Editors:
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The Implementation of Anti-BEPS Rules in the EU: A Comprehensive Study

IBFD

The Implementation of Anti-BEPS Rules in the EU

Why this book?
This book is a joint effort between the Amsterdam Centre for Tax Law (ACTL) of the University of Amsterdam, its partner institutions within the Global Tax Conference Project (New York University, the University of São Paulo and the Central University of Finance and Economics of Beijing) and IBFD, in the framework of well-established bilateral scientific cooperation.

Besides providing a comprehensive technical analysis of the EU Anti-Tax Avoidance Directive (ATAD), this book offers insight on selected issues connected with the OECD Base Erosion and Profit Shifting (BEPS) Project that are important for predicting its possible impact, including on relations with non-EU Member States.
Subjects discussed in this book are:

- EU-US relations in the field of direct taxes
- BEPS and 3D printing
- Patent boxes before and after BEPS Action 5
- Tax planning and State aid
- BEPS Action 6 and the limitation on benefits provision
- The switch-over clause
- BEPS Action 12, the lack of certainty and the infringement of taxpayers' rights
- The interest limitation rule of the ATAD
- Exit taxation and the ATAD
- General anti-abuse rules and the ATAD
- Controlled foreign company (CFC) rules and the ATAD
- The ATAD's CFC rule and third countries
- Hybrid mismatch rules under ATAD I & II
- Permanent establishment mismatches under ATAD II
- Imported mismatches

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Chapter 1

An Introduction to the Anti-Tax Avoidance Directive and the Implementation of the BEPS Project in the European Union

Pasquale Pistone and Dennis Weber*

1.1. Scope, research question and methodology

There are overt and covert links between the EU Anti-Tax Avoidance Directive (ATAD) and the OECD/G20 BEPS Project. Their interpretation and analysis will aid in better understanding the potential implications of the rules of this EU directive, which will apply within the EU internal market as of 1 January 2019.

Besides providing a comprehensive technical analysis of the ATAD, this book offers insight on selected issues connected with the BEPS Project that are important for predicting its possible impact, including in relations with non-EU Member States.

This book is largely a joint effort between the Amsterdam Centre for Tax Law of the University of Amsterdam, its partner institutions within the Global Tax Conference Project (New York University, the University of São Paulo and the Central University of Finance and Economics of Beijing) and IBFD, in the framework of well-established bilateral scientific cooperation.

The book fulfils the need for an overall assessment of the impact of the BEPS Project on the new impetus for EU positive tax integration, which, in less than a year, has made it possible to discuss and introduce rules that have the potential for shifting significant taxing powers from the national to the supranational level within the European Union.

For such purposes, it is important to share with the readers more than simply an overview of the other 19 chapters contained in the two core parts of this book.

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The ultimate goal of this book is to ascertain whether the ATAD can effectively achieve the goals that it officially proclaims and whether its rules are formulated in a way that prevents legal uncertainty and conflictive interpretation.

Various factors lead to a negative answer to both questions. Evidence of this conclusion is presented throughout this introductory chapter and in those that follow.

From a methodological perspective, the two parts of this book reconstruct the approach of the European Union to the implementation of the BEPS Project by combining the analysis of the overall framework of measures related to the ATAD with a commentary that addresses the specific implications of the measures envisaged in its various articles.

Part One comprises ten chapters, which focus on (i) the relations of the European Union with the United States and third countries; (ii) on selected issues in regard to the BEPS Project, which has served as a model for the European Union in developing and implementing its own anti-BEPS policy; and (iii) the Anti-Tax Avoidance Package of the European Union. Some chapters have a multi-faceted focus, addressing more than one of three groups of issues outlined.

Part Two includes the remaining nine chapters, which provide a comprehensive overview of relevant issues in respect of measures contained in the ATAD and its extension to third countries, known as ATAD II.

1.2. Part One: The Anti-Tax Avoidance Package and its impact on European tax law and policy in the era of global tax law

The first group of issues in Part One is examined in three chapters, namely chapters 3, 4 and 8. These chapters focus on the relations between the European Union and the United States. Chapters 3 and 4 address the same issue, namely the relations between the European Union and the United States, which they analyse as potential single regional blocs of global tax law. The analyses in these chapters share this point, but they otherwise differ in various aspects, reflecting how scholars from each side of the Atlantic Ocean perceive the BEPS Project and the emergence of international tax coordination.

In chapter 3, Haslehner submits that action by the European Commission in connection with the EU Anti-Tax Avoidance Package and the investigations into State aid in tax matters may lead to an even closer bilateral collaboration between the European Union and the United States, which would significantly reduce the national tax treaty policy of EU Member States. Haslehner predicts the possible development of external comprehensive competence for the European Union in tax matters, which may result in the gradual involvement of the European Commission in the negotiation of tax treaties of EU Member States.

In chapter 4, Shaviro outlines the various differences between the two blocs with regard to their policy goals and federalism but points out their similarities when it comes to the basic design of their income tax systems, incentives and positions as source states. After addressing the implications of their respective tax policies in the *Apple* case, Shaviro focuses his attention on the implications of the US check-the-box rules in the international context, including their effect of weakening Subpart F legislation. He addresses such issues from three theoretical perspectives, following up with a comparison with the BEPS Project and State aid investigations, which represent the European reaction to profit shifting by multinationals.

In chapter 8, Da Silva addresses limitation on benefits (LoB) provisions from the perspective of assessing their compatibility with EU law. His analysis takes into account the standards imposed by BEPS Action 6 in the light of selected case law from the Court of Justice of the European Union and scholarly interpretations, as well as the position expressed by the European Commission in the BEPS working groups and in the request for amending the Japan-Netherlands LoB clause of 19 November 2015. It is expected that this chapter will contribute to increasing awareness of such problems, in particular with regard to the relations between the European Union and the United States, which are generally covered by treaties including an LoB clause.

Since Action 6 constitutes part of the minimum standards of the BEPS Project and the BEPS Multilateral Instrument (MLI) does not allow for abandoning the LoB standards once EU Member States have adopted them, the authors suggest that such countries should instead cautiously follow the principal purpose test (PPT) approach in order to comply with the BEPS minimum standards. However, this caution may in part be impossible to exercise in light of the numerous LoB clauses that are currently included in the bilateral tax treaties of several EU Member States, in particular those concluded with the United States. In the authors' view, a possible solution

to such problems could be the negotiation of an EU Protocol Agreement to the MLI, immediately following a possible judgment that determines the incompatibility of some or all LoB clauses with the fundamental freedoms and the principles of EU law. Such a solution could be necessary in order to avoid the possible obligation of EU Member States to partially terminate the MLI in order to preserve the supremacy of EU law over the national law of the treaty source.

Various other chapters in Part One of this book address problems of the BEPS Project. In particular, chapter 2 portrays the BEPS Project as an alliance between states with antagonistic interests that is the result of a decrease in the financial resources available to support the needs of national communities. Whilst identifying the common enemy – taxpayers who do not pay taxes in any country – Schoueri points out that several states share responsibility for BEPS by structuring their systems in a way that has made it possible to exploit cross-border disparities for such purposes. Schoueri's intriguing parallel with military strategies captures the great potential of the BEPS Project, since the aligned exercise of taxing powers across borders in a holistic approach is the only effective solution to the problem. Chapter 2 also singles out possible shortcomings of the BEPS Project in connection with various Actions and serves as a framework for the analyses of other specific issues, such as those carried out in chapters 5, 6, 8 and 10.

This introduction has already outlined the main features of chapter 8. Chapters 5 and 10 correspondingly focus on cross-border taxation in connection with the digital economy (chapter 5) and the protection of taxpayers' rights (chapter 10), the former being the source of issues that have been identified –but not solved – and the latter being a domain that the BEPS Project simply did not cover.

With a combination of theoretical analysis and practical cases, in chapter 5, Olmos addresses the digital economy from the perspective of digital printing. His analysis shows the dramatic change of business models arising in the manufacturing industry in connection with this type of activity, which broadens the range of the digital economy and reinforces the need to adapt tax categories, particularly the category of permanent establishment, in order to limit the possible bias otherwise arising in such a context.

In chapter 6, Traversa and Flamini focus on the compatibility of patent box regimes with BEPS Action 5, which they also address in light of relevant developments in the European Union in a way that outlines some frictions between such regimes and the work of the EU code of conduct group.

Furthermore, they address the problems of compatibility with EU law's prohibition of State aid. This is particularly important if one considers that a large number of EU Member States have introduced this type of regime over the past few years, later being forced to gradually phase it out or amend it in order to make it compatible with the requirements and standards of the BEPS Project. Traversa and Flamini's precise historical reconstruction of the relevant developments leads to the question of whether the political compromise between Germany and the United Kingdom that has facilitated the agreement on the nexus approach should have really put an end to the analysis of the compatibility of intellectual property (IP) box regimes with the EU prohibition of State aid. In fact, by endorsing the right of new entrants by June 2016 and the abolition of such regimes by June 2021 without further investigation from a State aid perspective, the European Commission has tolerated a significant base-eroding tax advantage within the internal market. By giving up such investigation ex ante, the European Commission has in fact prevented their recovery for a 10-year period, had it otherwise regarded them incompatible with the rules prohibiting State aid. This has possibly given several EU Member States a significant tax advantage, in clear conflict with the object and purpose of the BEPS Project, as well as with the principles of the EU internal market.

The immediate object of De Haro's analysis in chapter 10 is the creation of mandatory disclosure rules. In this context, the author expresses concern over an exponential increase in legal uncertainty in connection with the unclear delineation of the boundaries of tax avoidance and aggressive tax planning in certain contexts, which deprives taxpayers of a global dimension in the protection of their fundamental rights. De Haro also addresses such issues in the light of some specific problems already arising in Mexico in connection with mandatory disclosure rules.

The third group of issues contained in Part One addresses some important features of the EU Anti-Tax Avoidance Package and the additional measures that characterize the European Union's reaction to BEPS.

Chapters 7 and 9 share common lines of inquiry with chapters 3, 6 and 8, and they complement those chapters with their analysis of issues connected to the prohibition of State aid and the coordination of tax policies within the European Union in the framework of the Anti-Tax Avoidance Package.

A thin conceptual line unites chapters 6, 7 and 9. Chapters 6 and 7 both address the implications arising in connection with how the prohibition of State aid is developing in tax matters. In this context, in chapter 7, Smit

reviews the decisions of the European Commission in respect of practices connected with transfer pricing and relief for double taxation that alter competition in the internal market. He shows some concern for the European Commission's approach to such issues, which he regards as inconsistent with the position taken by the Commission in 2009 in the investigation on the Dutch group interest box.

The action taken by the European Commission on State aid has an unprecedented size to affect tax matters. It has given rise to enormous legal uncertainty for business in the European Union, which will only be resolved once the Court of Justice decides on such cases in a few years. This action steers the exercise of taxing powers in a direction that secures a level playing field within the EU internal market, supplementing the failure of positive integration over several decades. Multinational enterprises are exposed to the obligation to repay illegal State aid 10 years back insofar as they may be held liable for having infringed competition rules. However, the exploitation, overexploitation or abusive exploitation of tax advantages across borders could have been avoided if EU Member States had committed to establishing a tax technical dialogue across borders instead of promoting unregulated tax competition within the internal market. After all, the blame is now put on multinational enterprises, but the responsibility of some Member States that have reassured such enterprises about compliance with their rules is hardly ever discussed.

The commitment of EU Member States to securing cross-border tax consistency in the framework of the rules established by the ATAD (comprehensively addressed in Part Two of this book) will help in making progress towards effective levels of positive integration of direct taxes rather than mainly relying on negative integration driven by rules on State aid or interpretation of the fundamental freedoms.

However, from a theoretical perspective, various critical points arise at the intersection between the interpretation of State aid rules by the European Commission and the standards that are commonly observed in practice by various countries in order to reflect a fair allocation of taxing rights between related enterprises. In the authors' view, in respect of the protection of competition within the internal market, the technical issues underlying such international standards, which have developed over decades and reflect the right of countries to apply different conditions in their bilateral relations within the framework put forward by the OECD, should be properly taken into account.

In search of coordination in EU tax policy, in chapter 9, Van Horzen and De Groot focus their attention on the switchover clause. This measure was first included in, and then removed from, the ATAD, but it still appears in the text of the proposed Common Corporate Tax Base (CCTB) Directive as a mechanism that secures the competitiveness of an EU business as opposed to business established outside of the internal market. The authors elaborate a constructive criticism of the use of this measure, prompting the European Commission to give a convincing motivation for including it in future secondary legislation on tax matters within the internal market or in relations with third countries.

In chapter 11, Avi-Yonah and Xu elaborate on the global value of the ATAD as a trendsetter in the implementation of the BEPS Project around the world. Among other things, they plead for the application of grandfathering rules and a transitional period for the implementation of BEPS measures for a duration that reflects that applicable to the ATAD within the European Union, i.e. until 1 January 2019.

1.3. Part Two: The ATAD

1.3.1. General remarks

Part Two of this book contains nine chapters that aim to provide more precise content regarding the initial questions posed by this introductory chapter.

Officially, the ATAD pursues the goal of streamlining the implementation of the BEPS Project in the European Union, avoiding differences across the national legislation of its Member States that could give rise to unintended tax biases within the internal market. Its intended consequence is therefore the production of secondary legislation in the European Union, subject to the interpretation of the Court of Justice of the European Union.

In some aspects, the content of the ATAD fails to fully implement the BEPS Project within the European Union; in other aspects, however, it goes beyond the BEPS Project, which may, in general, make one wonder whether it really achieves the goals that it officially pursues.

All three issues are subsequently briefly addressed with reference to the specific clauses of the ATAD and other measures contained in the EU Anti-Tax

Avoidance Package. (This book does not address BEPS Project measures that neither the ATAD nor the EU Anti-Tax Avoidance Package implement.)[1]

1.3.2. ATAD measures fully implementing BEPS Actions in the European Union

In its article 9, the ATAD fully implements BEPS Actions 2, 3 and 4. ATAD II has amended the ATAD in order to enhance the implementation of BEPS Action 4.

In chapter 18 of this book, Fibbe addresses the problems of hybrid mismatches in the ATAD and ATAD II, taking into account the problems of compatibility with primary law and criticizing a number of issues connected with conceptual and terminological vagueness. He also suggests that the elimination of hybrid mismatches should be achieved – at least within the internal market – on the basis of a uniform classification method that leads Member States to mutually recognize the tax classification in the host country.

Two additional chapters supplement the analysis of hybrid mismatches. In chapter 19, Pancham addresses the implications of permanent establishment mismatches under ATAD II, which give rise to various problems in terms of inconsistencies as to the application of the primary and defensive rules within the internal market and in relations with third countries. Furthermore, problems of legal uncertainty also arise in connection with ATAD II, mostly due to the absence of definitions in this directive. In the authors' opinion, the Court of Justice should address such problems at the level of interpretation, thus allowing ATAD II to achieve its ultimate goals in a framework of reasonable clarity for the business community.

In chapter 20, Peeters analyses the rule on imported mismatches in the framework of the ATAD and ATAD II. Among other things, he raises some criticism regarding the fact that the applicable provisions in the directives do not pay sufficient attention to the order for applying the rule and suggests an approach based on the comments included in the OECD Report, subject to a possible assessment of its consistency with the text of the directives and general EU law.

1. This is the case with BEPS Action 13, on transfer pricing documentation, implemented by EU Directive 2016/881/EU, and BEPS Action 14, on the cross-border settlement of tax disputes, on which the EU Council reached a political compromise on 23 May 2017 for the introduction of an EU directive.

In chapter 12, Schnitger makes a comparison between article 4 of the ATAD and the interest limitation rules of Action 4 of the BEPS Project, further taking into account the German equivalent rule (*Zinsschranke*), which could be seen as the other blueprint for this provision. Schnitger's analysis assesses the potential impact of article 4 of the ATAD and examines how it may interact with the other articles contained in the ATAD, suggesting the need to supplement this with additional targeted rules for identifying artificial structures.

1.3.3. Implementation of the BEPS Project through the ATAD and other EU Anti-Tax Avoidance Package measures

In some other cases, technical legal matters connected with the implications of issuing supranational EU law have prevented the implementation of some aspects of the BEPS Project via a directive, since this would otherwise automatically prevent Member States from regulating this field at the national level.

Accordingly, a non-binding instrument, Recommendation C(2016) 271 final, implements BEPS Action 6 within the European Union. It invites EU Member States to include a general anti-avoidance rule (GAAR) based on the PPT in their tax treaties. Yet the formulation of this clause more closely resembles the interpretation by the Court of Justice in order to reconcile the implementation of BEPS Action 6 within the general framework required by the EU legal system.

The ATAD and additional amendments to secondary legislation of the European Union, such as those to the Parent-Subsidiary Directive, strengthen the reaction of the European Union to cross-border abusive practices in a way that achieves an overall obligation for EU Member States to counter such practices in the field of direct taxes that are regulated by such directives.

Insofar as the goal pursued by the introduction of secondary EU law is to create a level playing field, one may wonder why and to what extent article 3 of the ATAD preserves the right of EU Member States to apply measures that safeguard a higher level of protection of the corporate tax base.

Directives generally bind their addressees to comply with their minimum content and do not prevent their over-implementation, as long as this does

not go against their object and purpose. In this context, the authors believe that Member States may go beyond the minimum level of protection established by the directive in a way that does not turn their rules into unjustified obstacles for the exercising of freedoms within the internal market. Accordingly, the connections between primary and secondary law at the level of interpretation – as well as the ancillary function that the latter performs in respect of the former – require a stricter GAAR to comply with the requirements established by the case law of the Court of Justice on the prohibition of abusive practices.[2]

By means of the GAAR contained in article 6, the ATAD partly covers BEPS Actions 6 and 7, implementing them in the legal system of the European Union.

The technical intricacies of the GAAR contained in article 6 of the ATAD are the object of chapters 14 and 15 of this book. In chapter 14, De Wilde addresses the interpretation, application and implications of article 6 of the ATAD from the perspective of the intra-firm legal structuring of multinational business operations. De Wilde reaches the conclusion that the wording of this provision in the context of the ATAD allows for an extensive interpretation that could stretch the limits of the international tax regime's operation to the point of collapse. Among other things, his analysis points out the uncertainty connected with expressions used in the provision, such as the reference to defeating the object and purpose of the applicable tax law and to the economic reality. In chapter 15, Perdelwitz reconstructs the possible meaning in the light of the interpretation of the limits established by case law of the Court of Justice on the prohibition of abusive practices, further taking into account the anti-avoidance provisions contained in other EU tax directives.

From a similar perspective, one may also question the different standards connected with article 7(2)(a) of the ATAD in respect of the application of controlled foreign company (CFC) legislation within the internal market and in relations with third countries. These are the issues Danon addresses in chapter 17. The conclusions reached in respect of the compatibility of such measures with primary law (including, in particular, the free movement of capital) are very persuasive. The authors believe that these conclusions should pave the way for the possible raising of preliminary questions that allow ascertaining the extent to which the ATAD CFC regime can reach

2. For more information on this, *see* ch. 15, addressing the issues connected with the interpretation of art. 6 ATAD.

harmonious application in line with the requirements established by primary law.

In chapter 16, Panayi describes the overall framework for the requirements of CFC legislation to apply in the European Union with a more detailed reference to the framework that originated the *Cadbury Schweppes* case. Taking this context into account, the authors feel that a significant difference should be recorded as to how the case-by-case approach required by EU law differs from the quasi-automatic approach applicable under Action 3 of the BEPS Project.

1.3.4. Other content of the ATAD

Some measures contained in the ATAD present only a more remote connection with the BEPS Project.

This is particularly the case of article 5, on exit taxes, which Vermeulen analyses in chapter 13 of this book with reference to developments in case law and the attempts by the European Commission to achieve consistent regulation in the taxation of capital gains in connection with the exercise of the fundamental freedoms across borders.

Although the object and purpose of this measure is more closely connected with the need to secure a consistent regulation of these matters affecting business within the European Union, Vermeulen also provides an interesting reconstruction of the existence of a possible link between article 5 of the ATAD and BEPS Action 6.

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