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MEETING DOCUMENT

From:	Presidency
To:	Working Party on Tax Questions (Direct Taxation – CCTB)
Subject:	Proposal for a Council Directive on a Common Corporate Tax Base - Second draft Presidency compromise on Articles 9, 11 and 42

Delegations will find attached a document from the Presidency in view of the meeting of the Working Party on Tax Questions (Direct Taxation - CCTB) on 30 May 2017.

Delegations will find in Annex a second draft Presidency compromise on Articles 9, 11 and 42 of the Proposal for a Council Directive on a Common Corporate Tax Base (doc. 13730/16)

New text (compared to documents WK 4528/17, 4623/17 and 4529/17) is marked **<u>bold and underlined</u>**, deletions are marked with ~~strikethrough~~.

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ANNEX

Article 9

Deductible expenses

1. Expenses shall be deductible only to the extent that they are incurred in the direct business interest of the taxpayer.
2. The expenses referred to in paragraph 1 shall include all costs of sales and all expenses, net of deductible value added tax, that the taxpayer incurred with a view to obtaining or securing income, including costs for research and development and costs incurred in raising equity or debt for the purposes of the business.
3. In addition to the amounts which are deductible as costs for research and development in accordance with paragraph 2 and~~ to the extent that the taxpayer is not entitled to a tax credit on these research and development costs,~~ **provided that the taxpayer does not avail itself, directly or indirectly, of any benefit in whatever form granted by any Member State in its national legislation, in relation to such research and development costs**, the taxpayer may also deduct, per tax year, an extra 50% of such costs with the exception of the costs **related to the assets** referred to in points (c), (d),and (e) of Article 33 (1) and (c), (d) and (e) of Article 33 (2) that it incurred during that year.

Presidency comments:

- *The presidency attempted to respond to the concerns of the Member States who requested alternative forms of assistance in respect of R&D. e.g. grants, tax credits, patent boxes. However, following the last meeting, it is clear that there is difficulty in reconciling between the super deduction and other forms of assistance.*
- *In the last meeting, the Commission has stated that Member States are free to apply any measures post-tax base, as this goes beyond the scope of the Directive. The Presidency is aware that this might still create issues for harmonisation.*
- *The Presidency is of the opinion that the original text as proposed by the Commission can limit the scope of harmonisation while possibly allowing for circumvention of the Directive through post-tax base measures. The text as proposed above attempts to*

provide a basic framework for disallowing double benefits with respect to the same R&D costs.

To the extent that costs for research and development reach beyond EUR 20 000 000, the taxpayer may deduct 25% of the exceeding amount.

By way of derogation from the first subparagraph, the taxpayer may deduct an extra [100%] of its costs for research and development up to EUR 20 000 000 where that taxpayer meets all of the following conditions:

(a) it is an unlisted enterprise with fewer than 50 employees and an annual turnover and/or annual balance sheet total that does not exceed EUR 10 000 000;

(b) it has not been registered for longer than five years. If the taxpayer is not subject to registration, the period of five years may be taken to start at the moment that the enterprise either starts, or is liable to tax for, its economic activity;

(c) it has not been formed through a merger or any other form of business reorganisation;

(d) it does not have any associated enterprises as referred to in Article 56**;**

(e) it does not avail itself, directly or indirectly, of any benefit in whatever form granted by any Member State in its national legislation, in relation to such research and development costs.

Presidency comment:

- *Sub-paragraph e) was added to restrict start-up companies from taking a double benefit in respect of their research and development costs as proposed in paragraph 3 above.*

4. Member States may provide for the deduction of gifts and donations to charitable bodies.

Article 11

Allowance for growth and investment ('AGI')

1. For the purposes of this Article, 'AGI equity base' means, in a given tax year, the difference between the book value of the equity of a taxpayer and that of its participation in the capital of associated enterprises as referred to in Article 56.

2. For the purposes of this Article, 'equity' **shall** mean**:** ~~s any of the following~~:

~~(a) 'capital and reserves', as described in letter A., under 'Capital, reserves and liabilities' in Annex III to Directive 2013/34/EU of the European Parliament and of the Council~~[1]

~~(b) 'capital and reserves', as described in letter L. in Annex IV to Directive 2013/34/EU~~

~~(c) 'equity', as defined in the International Financial Reporting Standards which are adopted and used in the Union pursuant to Regulation (EC) No 1606/2002 of the European Parliament and of the Council~~[2]~~.~~

(a) ~~[~~Where the taxpayer is a company, **the total of:** ~~the share capital of the taxpayer, any share premium, positive retained earnings, loans or other debt borrowed by the taxpayer which do not bear interest, and any other reserves resulting from a contribution to the taxpayer, and~~

(i) Subscribed capital;

(ii) Share premium account;

(iii) Revaluation reserve;

~~1 Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013, p. 19).~~

~~2 Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards (OJ L 243, 11.9.2002, p. 1).~~

(iv) **Reserves:**

- **Legal reserve;**
- **Reserve for own shares;**
- **Reserves provided for by the articles of association;**
- **Other reserves, including the fair value reserve;**

(v) **Accounting Profit or loss brought forward; and**

(vi) **Accounting Profit or loss for the financial year;**

(b) Where the taxpayer is a permanent establishment, the term shall mean the ~~capital~~ **equity** of that taxpayer which is attributable to the permanent establishment;~~]~~

Presidency comment: • *Following discussions in previous meetings, it was noted that delegates prefer a self-standing definition within the directive itself. To this effect, the Presidency has included a definition of 'equity' which is based on that provided in Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings[3], to ensure harmonisation in use of such term, while still making use of an already accepted definition within EU law.*

3. An amount equal to the defined yield on the AGI equity base increases shall be deductible from the taxable base of a taxpayer according to paragraphs 1 to 6. If there is an AGI equity base decrease, an amount equal to the defined yield on the AGI equity base decrease shall become taxable.~~provided that where the AGI equity base decrease is due to a loss, the AGI equity base shall be determined without regard to such loss. The latter provision shall apply mutatis mutandis in respect of losses brought forward from previous tax years. In this context, decreases in the AGI equity base due to losses shall be computed according to the rules provided for in this directive.~~

4. **(a)** AGI equity base increases or decreases shall be calculated, for the first [ten] tax years that a taxpayer is subject to the rules of this Directive, as the difference

[3] http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32013L0034

between its AGI equity base at the end of the relevant tax year and its AGI equity base on the first day of the first tax year under the rules of this Directive.

(b) **By derogation from the first subparagraph of paragraph 4, where the calculation of the AGI equity base results in an AGI equity base decrease, the movement in the AGI equity base shall be recalculated without regard to accounting losses incurred by the taxpayer from the first tax year under the rules of this Directive. Where such recalculation results in an AGI equity base increase, such increase shall be disregarded.**

(c) After the first ten tax years, the reference to the amount of AGI equity base that shall be deductible against the AGI equity base at the end of the relevant tax year shall annually be moved forward by one tax year.

Presidency comment:

- *Unlike the suggestion put forward in a previous draft, the Presidency is suggesting utilising "accounting loss" (as opposed to a "(tax) loss" under the Directive).*
- *The taxability of the defined yield resulting from equity base decreases, was considered as pro-cyclical by a number of delegations. One option which the Presidency invites the group to consider in this context is that of "freezing" the AGI equity base when the reduction in the equity value for that year emanates purely from an accounting loss, rather than other decreases in equity such as a dividend distribution. Such an approach would limit the generation of negative defined yields (i.e. taxable income) to loss reductions in the equity base, mitigating the pro-cyclical nature of the mechanism. Thus, in situations where the reduction in the AGI equity base is attributable to dividend distributions/other reductions in equity which in total, are in excess of the accounting profits earned from the first day of the first tax year under these rules, the negative defined yield would apply. The company would then be subject to taxation on the difference between the accounting profits earned and the reduction in equity which is not attributable to accounting losses. The following is an example of how this would work:*

01.01.2019

A standalone company with no participations in any subsidiaries joins the common tax base

31.12.2018

AGI equity base: 100,000

31.12.2019

Accounting profit: 20,000

<u>AGI equity base: 120,000 </u>(=100,000+20,000)

Increase in the AGI equity base: 20,000 (=120,000-100,000)

<u>The **'defined yield' for deduction** to be applied to 20,000</u>

31.12.2020

Accounting loss: 30,000

<u>AGI equity base: 90,000</u> (= 120,000-30,000)

Decrease in the AGI equity base: 10,000

<u>The **'defined yield' for taxation** cannot be applied (90,000+30,000)*</u>

***(In accordance with par 4(b) the accounting loss of 30,000 should be disregarded. The add back of accounting loss gives an increase in the AGI equity base which should be disregarded ending in a neutral position (no increases/decreases)

31.12.2021

Accounting profit: 15,000

<u>AGI equity base: 105,000</u> (= 90,000+15,000)

Increase in the AGI equity base: 5,000 (= 105,000-100,000)

<u>The **'defined yield' for deduction** to be applied to 5,000</u>

31.12.2022

Accounting profit: 20,000

Dividend distribution: 15,000

<u>AGI equity base: 110,000</u> (=105,000+20,000-15,000)

Increase in the AGI equity base: 10,000 (=110,000-100,000)

<u>The **'defined yield' for deduction** to be applied to 10,000</u>

31.12.2023

Accounting loss: 10,000

Dividend distribution: 5,000

AGI equity base: 95,000 (=110,000-10,000-5,000)

Decrease in the AGI equity base: 5,000

The '**defined yield' for taxation** cannot be applied (95,000+30,000+10,000)*

*(In accordance with par 4(b) the accounting losses of 30,000 and 10,000 should be disregarded. The add back of accounting losses gives an increase in the AGI equity base which should be disregarded ending in a neutral position (no increases/decreases).

31.12.2024

Accounting profit: 5,000

Dividend distribution: 45,000

AGI equity base: 55,000 (=95,000+5,000-45,000)

Decrease in the AGI equity base: 5,000 (=100,000-55,000+30,000+10,000) *

The '**defined yield' for taxation** to be applied to 5,000

*(In accordance with par 4(b) the accounting losses of 30,000 and 10,000 should be disregarded. However, the company still ends with a reduction in the AGI equity base which should be taxed)

In the example above, the 5000 'defined yield' for taxation is equal to the difference between accounting profits earned totalling 60,000 (20,000 + 15,000 + 20,000 + 5,000) less dividend distributions totalling 65,000 (15,000 + 5,000 + 45,000). The total accounting losses amounting to 40,000 (30,000 + 10,000) are thus disregarded.

5. The defined yield referred to in paragraph 3 shall be equal to the yield of the euro area 10-year government benchmark bond in December of the year preceding the relevant tax year, as published by the European Central Bank, increased by a risk premium of two percentage points. A floor of two per cent shall apply where the curve of the annual yield is negative.

6. By derogation to paragraphs 1 to 5, the following shall be excluded from the AGI equity base where the arrangement or a series of arrangements have been put in place for the essential purpose of obtaining a tax advantage under this Article:

   (c) intra-group loans and loans involving associated enterprises, as referred to in Article 56;

   (d) intra-group cash contributions and contributions in kind;

(e) intra-group transfers of assets and participations;

(f) the re-categorisation of old capital as new capital through liquidations and the creation of start-ups;

(g) the creation of subsidiaries;

(h) acquisitions of businesses, in full or part, held by associated enterprises;

(i) double-dipping structures combining interest deductibility and deductions under the AGI;

(j) increases in the amount of loan financing receivables towards associated enterprises as compared to the amount of such receivables at the reference date.

Presidency comment:

- *The Presidency acknowledges that if the detailed anti-abuse rules are to be provided within the Directive itself, much more work at a technical level would be needed. Written contributions by delegations would in this respect be most welcome.*
- *At the same time, the CCTB being a directive, it could remain at the level of principles and leave implementation details to MS in the transposition phase.*
- *Some delegations requested a more automatic rule with a reversed burden of proof, but the Presidency considers that consistency is needed with Article 58 (GAAR).*

Article 42

Loss relief and recapture

1. A resident taxpayer that is still profitable after having deducted its own losses pursuant to Article 41 may additionally deduct losses incurred, in the same tax year, by its immediate qualifying subsidiaries, as referred to in Article 3(1), or by permanent establishment(s) situated in other Member States. This loss relief shall be given for a limited period of time in accordance with paragraphs 3 and 4 of this Article.

By derogation from the first subparagraph, where a taxpayer is ~~permitted~~ **allowed** or required to act on behalf of a group as defined in the rules of ~~a~~ the national ~~group taxation system,~~ **legislation of a Member State, and where the companies forming part of such group are companies which are resident in such Member State and to which the rules of this directive apply, such** ~~the entire~~ group ~~shall~~ **may** be treated as ~~a resident taxpayer~~ **an immediate qualifying subsidiary**.

Presidency comments:

- *During the last meeting, the CLS confirmed that there is nothing in the proposal which prohibits taxpayers from continuing to apply their national group taxation systems with respect to definite surrender of losses since this article deals only with temporary loss relief. However, for this to work, it would be necessary that all companies/members of a group calculate their tax base in accordance with CCTB rules. It is also being clarified that the treatment of losses under national group taxation rules shall take precedence over the EU temporary loss relief mechanism. This means that where the group is to be treated as a single taxpayer, the aggregate loss resulting from the application of group loss relief provisions under domestic legislation can be considered as having been incurred by the immediate qualifying subsidiary, allowing for offset of losses against profits at the level of the parent company. Reference here is being made to the working document issued by the Commission dated 8th March 2017 [WK 2563/2017 REV 1] and to the example under 'Interaction with National Group Taxation Systems'.*

- *The reference to 'a taxpayer' in the second subparagraph above does not refer to a 'resident taxpayer' in the first subparagraph, but is a reference to any company within a Member State which is allowed to act on behalf of a national group.*

2. **A deduction for losses in accordance with this article shall only be available to the extent that such losses have not been deducted, temporarily or otherwise, under the national legislation of any Member State.**

Presidency comments:

- *This provision was added as an anti-abuse measure to prevent companies which form part of a group from utilising the same losses more than once.*

~~2~~**3.** The deduction shall be in proportion to the holding of the resident taxpayer in its immediate qualifying subsidiaries as referred to in Article 3(1) and full for permanent establishments. In no case shall the reduction of the tax base of the resident taxpayer result in a negative amount.

~~3~~**4.** The resident taxpayer shall add back to its tax base, up to the amount previously deducted as a loss, any subsequent profits made by its immediate qualifying subsidiaries as referred to in Article 3(1) or by its permanent establishments.

~~4~~**5**. Losses deducted pursuant to paragraphs 1**,** ~~and~~ 2 **and 3** shall automatically be recaptured into the tax base of the resident taxpayer in any of the following circumstances:

(a) where, at the end of the fifth tax year after the losses became deductible, no profit has been recaptured or the recaptured profits do not correspond to the full amount of losses deducted;

(b) where the immediate qualifying subsidiary as referred to in Article 3(1) is sold, wound up, merged or transformed into a permanent establishment;

(c) where the permanent establishment is sold, wound up or transformed into a subsidiary;

(d) where the parent company no longer fulfils the requirements of Article 3(1).