2024.01.24 Hearing on BEFIT

0 – Opening

I would like to thank the EESC for the kind invitation to present my technical views on BEFIT.

It is for me a pleasure to take part on this hearing and present some conclusions of a more comprehensive study published on the topic, drafted together with my colleagues Pasquale Pistone, Ivan Lazarov, Alessandro Turina and Sergio Messina.

The statements at this hearing are made on a personal basis, and are not intended to represent the views of my affiliation institutions.

1 – Structure

This statement will focus on **three** main areas:

a) Firstly, I will make an overall assessment of the proposal;

b) Secondly, I will focus on specific technical issues;

c) Thirdly, I will conclude with some reccomendations.

2 – Let's start with an overall assessment of the proposal

From a technical perspective, the BEFIT proposal appears to be feasible, neutral and adequate;

> - feasible since it offers a technical solution which can effectively be implemented in the short-term without requiring significant investment of resources or technical training of staff;
>
> - neutral (or mostly neutral) in the sense that, unlike CCCTB, the allocation of the taxable base between Member States remains mostly the same, avoiding the emergence of winners and losers (as in the CCCTB);
>
> - adequate: since the measure has the potential to be an appropriate tool to reach its underlying goal of simplifying tax compliance within the internal market;

However, notwithstanding such a positive assessment, there are still some technical issues that have to be addressed before adoption.

3 – Outstanding technical issues

In the impossibility of addressing all the technical challenges, I will cover only a small number of selected issues, illustrative of the type of problems that must be addressed.

3.1 Regarding the scope

In the definition of the mandatory scope, and in addition to general requirements, the proposal refers to annexes. Such annexes list different conditions per country. Accordingly, it is possible that two identical companies are treated differently (in the sense that one will be within the scope and the other out) just because they are incorporated in different EU Member States.

- just as an example, a company not carrying commercial activities (but generating profit) would qualify for BEFIT in most countries but not in Bulgaria.

[constituted under Bulgarian law and carrying on commercial activities]

In our view, the proposal needs to be revised in order to ensure that the eligibility conditions are the same, regardless of the Member State where companies are incorporated.

3.2 Regarding the compatibility with tax treaties

The proposal includes provisions that interact with tax treaties (which are instruments of public international law) and sometimes deviate from those provisions. That is the case, namely:

+ of the "EU materiality threshold" that distinguishes between groups with the ultimate parent in the EU and the ultimate parent outside the EU; in comparable situations, EU groups are mandatorily within BEFIT whereas non-EU groups will not be: that may be a breach of Art. 24(5) of the treaties, which requires companies not to be discriminated on the basis of having a foreign parent;

+ issues may also arise regarding the computation of profits of Permanent Establishments; BEFIT directly applies the OECD authorised approach and, for that reason, is not aligned with older treaties or with the specific treaty practice of Member States that do not align with the AOA (for example, Austria);

Of course, within the EU and between Member States, this interaction with EU law is not problematic. EU law will prevail over tax treaties.

However, this is not always the case in what concerns third countries, according to Art. 351 of the TFEU.

+ of course, post-1958 or post-accession treaties may not be invoked (according to Art. 351); but Member State would be in default on their treaty obligations under international law absent a renegotiation.

+ However, pre-1958 or pre-accession treaties, they do prevail over EU law and they may be invoked by taxpayers, precluding the application of the provisions of BEFIT; Member States are under an obligation to revise those treaties, but until they do, taxpayers may invoke the treaty undermining the uniform application of BEFIT.

In our view, this issue needs to be handled with care, either revising BEFIT provisions to prevent the interaction with treaties or providing a template treaty to amend the pre-1958 or pre-accession treaties (or, more broadly, all incompatible treaties with third countries) that can still be invoked by taxpayers.

2.4 Alignment with other EU law instruments and, particularly with Pillar II

Another issue is the alignment of BEFIT with the remaining secondary law and, particularly, with Pillar II. The Explanatory Memorandum explains, in a simplistic manner, that the rules should be "aligned as closely as possible with the Two-Pillar approach". However, this is not the case and there are deviations:

+ at the level of the acceptable accounting standard;

+ in the exclusion of dividends and capital gains

+ in the treatment of foreign exchange gains of losses.

The overall question is: is there a pressing policy reason that requires such deviation? Examining both proposals carefully, I could not identify such pressing policy justification. Accordingly, further efforts should be made to align the two proposals.

3.3 Now let's move to the problematic 48(2)

BEFIT aims at harmonising the determination of the taxable base. But then introduces a provision – art. 48(2) which allows all Member States, at their discretion, to increase or decrease, through additional items, the allocated part of the BEFIT group regarding their residents.

This means, in practice, that even if there is harmonisation at the level of the BEFIT taxable base, later on, Member States are allowed to completely annul such harmonisation by introducing, at their will, any additional elements for the purposes of the determination of the taxable base of their residents.

3.4 One stop shop and simplification of the compliance

BEFIT aims at simplifying compliance costs and at introducing a one-stop shop solution for groups. However, in practice, it requires the BEFIT informational return return (art. 57) and the individual tax return (art. 62). Instead of simplification, BEFIT introduces an additional filling at the filling entity level.

If simplification is really the goal, the better option would have been a single filling, following by a system of exchanges between the involved tax authorities.

4 – Recommendations

In our view, and besides the amendment of the technical issues of the type that were just illustrated (and that are comprehensively mapped in our study), it would be important to take on board the following issues:

- Creation of a technical working group (or a group of parallel topical working groups), formed by scholars and representatives from tax authorities, to address technical flaws of the proposal on a politically neutral basis; in the work of such group, the focus could be on:

- I believe that one should focus on simplifying compliance:

i) the proposal already simplifies compliance by introducing a single set of rules within the EU;

ii) however, it could go even further; if the proposal is based on financial consolidated statements which are either public or can be publicised, then it would make more sense that compliance would be aggregated, and with a single action, companies could comply with their tax and non-tax obligations;

iii) in case the Member States do not want to be so ambitious, it would always be possible to create an harmonised or single EU-return for all tax-compliance derived from the EU, which in direct taxation covers the DACs (1 to 9), the private and public CbCr, the Pilar II; and shortly, besides BEFIT, there will be HOT, TP directive, FASTER and Unshell.

iv) in general, it would be important to focus on IT solutions, making them available for tax authorities and businesses that would allow them to decrease their administrative and compliance costs.

- it is important to be mindful of the pace of tax developments

i) even for full-time researchers, it is quite difficult to keep up with the huge number of amendments, which add up to those decided at the domestic level; for businesses concerned with many other issues, this is even more difficult;

ii) maybe one could distinguish between, on the one hand, the political timing and using momentum to approve the proposals and, on the other hand, on the real economy timing, granting a bit more space for companies to adjust and implement all these proposals.

- in my view, the technical discussion on BEFIT should be accompanied by a political discussion, which has not yet taken place at the EU level, regarding the degree of "EU federalisation" of the corporate income tax system. And that discussion has an impact on several design options of BEFIT, and namely:

- in Art. 48(2), the degree of autonomy for the states to make adjustments at will to their allocated tax base;

- in Art. 74, in what concerns the role of the Commission in adopting delegated acts;

It is quite difficult to hold a technical discussion on the rules before the political debate takes place. And in our view, it would be important to address these issues directly. Again, not at the technical level but at the political level.

4 – Concluding remarks

In conclusion, in my opinion, BEFIT would represent a step in the right direction and a decisive improvement of the internal market.

This does not mean that the proposal is perfect as it is, and amendments are not only useful but also necessary. But they are technical and they can be implemented swiftly if the right actions are promoted.

Thanks for your attention, and I am available for any questions.

Annex on the position of Austria on the AOA

"Austria follows the AOA to the extent that it is compatible with the wording of Article 7 OECD MTC prior to the changes in 2010 ("AOA light"). Austria has reserved its right to use the previous version of Article 7, i.e. the version that was included in the OECD MTC immediately before its 2010 update (see para. 96 of the Commentary on Article 7 OECD MTC). All Austrian tax treaties thus include rules for the allocation of business profits based on the "old" Article 7 OECD MTC.

For the purpose of determining the profits of a permanent establishment ("PE") this means that a two-step analysis has to be carried out: 1) analysis of the (significant people) functions, assets and risks of a PE; 2) determination of the PE's profit by pricing dealings between the PE and the rest of the enterprise on an arm's length basis using the OECD TPG by analogy. However, Austria recognises dealings only to the extent that it is in line with the OECD MTC (and its Commentaries) in its 2008 version. Accordingly, internal interest, royalty and

rental payments are generally not recognized."

https://www.oecd.org/tax/transfer-pricing/transfer-pricing-country-profile-austria.pdf

Deviations in Pillar II

Deviations also exist concerning the accounting standard: Art. 15(2) GMT allows selecting any acceptable financial accounting standard besides the one that applies to the UPE, whereas BEFIT (art. 7) requires applying the accounting standard of the UPE.

Finally, a lot of adjustments to the taxable income do not match:

+ exclusion of dividends in qualified participations: Art. 16(1)(b) of the GMT directive allows the exclusion of 100% of the dividends received, whereas Art. 8 of the BEFIT proposal only allows the exclusion of 95% of the dividends received;

+ the same happens in what concerns capital gains: 100% in the GMT directive [Art. 16(1)(c)] whereas BEFIT only allows exclusion of 95% / 100% depending on the type of gains;

+ treatment of foreign exchange gains or losses: Art. 16(e) of GMT directive only asymmetric foreign currency gains or losses, defined as a foreign currency gain or loss of an entity whose accounting and tax functional currencies are different; Art. 20 of BEFIT excludes the amount of any unrealised foreign currency exchange gain or loss in relation to fixed assets and liabilities + and the amount of any provision recorded for an unrealised foreign currency exchange loss.