ETAF's feedback on the Implementing Directive for Pillar II

Introduction

On 22 December 2021, the EU became the first jurisdiction to start the legislative process for the transposition of the so-called Pillar II of the OECD agreement to reform the international tax system, i.e. the minimum 15% effective tax rate for large multinational enterprises (MNE).

Right after its publication, the European Tax Adviser Federation (ETAF) welcomed the proposal for an Implementing Directive, bringing the EU one step closer to fair taxation, and largely sees it as a genuine "tax revolution".

The proposed rules will apply to any large group, both domestic and international, which meets the annual threshold of more than €750 million of consolidated revenues in at least two of the four preceding years, and with either a parent company or a subsidiary situated in an EU Member State.

Only a grip of ETAF members will have to implement the new rules for their clients meeting the threshold. Indeed, 98% of our members typically represent SMEs. However, as ETAF represents the voice at EU level of 215 000 regulated tax advisers from France, Germany, Belgium, Romania, Hungary and Austria, it seemed crucial and relevant to present our general view on the proposal.

Taxation is a matter of perpetual evolution and tax advisers should be open and prepared to any future development, including a lowering of the threshold and the event of an application of the new rules to smaller companies.

This is all the more true as the OECD statement on a two-pillar solution to address the tax challenges arising from the digitalisation of the economy leaves the possibility to participant countries to apply the tax rules to MNEs headquartered in their country even if they do not meet the threshold. Recent media reports have shown that, during the negotiations, some Member States have indeed expressed their interest to keep this possibility open.

I. Uniform implementation at EU and OECD levels

ETAF members largely agree that a Directive is desirable to implement in a consistent and coordinated way the rules resulting from the OECD agreement within the EU. This is all the more welcomed if it ensures that 'gold plating' in Member States is avoided and can reduce uncertainties and administrative burden for companies.

The Directive follows the OECD model rules but expands the rules in the EU to domestic profits and to purely domestic companies that pass the threshold of €750 million turnover. According to the Commission, this addition is necessary to avoid any risk of legal controversy in the EU due to a difference in treatment between cross-border and domestic situations, which would be against the Freedom of establishment enshrined in EU Treaties.

As a large majority of MNEs operate cross-border, we do not expect any significant expansion of the number of MNEs falling under the scope of the Directive. Moreover, the intentions of EU Member States to opt to apply a qualified domestic top-up tax to low-taxed constituent entities located on their territory are not yet known.

While ETAF members generally believe that this departure from the OECD model rules is justified, they unanimously agree that, for the rest, the EU should strictly stick to the OECD model rules.

In that regard, we see with some concerns the last debate between the EU Finance Ministers on the Directive, which took place on 15 March 2022. We hope the worries expressed by some Member States during the discussion will not lead somehow to a renegotiation at EU level of what has already been negotiated and agreed at the OECD level.

We especially see with a sceptical eye the continued demand of Poland to add legal safeguards in the text to link the implementation of Pillar II to the implementation of Pillar I (reallocation of taxing rights) of the OECD agreement. From our point of view, it can be assumed that such an approach could only result in procrastination in effectively implementing Pillar II. We believe that the French proposal to annex a Council's statement to the text confirming the commitment of all Member States to the process under way within the Inclusive Framework concerning Pillar I and calling on the other States Parties to respect this commitment would be enough.

II. Ambitious but challenging timeline

The Commission decided to stick to the OECD timeline and to maintain the ambitious application date of 1 January 2023 while other jurisdictions like Switzerland already announced that they would apply the new rules only as of 1 January 2024.

This question is currently being debated in the Council of the EU. The latest compromise proposal tabled by the French Presidency delays the application of the new rules to 31 December 2023.

For ETAF, it is important that Europe keeps the leadership in this area. In that regard, we very much support France's ambition to make the minimum taxation in the EU a reality within its six-month presidency of the EU Council and to try to reach an agreement on a final text during the next Ecofin meeting on 5 April.

At the same time, we want to echo the fears we heard in some EU capitals about the timeline and recognize the complexity for tax authorities, tax advisers and for the companies they advise to implement the OECD tax deal in such a short period of time and as the fine-tuning of some rules at OECD level is still ongoing. For this reason, we believe that the one-year extension would be a reasonable compromise, while maintaining the political commitment to make Pillar II rules effective still in 2023.

Indeed, the OECD 'Commentary' on Pillar II has been published only recently and the work on the 'Implementation Framework', which has to be finalized before the end of 2022 and will address certain significant administrative and compliance issues, has just been launched.

Bearing in mind that every single change to the text will need to be adopted by the unanimity of Member States, we would strongly urge the EU Council and the European Commission to take into account the remaining work of the OECD on Pillar II before finalising the text of the Directive. Otherwise, we fear that this could lead to a lack of clarity, uncertainty and ultimately to a difference between the EU and the OECD rules.

From our point of view, the statements inserted in the text referring to the Commentary and the Implementation Framework as *"a source of illustration or interpretation"* are simply not enough. These detailed rules should be incorporated directly in the Directive and the choice to introduce these provisions into domestic legislation should not be left to the discretion of Member States.

Moreover, it is to be recalled that the OECD agreement on Pillar II only has the status of a ‘common approach’ which means that all the parties to the deal are not legally bound to adopt the new rules but, if they choose to do so, they will have to implement and administer the rules in a way that is consistent with what has been agreed internationally.

The success of the global minimum tax reform heavily relies on its worldwide implementation. Should some jurisdictions, like the United States, nevertheless decide against minimum taxation in the medium term, it must be ensured that the EU Member States are not stuck with a competitive disadvantage. In that regard, ETAF believes that a kind of sunset clause could be introduced in the text to ensure that if a significant number of our big international partners don’t comply with the deal, the Directive will automatically cease to apply.

Conclusion

For tax advisers' clients, legal certainty, clear regulations and the avoidance of double taxation are fundamental. Consequently, ETAF generally believes that the EU should implement the rules as closely as possible to the OECD model rules.

Turning to the future, if the threshold will be lowered and apply in an identical manner to smaller domestic entities, we expect the challenging need for a sufficient training offer for tax advisers and a significant increase of demand for consultation. We also expect a fast-learning process based on best practices to adapt with these new rules, as they will be already in force for MNEs.

ETAF members would also like to reiterate their attachment to finding a solution to tax the digital economy and consequently to Pillar I of the OECD agreement. The pressing need to modify the international tax system in this area remains valid and we look forward to the finalisation of the Multilateral Convention in the course of 2022.

In this regard, we welcome the approach taken by the OECD to proceed with public consultation in stages on several building blocks, to obtain feedback quickly and before the work is finalised. However, we regret the short deadline of only two weeks to send a comment on the draft rules for Nexus and revenue sourcing as well as for tax base determinations under Amount A.

ETAF will continue to follow closely the evolution of Pillar I and Pillar II both at OECD and EU level as well as continue to constructively engage in the discussions.