consolidated revenue of at least €750 million. This threshold will limit the investigative powers of tax administrations. Moreover, most tax administrations of developing countries will be left in the dark because they need to apply reciprocity arrangements which require high administrative capacity. The current approach of the Commission does, however, not exclude legislation on public disclosure obligations for companies in the future.

Communication on an external strategy regarding tax havens

After a first step towards a European blacklist of tax havens last June, the European Commission is willing to engage in new discussions with member states on building a common strategy to list and counter non-EU tax havens. The strategy will not apply to EU member states although some of them are widely known as non-cooperative jurisdictions. In addition, the proposed criteria should not only focus on secrecy jurisdictions, but also on schemes allowing corporate tax avoidance.