Euro Tax Flash from KPMG's EU Tax Centre

Updates to the EU list of non-cooperative jurisdictions

Council of the EU – Code of Conduct Group – Harmful Tax Regimes – EU list – Tax Transparency

On October 5, 2021, the Council adopted conclusions on a revised EU list of non-cooperative jurisdictions for tax purposes. The Council agreed to move Anguilla, Dominica and Seychelles to Annex II of the list (the so-called "grey list").

Costa Rica, Hong Kong (SAR), China (hereinafter, Hong Kong (SAR)), Malaysia, North Macedonia, Qatar and Uruguay were added to the grey list following a review of their foreign source income exemption (FSIE) regimes or other regimes deemed harmful and in light of commitments made to repeal or amend those regimes.

Australia, Eswatini and Maldives were removed from the document, having fulfilled all their commitments. No jurisdictions were added to Annex I (the list of non-cooperative jurisdictions).

Following this latest revision, the EU list of non-cooperative jurisdictions includes the following nine jurisdictions: American Samoa, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands, Vanuatu.

The grey list includes the following fifteen jurisdictions: Anguilla, Barbados, Botswana, Costa Rica, Dominica, Hong Kong (SAR), Jamaica, Jordan, Malaysia, North Macedonia, Qatar, Seychelles, Thailand, Turkey and Uruguay.

Background

The EU list of non-cooperative jurisdictions, first adopted in the Council conclusions of December 5, 2017, is part of the EU's efforts to clamp down on tax avoidance and harmful tax practices. Out of the ninety-two jurisdictions initially chosen for screening, seventeen jurisdictions were placed on the list in December 2017. Since then, in light of commitments made by listed jurisdictions to comply with the EU's criteria, both Annex I (the EU list of non-cooperative jurisdictions) and Annex II / the EU grey list (jurisdictions whose commitments to comply with EU standards are being monitored) to the Council conclusions) were amended several times. Please refer to Euro Tax Flash issue 442 for details of the state of play following the previous revision of the lists (February 22, 2021).

In October 2019, the Council approved guidance on FSIE regimes in the framework of the EU listing exercise (criterion 2.1 – fair taxation, e no preferential tax measures that could be regarded as harmful). According to the guidance, FSIE regimes are not, in themselves, harmful. In fact, exempting foreign profits is acceptable and even recommended for the prevention of double taxation. However, the EU considers such regimes problematic when they not only prevent double taxation, but also create situations of double-non taxation.

The guidance suggests that a harmful FSIE regime could be amended either:

- by introducing the taxation of passive income; or
- if certain types of passive income are excluded from taxation:
  a) by implementing adequate substance requirements to the entities concerned, in line with the EU's Code of Conduct (Business Taxation);
  b) by having robust anti-abuse rules in place; and
  c) by removing any administrative discretion in determining the income to be excluded from taxation.

In addition, jurisdictions should ensure the application of international principles in relation to the taxation of active income, notably with regard to the definition of permanent establishment provided by the OECD Model Convention on Double Tax Treaties (including by amending the definition of permanent establishment in a DTA in place already that does not respect international principles) and the consequent income allocation.

Against this background, on December 5, 2019, the Council approved a list of thirteen FSIE regimes to be investigated and invited the Code of Conduct Group (CoCG) to start with its assessment of these regimes. The COCG Chair informed the thirteen jurisdictions that a regime of this kind was identified in their tax system and the Commission services followed up with a questionnaire to nine jurisdictions in February 2020. It was agreed to screen four jurisdictions at a later stage.

Update to the EU list of non-cooperative jurisdictions

On October 5, 2021, the Council agreed to:

- move Anguilla, Dominica and Seychelles to the grey list, pending a supplementary review by the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes for the purposes of assessing compliance with criterion 1.2. Under this tax transparency criterion, the jurisdictions should possess at least a "Largely

Compliant" rating by the Global Forum with respect to the OECD Exchange of Information on Request (EOIR) standard;

- keep Panama on the EU list of non-cooperative jurisdictions due to the lack of commitment to repeal or amend their harmful FSIE regime.

As a result, the EU list of non-cooperative jurisdictions (Annex I to the Council conclusions) now comprises the following nine jurisdictions: American Samoa, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands, Vanuatu.

Update to the grey list

Following the review of the nine FSIE regimes, in its conclusion of October 5, 2021 the Council approved the inclusion of Costa Rica, Hong Kong (SAR), Malaysia, Qatar and Uruguay to the grey list. FSIE regimes in these jurisdictions were deemed harmful by the CoCG. All five states have already expressed their commitment to repeal or amend their FSIE regimes. In particular, Hong Kong (SAR) committed to amending its FSIE regime such that the amended system will take effect on January 1, 2023, with no grandfathering arrangement.

Furthermore, the Council made the following additional decisions with regards to the grey list:

- Australia, Eswatini and Maldives were removed from the list;
- Anguilla, Dominica and Seychelles were added to the list, as detailed above;
- North Macedonia, which committed to amending a tax regime identified as harmful, was added to the list;
- Botswana is now compliant with criterion 1.3, but is still on the grey list under criterion 1.2;
- Jordan (partly removed, partly added);
- Qatar – committed to reform the Financial Center Science and Technology Park Free Zone and Free Zones regimes, which were identified as harmful.

As regards commitments made by Turkey regarding compliance with the Transparency criterion 1.1 (OECD Automatic Exchange of Information (AEOI) related to the Common Reporting Standard – CRS), the Council noted that the progress made by Turkey is still not fully in line with the commitments required in connection with the exchange of information with Cyprus, with which Turkey does not have diplomatic relations. The report notes that Turkey made steps to activate the exchange of data with 26 Member States, but that further engagement and technical work from Turkey will be required to meet the agreed international standards and fully comply with the requirements with the conclusions of the Ecofin Council of February 22, 2021. Consequently, Turkey remains in section 1.1 of Annex II.

As a result, the grey list now contains fifteen jurisdictions: Anguilla, Barbados, Botswana, Costa Rica, Dominica, Hong Kong (SAR), Jamaica, Jordan, Malaysia, North Macedonia, Qatar, Seychelles, Thailand, Turkey and Uruguay.

Next steps

These changes will take effect from the day of publication in the Official Journal of the European Union of the revised Annexes I and II.

The CoCG will continue to monitor the implementation of commitments assumed and seek commitments from those jurisdictions that have not addressed their weak points so far.

The next revision of the EU list of non-cooperative jurisdictions is scheduled for February 2022.

EU Tax Centre comment

As previously reported (see KPMG's EU Tax Centre ETF 435 and ETF 442 for more details), in December 2019, the Council issued guidance on coordination of national tax defensive measures against non-cooperative jurisdictions, whereby Member States were invited to apply at least one of the legislative defensive measures suggested by the CoCG as of January 1, 2021 (or July 1, 2021 should they face institutional or constitutional issues):

— non-deductibility of costs;
— Controlled Foreign Company (CFC) rules;
— withholding tax measures;
— limitation of participation exemption on profit distribution.

Several EU countries have already introduced or proposed measures targeted at jurisdictions on the EU list. For further information, please refer to our summary of defensive measures against non-cooperative jurisdictions for tax purposes which provides a high level overview of defensive tax and administrative measures adopted by a selection of EU / EEA jurisdictions, plus the UK, against countries included on the EU list of non-cooperative jurisdictions for tax purposes as well as on equivalent national lists, where applicable.

It is expected that other Member States will follow in consideration of the CoCG's review of defensive measures, which was scheduled to start by July 2021.

Should you have any queries, please do not hesitate to contact KPMG's EU Tax Centre, or, as appropriate, your local KPMG tax advisor.

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