



EUROPEAN COMMISSION
DIRECTORATE-GENERAL
TAXATION AND CUSTOMS UNION
Direct taxation, Tax Coordination, Economic Analysis and Evaluation
Company Taxation Initiatives

Brussels, 30 September 2013
Taxud/D1/JT

DOC: Platform/003/2013/EN

PLATFORM FOR TAX GOOD GOVERNANCE

Draft Discussion Paper on the "Tax Havens" Recommendation¹

Meeting of 16 October 2013

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¹ Commission Recommendation of 6.12.2012, C(2012) 8805 final, regarding measures intended to encourage third countries to apply minimum standards of good governance in tax matters.

A. DIRECT TAXATION WITHIN THE EU

1. Direct taxation is generally a competency of the individual Member States. They are free to design their direct tax systems and set the accompanying tax rates, while observing the provisions of the Treaties, such as the rules on State Aid. In order to ensure the proper functioning of the internal market, however, a regulatory framework observed by all Member States has been developed within the EU that also covers direct taxation. This framework aims at preventing distortions of the internal market by ensuring appropriate cooperation between Member States' tax administrations², by eliminating tax barriers³ and by agreeing a clear distinction between acceptable and harmful tax competition⁴.
2. This existing regulatory framework could still benefit from substantial improvements, as illustrated by various pending legislative proposals for amendment as well as new legislative proposals such as the Council Directive on a Common Consolidated Corporate Tax Base (CCCTB). Yet it currently already provides for a common set of minimum standards for cooperation and coordination between all Member States in tax matters that is not necessarily present to the same extent between Member States and third countries. It generally is for each Member State separately to arrange its relations with third states⁵, while respecting the provisions on the freedom of capital that also apply to relations with third countries.

B. AGGRESSIVE TAX PLANNING IN RELATION TO THIRD COUNTRIES

3. Aggressive tax planning in general can be described as the practice whereby tax payers exploit loopholes of a single tax system or mismatches in the interaction between two or more tax systems via complex and/or artificial arrangements to reduce their tax liability. In these cases, the tax savings could be considered to be unintended by any of the jurisdictions involved, but the arrangement are generally not illegal. Such tax planning schemes frequently lack transparency and are therefore difficult to detect. Member States may not even be aware of their existence and therefore fail to propose effective remedies. It is therefore plausible that some schemes would not achieve their intended tax benefits if they were subject to effective exchange of information provisions.
4. In some other cases, tax planning arrangements are (partly) built on special tax regimes or specific features within the tax system of an individual jurisdiction. These regimes or

² Savings Tax Directive and Council Directive 2011/16/EU on Administrative Cooperation.

³ Parent-Subsidiary Directive, Interest & Royalties Directive.

⁴ Code of Conduct for Business Taxation.

⁵ Apart from exceptions such as the agreements with 5 third states to provide for measures equivalent to the Saving Tax Directive.

features specifically aim at attracting mobile activities or mobile income generators. A tax saving generated using such regimes or features could be considered intended – at least by the jurisdiction operating that regime or feature. Also in that situation, transparency and exchange of information by the jurisdiction operating the regime would help other countries to take effective remedies, where appropriate.

5. In summary, aggressive tax planning schemes can be considered to thrive on a lack of transparency, a lack of cooperation between tax authorities and the presence of special tax incentives.
6. Within the EU, we have established the policy and regulatory tax framework referred to above providing for a common set of minimum standards for tax cooperation and coordination between all Member States. However, such framework is so far missing in Member States' relations with third countries. It should therefore be no surprise that many aggressive tax planning schemes essentially concern arrangements between one or more Member States and one or more third countries.
7. Tax payers are generally free to organise their business as they see fit. For their relation with third countries they may be tempted to select the Member State that is most lenient towards aggressive tax planning schemes involving the third country in question. For example, they will prefer structuring their in- or outward investment to a specific third country via a Member State that has signed a double tax convention with that jurisdiction. This does not necessarily need to be a problem in all cases. However, it is a reason for concern if the third country in question offers tax regimes that would be considered harmful in the EU or does not provide for a level of tax cooperation that enables EU Member States affected to take appropriate remedies. In that case, the lenient approach of one MS towards a third country can hinder all other Member States to take effective action against aggressive tax planning schemes involving that third country and eroding EU tax base.
8. It is precisely to curb this lack of policy and regulatory coordination between Member States and third countries that has led the Commission to come forward with the so-called Tax Havens Recommendation. It aims at collectively promoting a set of minimum standards towards third countries that we already have implemented in the EU. Such collective action would represent a strong incentive for third countries to step up their standards for tax transparency, exchange of information and fair tax competition thereby significantly reducing opportunities for multinationals to engage in aggressive tax planning.

C. THE RECOMMENDATION ON 'TAX HAVENS'

9. The Recommendation directly builds on the established EU policy concerning the promotion of the EU principles on transparency and exchange of information and the

abolition of harmful tax measures as described in Commission Communication on promoting good governance in tax matters⁶ and Commission Communication on tax and development cooperation with developing countries on promoting good governance in tax matters⁷.

10. The ECOFIN Council welcomed the work by the Commission on developing measures to combat tax fraud, tax evasion and aggressive tax planning and recognised the useful role of the Recommendation in this regard. In addition the Council:

- confirmed its wish to promote the principles of good governance in the tax area (transparency, exchange of information and fair tax competition) amongst third countries;
- committed to further work on how best to ensure that third countries meet appropriate standards of good governance in tax matters, recalled the OECD list of non-cooperative jurisdictions and invited consideration of whether developing a European list of third country non-cooperative jurisdictions is appropriate; (...) and
- invited incoming Presidencies (...) to reinforce efforts in promoting standards of good governance in tax matters to third countries, underlining the importance of strengthening cooperation with the OECD and G20, sharing views, experiences and best practices between Member States.⁸

11. The Recommendation essentially has three elements:

- i. *It contains the criteria for identifying 'tax havens' by listing the minimum standards that should be applied by all third countries.*

The criteria are identical to the EU principles of good governance in tax matters and therefore represent the standards that already apply within the EU. They are therefore fully consistent with standing EU policy both internally and towards third countries.

- ii. *It recommends Member States to identify third countries that do not comply with these standards and to publicly list these jurisdictions (blacklisting).*

Member States are recommended to publish lists of third countries not complying with the minimum EU standards. If Member States already use the practice of publishing blacklists, then they should add such third states to the existing list. In

⁶ COM (2009) 201 final of 28 April 2009.

⁷ COM (2010) 163 final of 21 April 2010.

⁸ ECOFIN Council conclusions 14 May 2013, 9549/13, FISC94.

both cases they should make an explicit reference to the Recommendation on 'tax havens' in these lists.

- iii. *It contains measures that Member States are recommended to take against non-compliant third countries and in favour of compliant third countries.*

The measures listed in points 4.3, 5 and 6 of the Recommendation provide for a common set of negotiation tools. The threat of being blacklisted by Member States will already convince many third countries to consider complying with EU standards. The prospect of being offered closer cooperation and assistance or the conclusion of a double tax convention will be a further incentive for third countries to comply. Actual blacklisting itself may therefore not even be needed. It is important to clarify that even further stretching measures such as laid down in point 4.3 of the Recommendation must be seen as a measure of last resort in the common negotiation process, rather than an immediate automatic consequence for third countries of not meeting the EU standards.

D. THE CRITERIA FOR IDENTIFYING 'TAX HAVENS'

12. The criteria used in the Recommendation are based on the EU principles of good governance in tax matters: transparency, exchange of information and fair tax competition.
13. Concerning the first two elements, the Global Forum on Transparency and Exchange of Information for Tax Purposes (hereinafter "the Global Forum") has monitored the implementation of international standards of transparency and exchange of information for tax purposes which have been endorsed at global level. In addition, the Global Forum engaged in a comprehensive peer review process as of 2009, concerning the implementation of these standards.
14. This review process includes two phases: a Phase 1 review concentrating on the presence of the appropriate legal framework to exchange information upon request in line with the international standard and a Phase 2 review, concentrating on the jurisdiction's organisational and administrative ability to actually act in accordance with the standards. The Global Forum prepares peer review reports per jurisdiction for both the Phase 1 and the Phase 2 reviews, issues recommendations where needed and monitors to what extent jurisdictions act upon the recommendations.
15. Given this existing international standard on transparency and exchange of information and the extensive existing mechanism to monitor the implementation of the standards, the assessment of whether a third country meets the Transparency and Exchange of Information criteria can, from a technical point of view, fully rely on the Global Forum's work for the purpose of following-up the Recommendation on 'tax havens'.

- 1) Do the Platform members agree that the work of the Global Forum should be used for assessing the Transparency and Exchange of Information criteria under the Recommendation?**
- 2) Do the Platform members foresee practical or administrative difficulties in applying this approach in practice?**

16. Concerning the third criterion, fair tax competition, the Code of conduct for business taxation has successfully eliminated more than 100 harmful measures in the EU since its formation in 1997 and prevented the introduction of new harmful measures since. The wide and positive experience in applying the Code by Member States in the context of the Code of Conduct Group has been the reason why the criteria of that Code also have been relied upon for the purposes of identifying harmful tax measures under the Recommendation on 'tax havens'⁹.

- 3) Do the Platform members support the use of the Code criteria and existing Code assessments as a benchmark for the purpose of applying the fair tax competition criterion of the Recommendation?**

Alternative listing criteria?

17. In an international context, the existence of differing tax legislation is a direct consequence of fiscal sovereignty. Some, typically small, third countries with limited financial needs have therefore opted for a low level of income tax which applies generally, both to individuals and to companies. Some jurisdictions have even completely refrained from levying an income tax at all.
18. Within the EU there currently is no agreed minimum level of company tax as far as the general company tax rate is concerned. Lower taxation for specific activities, types of income or businesses may qualify as harmful under the criteria of the Code of Conduct or the EU state aid provisions, but even that is not always the case. This means that generally speaking, there is no regulatory or political agreement on the acceptability of a generally applicable low (or no) company tax rate and even diversified company tax rates (boxes) may currently be accepted.

⁹ The Code of Conduct Group (business taxation), has been set up within the framework of the Council to assess the tax measures that may fall within scope of the Code of conduct for business taxation, OJ C 99, 1.4.1998, p. 1.

19. In that context, various multinational companies have developed business models involving low or no tax locations to lower their overall corporate tax bill. From various sides, it has therefore been suggested that the effective level of company taxation or the statutory company tax rate should somehow be reflected in the criteria for identifying 'tax havens' at EU level.
20. The Commission, however, has taken the position that minimum standards to be imposed upon third countries should reflect the regulatory and political standards that are currently already applied within the EU. Moreover, a low tax rate may not necessarily be considered problematic as such, as long as the jurisdiction concerned participates in international cooperation in order to allow other states to enforce their tax laws. If a low level of income tax or none at all is combined with a lack of transparency or exchange of information with other states, non-residents are effectively offered a tax shelter, allowing them to conceal some types of mobile income or capital from the tax administration of their state of residence.

- 4) Do Platform members consider the intra-EU tax standards and regulations important in relation to the promotion of tax standards and regulations towards third countries?**
- 5) Do Platform members consider there to be a need to review internal EU standards with a view to raising the bar in the context of recent international developments?**

E. BLACKLISTING

21. The explicit listing for tax purposes of non-compliant third countries is new at EU level. It is intended to ensure a consistency between Member States, to increase transparency and to increase pressure on the third countries concerned. It will also make it easier to develop and implement common measures in favour of compliant or against non-compliant third countries. The practical application, however, may require some further consideration and coordination.
22. A key element in the effectiveness of the Recommendation is the fact that it concerns common standards. Their effectiveness relies on their consistent implementation by all 28 Member States:
- Its effect would be reduced if some Member States reviewed countries A, B and C concluding to put country B on the list, whereas other Member States decided to review countries D, E and F concluding to put country E on the list.
 - Its effect would even be undermined if Member States decided to assess the same countries but came to different conclusions as regards the application of the Recommendation's criteria.

23. Consistency amongst Member States is therefore critical to ensure its effectiveness but there is currently no institutional arrangement to this purpose. Consistency concerns both the question which third countries should be reviewed for having harmful tax regimes as well as the review process itself. There are various possibilities to achieve this: Member States could discuss these issues in Council Working Parties, they could ask the Code of Conduct Group to play a role in the process or they could mandate the Commission to assist in the technical work.

6) Do Platform members agree on the need for a consistent listing process within the EU?

7) What is the Platform members' view on how such consistency could best be achieved?

F. (OTHER) MEASURES TO BE TAKEN BY MEMBER STATES AGAINST 'TAX HAVENS'

24. On top of the blacklisting, the Recommendation indicates a set of other measures to be applied in relation to third countries to encourage them to meet the EU minimum standards of good governance in tax matters. These measures have been listed in points 4.3, 5 and 6 of the Recommendation. The measures indicated in this Recommendation and applied by Member States must be compatible with Union law, in particular with the fundamental freedoms enshrined in the TFEU. As it concerns relations with third countries, this especially regards the freedom of capital as defined in Article 63 TFEU which stipulates that "...all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited."

25. The measures are frequently referred to as 'sanctions', but that does not seem to do proper justice. In the first place, the measures of points 5 and 6 are positive measures rewarding third countries that comply with the minimum standards or that are willing to comply but need some help with it. Only the measure mentioned in point 4.3 concerning the renegotiation, suspension or termination of existing double tax conventions is a 'negative' measure. However, the rationale behind the Recommendation is that the threat of being collectively blacklisted in combination with positive measures will suffice to convince most third countries to comply with EU standards. As a consequence, there would be limited practical application of the negative measures. Moreover, the negative measures are proportionate and allow flexibility based on a case by case assessment of both the seriousness of the non-compliance and of interests other than tax good governance.

26. For example: in case of a third country operating a harmful tax regime, the treaty could be renegotiated to exclude treaty benefits for tax payers benefitting from the harmful regime. Depending on the scope and damage done by the harmful regime, the treaty could alternatively be temporarily suspended awaiting the amendment. And only in case a third country is persistently unwilling to address the issues, the treaty could be cancelled.

- 8) Do Platform members agree on the need for consistency amongst Member States in applying the measures from the Recommendation?**
- 9) Do Platform members believe that a form of coordination would be needed with respect to the positive measures (assistance and secondment of personnel)?**
- 10) What is the Platform members' view on how such consistency could best be achieved?**
