Euro Tax Flash from KPMG's EU Tax Centre

Conclusions of June 21 ECOFIN meeting

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Key Summary:

On June 21, 2024, the final scheduled meeting of the Economic and Financial Affairs Council of the EU (ECOFIN) under the Belgian Presidency of the Council took place.

Key takeaways related to direct tax initiatives include:

- the ECOFIN approved a report to the European Council, which provides an overview of the progress achieved in the Council on a range of direct tax initiatives, including on the FASTER, Unshell, Transfer Pricing and BEFIT directive proposals.
- the ECOFIN Council also approved a report by the Code of Conduct Group on its work performed during the term of the Belgian Presidency (first half of 2024).

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Council of the EU – Pillar Two – FASTER – Unshell – BEFIT – Transfer Pricing – UN Tax Committee – Code of Conduct Group (Business Taxation) – Preferential tax measures – List of non-cooperative jurisdictions

On June 21, 2024, the final scheduled meeting of the Economic and Financial Affairs Council of the EU (ECOFIN Council) under the Belgian Presidency of the Council took place.

June ECOFIN meeting

During the meeting, the ECOFIN Council approved a report to the European Council (the ECOFIN report), which provides an overview of the progress achieved in the Council on a range of EU direct tax initiatives, including on Directive proposals such as FASTER, Unshell, Transfer Pricing and BEFIT.

The ECOFIN Council also approved a report by the Code of Conduct Group ('CoCG' or 'the Group') on its work performed during the first half of 2024 under the Belgian Presidency (the Group's report).

Background

On January 1, 2024, Belgium succeeded Spain in holding the Presidency of the Council of the EU for the first half of 2024. According to the program published by Belgium at the beginning of the term, key priorities from a direct tax perspective included:

- prioritizing measures aimed at curbing tax evasion, tax avoidance, aggressive tax planning and harmful tax competition (i.e., updating EU's list of non-cooperative jurisdictions, progressing the FASTER initiative, etc.);
- welcoming the Business in Europe Framework for Income Taxation (BEFIT) package;
- exploring the usefulness of more unified tax rules in other fields over the longer term (e.g., in relation to mobile workers);
- supporting the implementation of the Unshell Directive and backing the SAFE initiative;
- conducting work to ensure greater tax transparency and reinforcing the exchange of relevant information within the EU, in particular concerning the effective functioning of the Minimum Tax Directive.

In December 2023, the CoCG reported to the Council on the work undertaken in the second half of 2023 and on future direction. Key items included:

- current state of the standstill and rollback review process in relation to preferential tax measures;
- assessment of cooperative compliance programs in the EU;
- update on the EU listing exercise and defensive measures against non-cooperative jurisdictions and on-going work on a further strengthening of the EU list and a gradual extension of its geographical scope.

For more information, please refer to E-News Issue 189 (priorities of the Belgian Presidency) and Euro Tax Flash Issue 529 (ECOFIN report and COCG's report).

ECOFIN report – Update on files related to direct tax

ECOFIN report

The ECOFIN report details progress made in the area of direct taxation at ECOFIN level during the first half of 2024, as follows:

FASTER: Council reaches agreement (general approach) on the proposal

On June 19, 2023, the EC issued a proposal for a Council Directive providing for the "Faster and Safer Relief of Excess Withholding Taxes (FASTER)", which aims to make withholding tax procedures in the EU more efficient and secure for investors, financial intermediaries, and local tax authorities.

FASTER

The ECOFIN report notes that a compromise text (general approach) in relation to the Council Directive for a "Faster and Safer Relief of Excess Withholding Taxes" was agreed at ECOFIN level on May 14, 2024, with a view to adopting the Directive following re-consultation with the European Parliament and legal-linguistic revision.

Unshell: Council presents a new approach to move forward

Unshell

On December 22, 2021, the EC issued a proposal for a Directive aimed at fighting the use of shell entities and arrangements for tax purposes (Unshell). The initial proposal set out a list of indicators to filter entities at risk of being misused for tax purposes. High-risk entities would then be required to report on a series of substance indicators through their annual tax return. Companies failing to meet the substance indicators would be deemed to be 'shell' entities, potentially triggering tax consequences.

Since then, the text of the Directive has been subject to discussions in the Council working groups. As previously reported, several compromise texts were submitted but Member States were not able to reach consensus on the initiative.

The report notes that, in principle, most delegations have supported the objectives of the proposal, but were of the view that further important technical work was necessary before an agreement could be feasible. Among the most discussed issues, the report lists tax consequences, links with domestic anti-abuse legislation, excluded entities, minimum substance, rebuttal of the presumption and reduction of administrative burden, tax residency certificate and exchange of information.

According to the report, the Belgian Presidency presented a possible way forward at the High Level Working Party (HLWP) on June 11, 2024, which will be subject to further discussions to find compromise solutions on outstanding issues.

Transfer Pricing proposal: Member States reject proposal in its current form

Transfer Pricing proposal

The ECOFIN report provides a status update on the Transfer Pricing Directive proposal, which was released by the European Commission in September 2023. The proposal aims at implementing common TP rules into EU law including the incorporation of the OECD arm's length principle and a reference to the 'OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations' into EU law.

According to the ECOFIN report, while the initial discussions on the Commission proposal showed that Member States generally support the objectives of the proposal, some raised general concerns about the inclusion of transfer pricing rules into an EU Directive. The report also notes that specific concerns were raised about the risk of possibly creating a double standard in the field of transfer pricing (i.e., at the OECD level and at the EU level), as well as about the loss of flexibility available to Member States in negotiating and applying the OECD Transfer Pricing Guidelines.

In addition, the report indicates that discussions on this file at the level of the Working Party on Tax Question (WPTQ) showed that the Directive proposal will not be supported by Member States in its current form. Finally, the ECOFIN report notes that Member States have expressed interest in establishing a new EU Transfer Pricing Platform, which would be (to a certain degree) comparable with the Joint Transfer Pricing Forum (JTPF)[1].

According to the report, further work would be required on such a "*soft law*" approach, including decisions on the composition of the Platform (membership), its institutional set-up (in relation to Member States and Council), its mandate (scope, duration, competence, deliverables), its governance (chairmanship chair function (elected or appointed), voting rules and secretariat services), as well as other relevant aspects of substance and/or process (such as public access to documents.

BEFIT proposal: Council highlights the need for political and technical discussions

The ECOFIN report provides a status update on the BEFIT proposal, which was released by the European Commission in September 2023 and provides common rules for determining the corporate tax base for EU-based entities that are part of a group with global consolidated revenues above a certain threshold. BEFIT would

[1] The JTPF was established in 2002 and operated until 2019. It worked within the framework of the OECD Transfer Pricing Guidelines and proposed to the Commission, on the basis of consensus, pragmatic, non-legislative solutions to practical problems posed by transfer pricing practices in the EU.

also include provisions for the allocation of profits to relevant Member States. Once allocated, profits would be subject to the corporate income tax rate of the respective Member State.

BEFIT proposal

The ECOFIN report notes that, while the overall objectives of simplifying corporate taxation rules in the EU and reducing the administrative burden for businesses and tax authorities were supported by Member States, multiple concerns were expressed on whether the Directive, as proposed by the Commission, would successfully achieve these goals. According to the report, the concerns focus on the interplay of the BEFIT rules with existing tax legislation (including national corporate tax rules, Pillar Two rules, EU anti-abuse measures) and also on the scope and determination of the preliminary tax result of in-scope groups.

Finally, the report mentions that some Member States called for a political discussion (which was then removed from the ECOFIN meeting agenda) and acknowledges that further reflection and technical work will be required to determine the next steps in these negotiations during the Hungarian Presidency (second half of 2024).

Head Office Tax System (HOT): political discussion to take place before any further technical work

The ECOFIN report provides a status update on the HOT proposal, which was released by the European Commission in September 2023. The Directive would allow certain EU-based standalone SMEs that operate in other EU Member States only through permanent establishments (PEs) to make a five-year election to determine the taxable results of the PEs according to the rules of the Member State of their head office.

HOT proposal

According to the report, several Member States raised serious concerns as regards several aspects of the proposal, such as the administrative challenges that the current proposal may create for tax authorities, concerns about the potential effect on tax revenues and tax sovereignty of Member States as well as risks linked to competitiveness of the domestic markets.

It is further noted that a number of Member States are of the view that a more general discussion on this file should take place before any further technical progress can be made. The ECOFIN report also mentions that additional work on this file could continue with the objective of preparing a high-level discussion on the policy choices that would need to be made.

United Nations (UN) resolution on promoting inclusive and effective international tax cooperation

On December 22, 2023, the General Assembly of the United Nations (UN) approved a resolution which establishes a newly created intergovernmental Committee for the purpose of drafting terms of reference for a UN framework convention on international tax cooperation.

UN framework convention

In this regard, the ECOFIN report notes that the Belgian Presidency continued to update the HLWP on the state of play of the ongoing discussions at the UN and facilitated the adoption of a common position on behalf of the European Union and its Member States that was delivered during the first substantive session of the UN Ad Hoc Committee on April 26, 2024.

The Belgian Presidency informed the ECOFIN Council on the outcome of the first session of the Ad Hoc Committee. According to the Presidency, the Ad Hoc Committee Chair proposed a timeline for the next steps, including the circulation of a zero-draft of the terms of reference and opportunities for written submissions from UN Member States and stakeholders in the lead-up to the second substantive session. The Presidency also reported that the session highlighted the existence of notable differences in the positions of various UN Member States and groups, particularly between developed and developing countries and the need for further work to make progress with the aim of achieving consensus on some of the issues, whilst ensuring that the framework effectively addresses the needs of all countries.

Work performed by the Code of Conduct Group during the Belgian Presidency

CoCG's report

The CoCG's report, as approved by the ECOFIN Council on June 21, 2024 (Group's report) details the work performed during the Belgian Presidency.

Current state of the standstill and rollback review process in relation to preferential tax measures

The Group's report notes that a call for standstill and rollback notifications of new preferential tax measures enacted by the end of 2023 was launched in November 2023, and the results were presented at the CoCG meeting of February 7, 2024. The following regimes were notified:

Standstill and rollback review process

- *Italy*: Tax credit for investments in the Single Economic Zone for the year 2024;
- *Italy*: Tax credit for research and development in the microelectronics sector;
- *Italy*: Additional income tax deduction to encourage an increase in the employment base and open-ended employment contracts;
- *Lithuania*: Amendments to the CIT tax for companies implementing large-scale projects;
- *Portugal*: Tax Regime to Incentivize the Capitalization of Companies;
- *Portugal*: Madeira Free Trade Zone (MFTZ).

The following decisions were made by the COCG:

- The Group agreed that (i) Italy's Additional income tax deduction to encourage an increase in the employment base and open-ended employment contracts, as well as (ii) Lithuania's Amendments to the CIT tax for companies implementing large-scale projects do not need to be assessed by the Group.
- The Group agreed that Portugal's MFTZ does not need to be assessed by the Group. Nevertheless, Portugal committed to providing the Group with the number of entities licensed between January 1, 2023 and December 31, 2024 to operate in the MFTZ, by year and by business sector.
- A new version of the Croatian Investment Promotion Act was implemented. In this regard, the Group stresses that the previous assessment remains valid such that the rollback notification is still pending and should be extended to the New Investment Promotion Act.
- The Group's report also notes 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.

With respect to measures that were subject to scrutiny and put under annual monitoring in order to assess their impact on business location decisions, the Group's report notes that Member States should provide the Group with the relevant data (for year 2022) by the end of June. This shall enable the Group to investigate the actual effects of such measures during the second half of 2024. The report further notes that the Group will consider the effects of the few remaining measures from the 2023 monitoring cycle for which no sufficient data was available.

Update on the EU listing exercise and defensive measures against non-cooperative jurisdictions

The Group's report details the work performed with regards to the revised EU list of non-cooperative jurisdictions ("Annex 1") and commitments taken by cooperative jurisdictions to implement tax good governance principles ("Annex 2" or "grey list"). The most recent amendments to the two lists were approved by the ECOFIN Council on February 20, 2024 and published in the Official Journal on February 26, 2024. For more information about the latest update of the EU list of non-cooperative jurisdictions, please refer to Euro Tax Flash Issue 538.

According to the Group's report, additional developments in relation to the EU listing exercise that occurred after the last update of the list include:

EU listing and defensive measures

- *New Criterion 1.4 (beneficial ownership information):* The Group's report notes that work and discussions on the design of this new criterion continued in the first half of 2024.
- *Criterion 2.*1 (no harmful preferential tax measures): The Group's report notes that the Forum on Harmful Tax Practices (FHTP) decided at its meeting on May 14 and 15, 2024, that the Armenian "Free economic zones" and the "Special economic zones" regime in Eswatini are not harmful as amended. Regarding the foreign source income exemption regimes, the report mentions that the FSIE regime in Malaysia was amended to meet COGG requirements and that the Group will draw a conclusion on the regime in the next update of the EU list.
- *Criterion 2.2 (no facilitating of offshore structures):* The report notes that since the FHTP concluded that the United Arab Emirates is no longer a *no or only nominal tax jurisdiction* with the introduction of a 9 percent corporate income tax, the CoCG does not need to assess this jurisdiction under criterion 2.2. In addition, the Group's report notes that the CoCG continues its specific monitoring for Collective Investment Funds and partnerships.

- *Criterion 3.2 (implementation of County-by-Country Reporting (CbCR) minimum standard):* The Group's report highlights that the CoCG started focusing on jurisdictions that joined the BEPS Inclusive Framework (IF) since January 1, 2018, and that were subject to the 2023 Global Forum peer review and have not fully implemented the global standard on CbCR. According to the Group's report, the CoCG asked these jurisdictions to provide information about MNEs and was informed about the replies from 18 jurisdictions in April 2024. It is further noted that the Group will take stock of progress in the relevant jurisdictions and decide on possible requests for commitments based on the 2024 peer review report, which is expected to be released in September 2024.

At its meeting on November 22, 2023, the CoCG considered a proposal with a view to monitor the implementation of tax defensive measures. The Group's report notes that in the first half of 2024, the Group agreed on a revised paper on the approach and the monitoring questionnaire for the annual monitoring of tax defensive measures and indicates that the first monitoring exercise will take place in 2025 with respect to the application of the measures in 2021.

Finally, the Group's report notes that the CoCG discussed at its previous meetings the possibility to extend the geographical scope of the EU listing exercise and agreed to include Brunei Darussalam, Kuwait and New Zealand. It is indicated that the Chair sent letters to the jurisdictions in December 2023 announcing that the screening process for the implementation of the EU list criteria had started. The Group's report further notes that the Group will reflect on the most appropriate indicators to select additional jurisdictions for future extensions of the geographical scope of the EU list.

Next steps

Hungarian Presidency

Hungary will take over the Presidency of the EU as from July 1, 2024. According to their program, the objective is to effectively advance the discussions on the taxation files and international issues currently on the agenda, in order to achieve progress which responds to the needs posed by new business models, international cooperation, and fiscal revenues. The high-priority areas outlined by the Hungarian Presidency are (i) fighting tax evasion, (ii) ensuring legal certainty for taxpayers, and (iii) supporting the international engagement of the European Union.

ETC Comment:

It is anticipated that the Council working groups will continue working on all of the pending files. However, it remains to be seen which ones will be effectively treated as priorities by the Hungarian Presidency. In addition, we have seen several Member States expressing concerns on the different initiatives currently on the agenda (BEFIT, TP Directive, Unshell), highlighting the need for further political and technical discussions to find compromise solutions on the outstanding issues.

Whilst the Belgian Presidency was able to facilitate an agreement (general approach) on the FASTER proposal, the Directive has not yet been formally adopted. During the ECOFIN meeting on May 14, it was clarified that the final text of FASTER would be sent to the Council for formal adoption after legal linguistic revisions have been finalized and once a revised opinion is issued by the European Parliament on the final text. In light of the recent EP elections, it is expected that the formal legislative process will not be completed before early 2025.

With regard to the ongoing work taking place at the level of the UN, the Bureau of the Ad Hoc Committee released on June 7, 2024, a proposal for the zero draft terms of reference for an UN framework convention on international tax cooperation. The document sets out the basic parameters and mechanisms of a UN Framework Convention on International Tax Cooperation and aims to provide guidance to the negotiation of the framework convention. A public consultation on the draft was open until June 21, 2024, to which KPMG was pleased to contribute.

The status of other EU direct tax initiatives that have not been mentioned in the ECOFIN report can be summarized as follows:

- *EU Minimum Taxation (Pillar Two):* All EU Member States were required to transpose the EU Minimum Tax Directive by December 31, 2023. On May 23, 2024, the EC sent reasoned opinions to Cyprus, Latvia, Lithuania, Poland, Portugal and Spain for failing to transpose the Directive into domestic legislation. In addition, the EC announced its intention to expand the scope of the Directive on Administrative Cooperation to facilitate the exchange of information in relation to minimum taxation rules under Pillar Two (DAC9). A draft proposal is expected once further progress has been made at the level of the OECD / Inclusive Framework.
- *Public Country-by-Country Reporting*: All EU Member States were required to transpose the Directive into national law by June 22, 2023. On May 23, 2024, the EC sent reasoned opinions to Austria, Belgium Cyprus, Italy, Finland and Slovenia for failing to transpose completely the EU Public CbyC reporting into domestic legislation.

Finally, it should be noted that a new legislative term of the European Parliament has started with the European elections that took place on June 6 to 9, 2024. Members of the European Parliament (MEPs) will first elect a new President of the European Parliament during the first plenary session, which will take place on July 16 to 19, 2024, but also a new President of the European Commission at a later stage. The new Commission will also be required to obtain Parliament's approval in a plenary vote before taking office. Therefore, this process could also have an impact on the agenda of the EU as regards direct tax matters. As things stand, European Commission work plan for 2024 includes a review of the Directive on Administrative Cooperation (DAC), Unshell, Carbon Border Adjustment Mechanism (CBAM) and cross-border mobile workers.

Additional relevant links

- Euro Tax Flash Issue 521 – European Commission publishes BEFIT and Transfer Pricing proposal
- Euro Tax Flash Issue 522 – European Commission publishes Head Office Tax system for SMEs
- Euro Tax Flash Issue 529 – Conclusions of December 8 ECOFIN meeting
- Euro Tax Flash Issue 538 – February 2024 update of the EU list of non-cooperative jurisdictions
- Euro Tax Flash Issue 541 - Council agrees on new rules for harmonized withholding tax procedures in the EU (the FASTER Directive)
- E-News Issue 189 – Priorities of the Belgian Presidency of the Council of the EU released
  E-News Issue 195 – DG TAXUD publishes work plan for 2024

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