Euro Tax Flash from KPMG's EU Tax Centre

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EU Code of Conduct Group reports to ECOFIN

Code of Conduct Group (Business Taxation) – Harmful Tax Practices – Preferential Tax Regimes – Defensive Measures – EU List of Non-Cooperative Jurisdictions

On December 7, 2021, the Economic and Financial Affairs Council of the EU (ECOFIN Council) approved the Code of Conduct Group's report on the work performed during the Slovenian Presidency (second half of 2021), which includes the following sections:

- Revision of the mandate of the Code of Conduct Group;
- Current state of the standstill and rollback review process;
- Update on the Group's screening and listing exercise with regards to non-cooperative jurisdictions;
- Overview of the defensive measures against non-cooperative jurisdictions currently applied by Member States.

Background

On December 1, 1997, the ECOFIN Council adopted conclusions on a legally non-binding Code of Conduct (the "Code") focusing on the identification and withdrawal of harmful tax measures. As a next step, the Code of Conduct Group (the "Group") was set up on March 9, 1998 to focus on the Member States' commitment to eliminate existing harmful tax practices (rollback process), while refraining from implementing new ones (standstill process) in accordance with the Code.

In December 2017, Member States also agreed on promoting the adoption of transparency and good governance principles by third countries by way of a common EU list of non-cooperative jurisdictions for tax purposes. Since then, the list has been regularly revised based on the work performed by the Group (see Euro Tax Flash issues 442 and 457 for the latest developments).

Furthermore, in December 2019, the ECOFIN Council adopted guidance on coordination of national defensive measures in the tax area against non-cooperative jurisdictions, inviting Member States to apply legislative defensive measure as of January 1, 2021 (or July 1, 2021 should they face institutional or constitutional issues). The Group committed to reviewing the work on legislative defensive measures in the tax area and have an overview of such measures applied by Member States in place by the end of 2021 (see Euro Tax Flash issues 419 and 435 for more details).

With respect to the different actions it has been mandated with, the Group regularly reports to the ECOFIN Council on the work performed during each Council Presidency.

Work performed by the Group during the Slovenian Presidency

The Group's report, as approved by the ECOFIN Council on December 7, 2021 (Group's report) details the work performed during the Slovenian Presidency as follows:

No agreement on a revised mandate of the Code of Conduct Group

In its conclusions on fair and effective taxation in times of recovery, on tax challenges linked to digitalisation and on tax good governance in the EU and beyond of November 27, 2020, the ECOFIN Council had welcomed discussions on the revision of the mandate of the Group and agreed that the scope should also cover features of tax systems that have general application and that may have harmful effects.

In an initial draft of the Group's report to the ECOFIN Council dated November 26, 2021, the Group presented its revised Code proposal. However, during a press conference held after the ECOFIN Council meeting on December 7, 2021, the Slovenian Minister of Finance (Andrej Šircelj) announced that Member States did not agree on the revised Code proposal prepared by the Group.

The revised Code proposal provided for an expanded definition of harmful tax regimes to cover features of tax systems that have general application and that may have harmful effects, provided for additional options to rollback harmful tax regimes, and for stricter rules for the exchange of information on new potential harmful tax measures.

Current state of the standstill and rollback review process

The Group's report notes that a number of newly identified tax measures do not need to be assessed by the Group (including Italy's introduction of tax credit to the Budget law[1], Lithuania's corporate income tax for companies implementing large projects[2] and Romania's tax measures to support the maintenance/increase of own capitals (for the last two the future application should be monitored)[3].

With respect to the standstill review, the Group's report makes reference to a number of preferential tax measures due to be assessed (including Croatia's reduction of the tax rate for

[1] See doc 14230/21 ADD 1.

[2] See doc 14230/21 ADD 2.

[3] See doc 14230/21 ADD 3.

small and mid-sized taxpayers). In addition, it was decided that the standstill review of Romania's profit tax exemption for companies with innovation and R&D activities is kept on hold until the relevant national legislation is adopted.

As regards the rollback review process, the Group's report notes that Poland informed the Group that legislative work has been completed regarding two out of the three aspects raised in the assessment of Poland's Investment Zone[4] while the amendment of the third aspect is still pending. The Group agreed to examine the adequacy of the rollback as soon as the work in respect of the third aspect is completed.

Update on the Group's screening and listing exercise with regards to non-cooperative jurisdictions

The Group's report also details the work performed with regards to the revised EU list of non-cooperative jurisdictions, which was approved by the ECOFIN Council on October 5, 2021 and published in the Official Journal on October 12, 2021 (see Euro Tax Flash issue 457 for more details).

As regards the future transparency **criterion 1.4** (exchange of beneficial ownership information), which was already approved by the ECOFIN Council in November 2016, the Group's report notes that due to COVID-19 it was not possible to have further discussions on this and that the Group will need to come back on this additional criterion at a later stage.

With respect to the assessment of harmful tax regimes (criterion 2.1) and tax regimes that facilitate offshore structures which attract profits without real economic activity (criterion 2.2), the Group's report links to an updated overview of foreign jurisdictions' preferential tax regimes and other measures examined by the Group. The report provides updates in respect of a number of regimes including:

- The Group formally endorsed the assessment of the Russian tax regime "International Holding Companies" (Special Administrative Regions) as overall harmful and initiated a dialog with the competent Russian authorities.
- It is clarified that, following the review of nine foreign source income exemption (FSIE) regimes, in total six FSIE regimes were deemed harmful by the Group. While five jurisdictions, namely Costa Rica, Hong Kong (SAR), China, Malaysia, Qatar and Uruguay, already expressed their commitment to repeal or amend their regimes (and were added to the grey list - as previously covered in Euro Tax Flash issue 457), the Group's report notes that Panama did not express the requested commitment. The remaining three FSIE regimes of Maldives, Nauru and Singapore were deemed compliant under criterion 2.2.

With respect to **criterion 3.2** on country-by-country reporting (CbCR) it is announced that the Group agreed on the assessment of the relevant jurisdictions for compliance with the exchange of information requirements under this criterion in view of the update of the EU list in February 2022. The general approach for the assessment was agreed in 2019 and comprises two main elements:

[4] See doc ST 14114/19 ADD 3.

- Jurisdictions should have arrangements (multilateral or bilateral qualifying competent authority agreement) in place to exchange CbCR reports with all Member States with whom they already have an international agreement in effect (MAC or bilateral Double Tax Convention / Tax Information Exchange Agreement that provides for the automatic exchange of tax information) by the end of 2019.
- Jurisdictions should be assessed positively in the Inclusive Framework's Phase 3 peer reviews.

Lastly, in respect of the geographical scope of the EU screening exercise, the Group's report notes that further work is required in terms of reviewing the economic data used for selecting jurisdictions, which had been previously already planned for the selection in 2020, for application as from 2021.

Overview of the defensive measures currently applied by Member States

Finally, the annex of the Group's report includes an overview on the implementation of defensive measures in the tax area against non-cooperative jurisdictions applied by Member States in line with the guidance on defensive measures agreed by the ECOFIN Council in December 2019.

For more information on defensive measures adopted by Member States, please refer to KPMG's summary of defensive measures against non-cooperative jurisdictions for tax purposes

EU Tax Centre Comment

The work of the Group is under the scrutiny of the European Parliament, which recently adopted a resolution (October 21, 2021) calling the current list of non-cooperative jurisdictions a "blunt instrument" which has been watered down by Member States' finance ministers (for previous coverage please also refer to E-news issue 142).

In particular, Members of the European Parliament (MEPs) called on the ECOFIN Council to agree on the forthcoming transparency criterion 1.4 as a matter of urgency and to consider the conclusions and recommendations of the Parliament's resolution of January 21, 2021 on reforming the EU list of non-cooperative jurisdictions in terms of broader and stricter listing criteria and coordinated defensive measures (for more details on the January resolution please refer to Euro Tax Flash issue 440). As resolutions adopted by the European Parliament are not binding on the Council of the EU and the European Commission, the request on reforming the EU list of non-cooperative jurisdictions and the work performed by the Group in that regard remains at the discretion of the two institutions. It therefore remains to be seen how much the Group's work under the incoming French Presidency will be impacted by the current reform discussions.

Furthermore, as regards the failed revision of the Code, during the meeting of the European Parliament sub-committee on tax matters (FISC) on November 30, 2021, the European Commissioner for Economy (Paolo Gentiloni) welcomed the proposal of an "initial" reform of the Code but also informed MEPs that two Member States, namely Estonia and Hungary, were blocking the reform. In a press release issued on December 7, 2021, the Estonian government explained that they first want to monitor the results of the implementation of the OECD's global tax reform before revising the mandate of the Group. Against this background, it remains to be seen whether the ECOFIN Council can agree on a revision of the mandate before 2023 (when

the OECD's global tax reform is currently scheduled for) as changes to the Code require consensus between the Member States.

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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