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EU directive proposal laying down rules on Business in Europe: Framework for Income Taxation (BEFIT)

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UEL response to the EU public consultation

The EU Commission released in September 2023 a directive proposal (hereafter the "Directive proposal") on the introduction of a common legal framework to harmonize the fundamental features of corporate income tax systems with a view to simplifying tax rules and ensuring a fair competition between EU Member States (hereafter the "MS") (hereafter the "BEFIT initiative"). The BEFIT initiative is presented as aiming at reducing compliance costs and creating a level playing field by introducing a common framework for corporate income taxation in the EU. The EU Commission has opened a public consultation on the Directive proposal.

Besides, the European Council called for the general regulatory environment to be simplified and for the administrative burden to be reduced[1]. In addition, the Committee on Economic and Monetary Affairs of the EU Parliament recently stated in its draft report on further reform of corporate taxation rules that "simplifying the complexity of the legal framework for corporate tax systems helps to attract foreign direct investment and reduces the risk of companies relocating to non-EU countries"[2].

UEL, and the Luxembourg business sectors it represents, generally support any initiative brought forward by the EU Commission to provide a fair and sustainable business environment, by:

- Reducing the tax compliance administrative burden and the tax compliance costs;
- Simplifying the operations across the Single Market for businesses; and
- Facilitating cross-border activity for EU resident companies.

However, and as outlined in the below developments, we fear that the BEFIT initiative is quite unlikely to reach its goals of simplifying the tax environment and reducing compliance costs within the EU and may even trigger negative consequences for certain MS (incl. increased compliance costs for both taxpayers and tax authorities alike).

We therefore believe that the contents of the Directive proposal should be reworked to ensure that it is an effective tool to reduce compliance costs for EU businesses, putting all MS on an equal footing and ensuring the competitiveness of the EU internationally.

[1] https://data.consilium.europa.eu/doc/document/ST-4-2023-INIT/en/pdf
[2] https://www.europarl.europa.eu/doceo/document/ECON-PR-736738_EN.pdf

UEL is committed to engage in a constructive dialogue with the EU Commission and MS to ensure that the BEFIT initiative achieves its goals and contributes to the increased efficiency and competitiveness of the Single Market.

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Detailed comments

We appreciate the opportunity to provide input on behalf of UEL on the Directive proposal and we are pleased to provide the following comments:

Need to reinstate a more competitive Europe

- The EU Commission and the MS have taken a considerable step in harmonizing tax matters within the EU in the recent years, which notably resulted in the integration of BEPS measures into the EU tax landscape (e.g. ATAD 1, ATAD 2….). However, these initiatives also led to an increased complexity of the tax framework, which will be drastically reinforced with the upcoming EU initiatives recently launched in the tax field (including the directive on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union ('Pillar 2' directive));
- This increased complexity triggers not only legal uncertainty for taxpayers, but also higher compliance costs, thus negatively impacting the competitiveness of EU businesses in global markets. These increased costs should be understood broadly beyond simple tax compliance costs, but also including administrative, IT, staff costs implied to produce and manage the accounting and tax data, as well as the documentation required to comply with these new obligations (and not considering the growing regulatory compliance obligations within the EU, notably linked to non-financial reporting);
- We therefore welcome the fact that the EU Commission recently recognized "the importance of a growth-enhancing regulatory framework for supporting competitiveness and productivity of EU businesses"[3]. The EU Commission thus committed to simplify reporting requirements for companies and administrations with the aim of reducing such burdens by 25%;
- In this context, we generally support the goal of the BEFIT initiative in so far as it aims at reducing compliance costs for EU businesses;
- However, we fear that the BEFIT initiative is unlikely to reach its goals of simplifying the tax environment and reducing compliance costs for the reasons outlined below;
- Furthermore, we believe that a more comprehensive and ambitious agenda for simplifying the tax landscape should be introduced by the EU Commission to provide an effective solution to the problem of increased administrative burden of companies, while safeguarding the competitivity of the EU;
- We therefore support the recent conclusions of the Committee on Economic and Monetary Affairs of the European Parliament regarding the need to reduce the compliance burden for EU companies and according to which it "calls on the Commission to present an overall evaluation of

[3] https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13990-Charges-administratives-Rationalisation-des-obligations-dinformation_fr

actions taken on corporate taxation since 2011 and to immediately ease the burden on businesses by invoking a regulatory moratorium and delaying those tax acts that would unnecessarily increase costs for businesses already under strain; calls on the Commission to carry out competitiveness checks for new legislative tax proposals, as requested by the European Council for all new proposals on 22 March 2023"[4];

- Finally, and given that some of the adjustments foreseen by the Directive proposal appear to be stricter than those existing in domestic tax regimes (e.g. denial of provisions for unrealized foreign currency exchange losses, depreciation of buildings over 28 years), the question may be raised if this may not discourage EU businesses to engage in cross-border investments.

Possible reduced benefit in terms of lowering administrative burden and compliance costs

- We understand that the BEFIT initiative aims at achieving administrative simplification by introducing (i) a new single set of rules to determine the EU tax base of multinational groups (operating therein) and (ii) a one-stop-shop mechanism that will allow one group member to fill in the group's information returns with the tax administration of one MS. According to the EU Commission, the new BEFIT rules could reduce EU businesses' current tax compliance costs by up to 65%;
- We welcome these measures in so far as they aim at helping to reduce the administrative burden for taxpayers and administrations alike;
- However, we fear that the expected reduction of compliance costs could be possibly limited, or even inexistent for some taxpayers, whereas the new BEFIT rules would trigger even higher administrative costs in practice, since:
    - For taxpayers falling within the scope of the Pillar 2 rules, two parallel tax systems would need to co-exist as the new rules are not fully aligned with the Pillar 2 rules (but only close to them – see further details below). These taxpayers will therefore have to incur costs in order to implement continuous training, possibly hire additional human resources, adapt to and/or develop new local IT tools for the two parallel tax systems to function properly;
    - Therefore, we believe that the calculation of the taxable basis under BEFIT rules should be aligned to the Pillar 2 model rules to leverage on tax data collection and management work already undertaken to apply the provisions of the Pillar 2 directive and related OECD model rules. This would strengthen the coherence of the taxable basis calculation and leverage on the processes implemented by concerned businesses across the EU. If not lowering complexity and compliance costs, this would at least not add further complexity to the system and would not add compliance costs;
    - This BEFIT initiative will also likely significantly increase the administrative burden for tax authorities which will have to deal with 3 parallel tax systems (i.e., Pillar 2 rules, BEFIT rules and local tax rules). This will require additional human and technical resources for tax authorities, and we fear that not all MS may have the immediate capacity to respond to this need for additional resources;

[4] See note 2

  - Despite the one-stop-shop for the BEFIT information return, the combination of entity-based calculations, the aggregation of profits and losses of all the BEFIT group members into a single group tax base, the subsequent allocation of this group tax base between MS, and the potential additional local adjustments de facto rule out the very principle of simplification which underpins this BEFIT initiative;
  - Besides, each BEFIT group member will still have to file an individual tax return to their local tax administration and would still be required to meet Pillar 2 compliance obligations if they fall within scope of the Pillar 2 rules;
  - Furthermore, tax controversy may increase since BEFIT group members are exposed to questioning and challenging with respect to the BEFIT information tax return and their individual tax return. The BEFIT team is supposed to achieve consensus on the content of the BEFIT information return, while the competent authority of a MS shall issue an individual tax assessment as regards the individual tax return. Tax audits and dispute settlement in turn can only be initiated at the level of each MS, but the MS can request a joint audit. Given the numerous parties involved in the process, one can wonder if these features will allow reaching the stated objective of achieving administrative simplification, or if, on the contrary, they are likely to increase the administrative burden, tax controversy and uncertainty as regards the tax positions of the BEFIT group members.

- Besides, ultimate parent entities (hereafter "UPEs"), or filing entities if the UPE is not located within the EU, will have to file the BEFIT information return pertaining to the entire group within 4 months following the closing of the relevant financial year. This appears highly ambitious since all companies that are members of the same group will first have to calculate their own tax base in accordance with the new set of rules, before the BEFIT information return can be prepared and filed. One should bear in mind that, in practice, many jurisdictions already allow a significantly longer period to prepare and approve financial statements which serve as the basis for the tax returns based on domestic rules, and to file said tax returns. And, by design, larger cross-border groups will need an even longer period to achieve all aggregation and compliance work as opposed to smaller groups with little or no cross-border activities. Furthermore, this timing is not in line with the one foreseen in the Pillar 2 rules, which may thus trigger additional difficulties and compliance costs for taxpayers;
- In addition, we fear that the administrative burden inherent to the application of the BEFIT rules may hinder the effective access to this proposal for SMEs (irrespective of the fact that its application is left optional for these taxpayers);
- Considering the above, we struggle to see how these elements will be reconciled for the purpose of the BEFIT initiative, and thus wonder whether the desired outcome of reducing compliance costs by 65%, as announced by the EU Commission, is at all realistic or accurately set. We therefore believe that the EU Commission should present an updated evaluation of the impact of the BEFIT proposal on the reduction of compliance costs for taxpayers before any further discussion on that file at EU level to help MS achieve an informed opinion;
- In this respect, we note that the EU Commission has acknowledged that "The costs of the proposal cannot be determined with any precision because the BEFIT proposal does not have a precedent

and there is no dedicated data that can be used reliably for concrete estimates"[5]. We believe that the implementation, running costs and administrative burdens deriving from the application of the Pillar 2 rules by taxpayers (and tax authorities) could provide a reliable comparable to better estimate the costs expected from the implementation of the BEFIT rules. In any case, it will be key that a more accurate assessment is performed by the EU Commission once the implementation phase of the Pillar 2 rules has elapsed and before working further on the design of the BEFIT initiative;

- In addition, it should be contemplated to introduce an initial trial period to apply the BEFIT rules on a temporary and optional basis. This trial period could be aligned with the 5 years period foreseen by the Directive (art.77) to allow the EU Commission to "examine and evaluate (the BEFIT rules') functioning and report to the European Parliament and the Council", after which "a proposal to amend this Directive" could be submitted. This would ensure that the full consequences of such a proposal on the effective reduction of compliance costs and administrative burden for businesses are assessed. In this respect, we therefore support the recent conclusions from the European Parliament regarding the need to reduce the compliance burden for EU companies and according to which it "highlights the idea of a one-stop-shop allowing for the filing of one consolidated tax return; calls on the Commission to introduce a one-stop-shop for the application of the BEFIT rules in a test phase and to incorporate it as a permanent feature of BEFIT if the test phase is successful"[6]. Having this initial trial period would also allow to identify possible divergences in the interpretation of the BEFIT rules between the various MS and thus to improve the rules before they become permanent so as to allow a more coherent and uniform interpretation within the EU;
- Finally, optionality in the application of the BEFIT rules could generally be contemplated for all companies (and not only for SMEs), to ensure that taxpayers will not unduly bear an additional administrative burden resulting from the application of this initiative and may decide to opt for this regime after having performed a cost/benefit analysis at their level.

Possible adverse consequences deriving from the interaction of the BEFIT initiative with Pillar 2 rules

- As mentioned above, we understand that the BEFIT initiative is only partly aligned with the Pillar 2 rules (notably in respect to the group scope and especially further to the publication of a package of Pillar 2 safe harbor rules, likely to be implemented by the various MS). In addition to the increased complexity that this may create for in-scope taxpayers, we fear that the interaction between the two sets of rules might create double taxation in situations where the taxable BEFIT result would be subject to a top-up tax as a result of the BEFIT profit/loss allocation, and / or an additional tax burden for taxpayers;
- Indeed, the BEFIT mechanism applies on a compensation of profits and losses within the EU across the BEFIT group followed by an allocation entity per entity (i.e., BEFIT group member), whereas Pillar 2 rules apply on a jurisdictional basis. This major difference could lead to a significant risk of under-taxation under Pillar 2, resulting in the levying of a top-up tax. Similarly, the proposal does not foresee how the allocation of taxable basis to the BEFIT group entities interacts with the Pillar

[5] See the Explanatory Memorandum, page 10
[6] See note 2

2 rules and the requirement for a jurisdictional effective tax rate of 15%, noting that local adjustments are also possible;

- Interactions with Pillar 2 effective tax rate calculations should be anticipated by the Directive proposal to ensure that BEFIT would remain neutral and compatible with the global minimum tax. In particular, BEFIT should not trigger any additional impact of the income inclusion rule or the under taxed payment rule (UTPR) as a result of the (re)allocation of the taxable base across EU MS;
- Besides, the EU Parliament has recently stated that "companies are focusing their financial and human resources on applying the Pillar 2 rules; calls on the Commission to give companies breathing space and enough time to prepare for the possible new BEFIT rules"[7];
- We therefore believe that the rules should be further amended to be fully aligned with the Pillar 2 rules. If this is not the case, we believe that the EU Commission should work towards reaching an agreement at OECD level to ensure the complementarity of the two initiatives and the acceptability of the BEFIT initiative at international level[8].

Need to further enhance the framework for eligible tax incentives

- The explanatory memorandum of the BEFIT initiative states that "Member States will be free to further apply any (…) tax incentives (…) without restrictions. The only requirement that Member States will need to respect in this regard, are the rules of the Pillar 2 Directive (…)". However, as they stand, and as recently recalled by the European Parliament[9], the Pillar 2 rules considerably limit the number (and nature) of tax incentives that may be granted by jurisdictions without negatively impacting the effective tax rate of in-scope taxpayers. Tax incentives which are not Pillar 2 compliant might trigger the application of a top-up-tax (domestic or not), also risking this tax revenue to be recaptured elsewhere;
- However, tax incentives are a crucial tool for jurisdictions to support economic growth and long-term investments within the EU, especially in the context of the EU's objectives pertaining to supporting digital and green transition, as well as innovation[10]. As such, the EU Parliament has recently reiterated that it "takes note of the renewed debate on tax incentives following the US Inflation Reduction Act; calls on the Commission to allow for experimentation with tax credits; insists, nevertheless, that all decisions should be taken in a coordinated manner to preserve the functioning of the single market"[11];
- Consequently, we believe that the EU Commission should undertake discussions at OECD level to agree on a further amendment of the OECD Pillar 2 rules on what constitutes a qualifying tax incentive (at least in the area of the digital and environmental transitions) before finalizing the BEFIT rules.

[7] See note 2
[8] We also note that future interactions between BEFIT and the upcoming OECD Pillar 1 are not foreseen yet but will need to be considered once the latter would be adopted.
[9] https://www.europarl.europa.eu/RegData/etudes/ATAG/2023/749793/EPRS_ATA(2023)749793_EN.pdf
[10] https://ec.europa.eu/commission/presscorner/detail/en/qanda_23_511
[11] See note 2

Need to clarify the allocation of profits after the transition period

- The Directive proposal foresees that, once computed and aggregated, the BEFIT tax base should be allocated to BEFIT group members in their respective MS based on applying a baseline allocation percentage, computed on the average of the taxable results in the 3 previous years. This mechanism should be applicable during the transition period only (i.e., between 1 July 2028 and 30 June 2035);
- After the transition period, the Directive proposal indicates that the allocation could be carried out via a formulary apportionment, the design of which would be achieved following a "comprehensive review of the transition rule" and based on a relevant study, to be submitted to the Council by 2031. In other words, the BEFIT initiative, in its current state, does not provide a definitive proposal as to how the BEFIT tax base would be allocated after the transition period;
- Given that this allocation is key in the design of the Directive proposal, and would effectively impact MS' tax revenues, the absence of clarity in this respect creates uncertainties regarding the tax revenue that MS would generate from the allocated corporate income tax. This significant legal uncertainty is detrimental to MS achieving an informed decision on this initiative. On the longer run, this uncertainty might create some difficulties for MS when elaborating a long-term budgetary roadmap;
- Any allocation key would thus have to be accompanied with a proper impact assessment on MS's tax revenues before MS can decide whether or not such allocation key is appropriate. The opposite approach would significantly call into question the fundamental principal that direct taxes remain a competency of each individual MS;
- Therefore, MS should refrain from agreeing on the current proposal without having the definitive allocation key (applicable after the transition period) included in the proposal, together with a real impact assessment.

Need to introduce a mechanism to increase legal certainty

- The Directive proposal foresees that, for each BEFIT group, there will be a so-called 'BEFIT Team' which will bring together representatives of each relevant tax administration from the MS where the group operates. The members of each BEFIT Team will be sharing information, coordinating, providing a degree of early certainty on specific topics and resolving issues through an online collaborative tool;
- We welcome the stated objective of having a common administrative framework and a common assessment made by the BEFIT Team to allow businesses to obtain a degree of early certainty on certain items and to help reduce the number of tax disputes;
- However, given the high complexity of the Directive proposal and the expected disputes between the various BEFIT Teams which may arise from its implementation, we believe that these features should be complemented by the introduction of a "cooperative compliance program" embedded into the BEFIT initiative (e.g., into the role and responsibilities of the BEFIT Team);
- Such program could, for example, be based on the ETACA pilot project run at EU level. This would be consistent with the willingness of the EU Commission to implement such a program on a

permanent basis[12]. In a BEFIT context, this program should aim at creating a framework for a preventive dialogue between tax administrations and businesses regarding the application of the BEFIT rules. It would thus bring a higher level of legal certainty for taxpayers and would thus contribute to reduce the overall administrative burden. It should however be ensured that MS would allocate sufficient human resources to this program, as well as to the national BEFIT Team, to ensure their efficiency and success in practice;

- In addition, BEFIT rules should be accompanied with efficient dispute resolution mechanisms to protect taxpayers' rights and limit risks of double taxation. In particular, the management of secondary adjustments with non-EU countries should be addressed from a procedure standpoint, as well as responsible tax authorities and timing perspectives, to avoid lengthy processes with uncertain outcome.

Conclusion

We welcome the willingness of the EU Commission to reduce the administrative burden and compliance cost for EU businesses as this is an important factor for supporting their competitiveness and productivity. However, we fear that the BEFIT initiative is unlikely to reach its goals of simplifying the tax environment and reducing compliance costs within the EU.

Furthermore, the current design of the BEFIT proposal fails to provide clarity on key aspects of the contemplated rules (in particular on the future allocation key), which prevents MS from achieving an informed decision on this initiative.

We therefore believe that:

- The content of the Directive proposal should be reworked to ensure that it is an effective and efficient tool to reduce compliance costs for EU businesses, putting all MS on an equal footing and ensuring the competitiveness of the EU. One key feature of the proposal should be its full alignment with the Pillar 2 rules;
- In addition, the EU Commission should address with the OECD the necessity to broaden the scope of eligible of tax incentives for Pillar 2 purposes (especially in the area of the digital and green transitions), before finalizing the BEFIT rules;
- Besides, and due to its overall complexity, it will be key to ensure that the design of the BEFIT initiative ensures a higher level of legal certainty for taxpayers, by introducing a "cooperative compliance program" in the context of the BEFIT rules and efficient dispute resolution mechanisms;
- Finally, the EU Commission should present an updated evaluation of the impact of the BEFIT proposal on the reduction of compliance costs for taxpayers before any further discussion on that file occur at EU level. Such evaluation also needs to consider the final allocation key (which is missing from the current BEFIT proposal).

[12] See p.6 of the Directive proposal on transfer pricing : https://taxation-customs.ec.europa.eu/system/files/2023-09/COM_2023_529_1_EN_ACT_part1_v7.pdf

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***About UEL**:*

UEL (Union des Entreprises Luxembourgeoises) is the Luxembourg Employers' Association. UEL represents the Luxembourg private-sector businesses, except for the primary sector, and includes the Grand Duchy's professional chambers and employer federations.

UEL works for a sustainable and prosperous economy for Luxembourg, its inhabitants and those who work there. It endeavors to provide an economy that is attractive to both investors and talented individuals.

To accomplish its mission, UEL facilitates working groups and discussions with its member organizations on major inter-branch topics. It is thereby able to present joint positions to the public authorities and social partners on these topics which they can then review together.

The initiatives launched by UEL are based on the values of the social market economy, sustainable development, business ethics, good governance and dialogue.