ECOFIN concludes on EU blacklist and on taxation of digital economy

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On December 5, 2017 the Economic and Financial Affairs Council of the EU (ECOFIN) reached agreement on the EU list of non-cooperative jurisdictions for tax purposes: Seventeen countries have been placed on a blacklist, forty-seven countries on a grey list and eight 'hurricane countries' (i.e. countries recently affected by tropical storms) have been given additional time to comply.

The ECOFIN also adopted conclusions on the taxation of profits of the digital economy, with the objective to outline a common EU position in discussions at the international level.

EU lists of non-cooperative tax jurisdictions

In January 2016, the EU Commission presented its Anti-Tax Avoidance Package (see Luxembourg Tax Alert 2016-4). Among the measures proposed was a common approach to third country jurisdictions on tax good governance matters. The aim was to replace the current patchwork of national lists with a single EU listing system which would provide "clear, coherent and objective criteria". The listing process followed a three step approach comprising a pre-assessment of countries, an extensive screening phase and, finally, the listing of non-cooperative jurisdictions.

After pre-assessment of third country jurisdictions (based on factual information and risk indicators such as economic ties, financial activity and stability factors), an extensive screening and dialog process with the identified jurisdictions took place, with the criteria being assessed based on the following:

- **tax transparency** – consisting of three sub-criteria: (**1**) compliance with international standards on the automatic exchange of information (AEOI or Common Reporting Standard, CRS), (**2**) rating of "largely compliant" by the OECD Global Forum on Transparency with respect to the exchange of information on request (EOIR), and (**3**) ratification of the OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters or bilateral agreements with all EU Member States, effectively allowing both AEOI and EOIR. In the future, a fourth criteria will be the global exchange of beneficial ownership information;
- **fair taxation** – the absence of harmful tax regimes and no facilitation of offshore structures aimed at attracting profits which do not reflect real economic activity in the jurisdiction; and
- **implementation of the BEPS minimum standards** measured according to OECD BEPS Inclusive Framework reviews.

As a result of the screening process, the Council placed the following seventeen countries on the EU blacklist of non-cooperative jurisdictions: American Samoa, Bahrain, Barbados, Grenada, Guam, South Korea, Macao, Marshall Islands, Mongolia, Namibia, Palau, Panama, Saint Lucia, Samoa, Trinidad and Tobago, Tunisia and the United Arab Emirates. The Council recommended that the list be revised at least once a year. Listed jurisdictions are encouraged to make the required changes and to engage in discussions with the Code of Conduct Group that will be monitoring the criteria and commitments made.

Twenty jurisdictions were given the all-clear. Forty-seven jurisdictions were identified as cooperative, subject to successful delivery on their commitments to comply with the EU screening criteria. In this respect, commitments taken by these grey-listed jurisdictions will be monitored and should be implemented by the end of 2018 for most countries, with a possible extension to 2019 for developing countries. Eight countries recently affected by tropical storms – the 'hurricane countries' (including the Bahamas and the British Virgin Islands) will have until February 2018 to comment.

In response to the publication of the blacklist, Member States are expected to apply at least one of the following administrative measures:

- stricter monitoring of certain transactions;
- increased audit risks for taxpayers benefiting from the disputed regimes; or
- increased audit risks for taxpayers using structures or arrangements involving blacklisted jurisdictions.

The Council takes the view that Member States could take certain tax defensive measures in accordance with their national legislation and with EU and international law, such as the non-deductibility of costs, withholding tax provisions, controlled foreign company rules and the limitation of the participation exemption, switch-over rules, reversal of burden of proof, special documentation requirements or mandatory disclosure by tax intermediaries of specific tax schemes.

At an EU level, the EU Commission stated that defensive measures in non-tax areas will be applied, such as limiting access to EU funding or stricter reporting requirements for multinationals that have a presence in blacklisted jurisdictions.

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The EU Commission has expressed its preference for the implementation of stronger defensive measures against the listed jurisdictions. While the Council's conclusions underline the dissuasive effects of the listing, it remains to be seen how the listed jurisdictions will react and whether the Member States will agree to implement sanctions at the EU level.

Conclusions on the taxation of profits in the digital economy

Following the informal ECOFIN meeting in September 2017, the European Commission issued a Communication on a fair and efficient tax system in the European Union for the digital single market. The Commission proposed both long-term solutions (building on traditional international tax rules) and short-term solutions, such as the introduction of an equalization tax on turnover, a withholding tax on digital transactions or a levy on revenues generated from the provision of digital services or advertising activity.

The Council's (draft) conclusions on "Responding to the challenges of taxation of profits of the digital economy", adopted by the ECOFIN during its meeting of December 5, build on those discussions. The conclusions are aimed at defining a common EU approach in view of subsequent discussions at the international level. In this respect, the Council particularly highlights the urgency of agreeing on a policy response at a global level, and stresses the importance of reaching consensus internationally.

In addressing the challenges posed by the digital economy, the Council suggests that the concept of a 'virtual permanent establishment' be explored, based on elements specified by the OECD such as revenue-based, user-based and digital factors. Finally, the Council's conclusions take note of the proposal for an equalization tax favored by certain Member States, considering that such a tax could also be assessed by the European Commission, but would remain outside

Scan barcode to visit KPMG Luxembourg's Tax Alerts the scope of bilateral tax treaties concluded by Member States.

Calling for action at the global and possibly EU level, the Council also urged the OECD to find appropriate solutions for upgrading the global network of bilateral treaties, the OECD Model Tax Convention and accompanying commentaries, as well as the various OECD guidelines on transfer pricing. It also invited the European Commission to put forward proposals for early 2018, after having assessed the economic impact of the envisaged responses.

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While some Member States strongly advocate the implementation, at the EU level, of an equalization tax targeting digital businesses, it seems that the recent stance taken by the Council will focus on reaching a wider consensus through an update of the international tax framework, including the introduction of the concept of a ‘digital presence’ in the definition of a permanent establishment.