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NOTE

From:	General Secretariat of the Council
To:	Delegations
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Subject:	ECOFIN Report to the European Council on Tax issues

1. The Council (ECOFIN) was invited to report back to the European Council on various tax issues mentioned, in particular in its conclusions of March and June 2012 and of 22 May 2013.

2. A draft ECOFIN Report to the European Council on Tax issues was prepared in the Council High Level Working Party on Tax issues (HLWP) on 23 May 2014, for submission to the Council via Coreper.

3. ECOFIN on 20 June 2014 endorsed the report as set out in the Annex, and agreed to forward it to the European Council on 26/27 June 2014.

ANNEX

ECOFIN REPORT TO THE EUROPEAN COUNCIL ON TAX ISSUES

1. This report covers various issues mentioned in the European Council Conclusions of 1/2 March 2012[1] devoted to growth, as well as in the European Council Conclusions of 28/29 June 2012 and the relevant Council Conclusions on the future of VAT and on the fight against tax fraud and tax evasion[2]. It gives an overview on the state of play of Council work regarding some key legislative proposals, which were specifically mentioned in the aforementioned conclusions, such as Energy Taxation, the Common Consolidated Corporate Tax Base, the Financial Transaction Tax, the revision of the Savings Tax Directive and the Negotiating Directives for Savings Taxation agreements with third countries.

2. In particular the European Council on 22 May 2013[3], and more recently on 24/25 October 2013[4] 19/20 December 2013[5] and 20/21 March 2014[6], identified tax dossiers where progress needed to be made. These dossiers are covered by the current report.

3. The report shows that during the Hellenic Presidency further progress has been made across a range of files, although additional work will be necessary.

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1 EUCO 4/3/12 REV 3 (items 9 and 21).
2 Docs 9586/12 FISC 63 OC 213 and 14877/12 ECOFIN 864 FISC 136 OC 579.
3 EUCO 75/1/13 REV 1, 22 May 2013.
4 EUCO 169/13, 24/25 October 2013.
5 EUCO 217/13, 19/20 December 2013.
6 EUCO 7/1/14 REV 1, 20/21 March 2014.

A. <u>Legislative files in the field of direct and indirect taxation</u>

Savings Taxation

1. In 2008, the Commission submitted a proposal to amend the Directive 2003/48/EC on taxation of savings income in the form of interest payments in order to increase its efficiency and to address significant loopholes which could facilitate tax fraud and evasion.

2. The technical work on this proposal has been finalised during previous Presidencies. However, Austria and Luxembourg indicated that level playing field concerns in relation to third countries should be addressed before a formal adoption of the Directive.

3. The Commission presented on 17 June 2011 a recommendation for a mandate to initiate negotiations with Switzerland, Liechtenstein, Andorra, Monaco and San Marino, in order to upgrade the EU's agreements with those countries and to ensure that they continue to apply measures equivalent to those in the EU.

4. At the Council on 14 May 2013 agreement was reached on the Negotiating Mandate, in line with the recent developments at global level, where it was agreed to promote automatic exchange of information as an international standard.

5. The European Council of 19/20 December 2013 concluded:

> *"27.* [*The European Council*] *calls for speeding up the negotiations with European third countries and asks the Commission to present a progress report to its March meeting. In the light of this, the revised Directive on the taxation of savings income will be adopted by March 2014."*

6. As a response to this call by the European Council, the Presidency addressed the issue at the preparatory bodies of the Council and submitted the file to the Council (ECOFIN) on 11 March 2014 for adoption. The Commission updated Member States on its contacts with the five non-EU Western European countries. The Council agreed that, once the European Council has politically endorsed this at its meeting on 20/21 March 2014, the formal adoption of the directive would take place at the Council formation meeting following the European Council.

7. The European Council endorsed the amended Directive on 20/21 March 2014 and, against this background the Council (AGRIFISH) adopted the revised Savings Directive in the form agreed at technical level at its meeting on 24 March 2014[7].

8. The European Council also called on the Commission to carry forth the negotiations with Switzerland, Liechtenstein, Monaco, Andorra and San Marino swiftly with a view to concluding them by the end of the year, and invited the Commission to report on the state of play at its December meeting. If sufficient progress is not made, the Commission's report should explore possible options to ensure compliance with the new global standard.

Common Consolidated Corporate Tax Base (CCCTB)

9. The Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB) was tabled by the European Commission on 16 March 2011, as a contribution to more growth-friendly taxation advocated by the Europe 2020 strategy. Since then, intensive technical discussions on this proposal have been taking place in the Council preparatory bodies.

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[7] OJ L 111/50 of 15 April 2014.

10. On 13 March 2013, the High Level Working Party (HLWP) agreed that:

a) work on the proposal should focus on a step-by-step approach;
b) the first step should focus on those matters which are related to the tax base;
c) the issue of consolidation should be addressed in a second step when work on the base has been sufficiently advanced;
d) the proposal was not yet ready for a political discussion;

and invited the Presidency to begin the task of drafting a compromise text on that basis.

11. In line with this roadmap, the Hellenic Presidency organised three Working Party meetings on this proposal during which several technical aspects of the tax base have been examined through the use of practical examples facilitating Member States to develop better understanding of their differences in complex issues. Furthermore the Presidency circulated a compromise text covering specific elements of the common corporate tax base such as stocks and work in progress (WIP), depreciation, provisions etc. The work on this proposal should continue in accordance with the roadmap set out in the ECOFIN report to the European Council on Tax Issues submitted in June 2013 during the Irish Presidency. While progress was made, some Member States maintained substantial objections to the proposal.

Revision of the Energy Taxation Directive (ETD)

12. In April 2011 the Commission presented to the Council a proposal for a Council Directive amending Directive 2003/96/EC restructuring the Community framework for the taxation of energy products and electricity ("the Energy Taxation Directive" or "the ETD"). The proposal presented by the Commission seeks to bring the ETD more closely into line with the EU's energy and climate change objectives as requested by the March 2008 European Council. In June and October 2012, the European Council asked that work and discussions on the Commission proposal on energy taxation should be carried forward.

13. The proposal has been discussed at five meetings of the Council's Working Party on Tax Questions and once at the High Level Working Party on Taxation during the Hellenic Presidency, building on work carried out by previous Presidencies.

14. Following the state of play report endorsed by ECOFIN on 21 June 2013, the Hellenic Presidency focussed its effort on an article by article examination, while paying attention to a number of open technical issues.

15. In this context, the Working Party has discussed compromise texts presented by the Presidency, where extensive discussions took place. However, major issues could still not be resolved and further discussions at technical level have to take place, including on: minimum rates for motor fuels; minimum rates for heating fuels; treatment of sustainable biofuels and transitional periods. Some Member States expressed their reservation regarding the structure of taxation.

16. [Against this background, the Presidency issued a progress report, which was submitted to ECOFIN on 20 June 2014 for endorsement.]

The common system of Financial Transaction Tax (FTT)

17. The proposal for a directive on a common system of financial transaction tax was submitted by the Commission to the Council on 28 September 2011. The proposal had as objectives a fair contribution of the financial sector to the costs of the crisis, avoiding fragmentation of the single market, and creating appropriate disincentives for transactions that do not enhance the efficiency of financial markets.

18. Unanimous agreement by all Member States could not be attained within a reasonable period. A number of Member States supported the examination of the FTT in the framework of enhanced cooperation. Adoption of a decision formally authorising enhanced cooperation took place at the ECOFIN meeting on 22 January 2013. A formal Commission proposal for a Directive implementing enhanced cooperation in the area of financial transaction tax was put forward to the Council on 14 February 2013.

19. The Hellenic Presidency has been continuing the work on the FTT at the level of the Working Party.

20. A first technical read-through of the proposal has been performed, during which the Commission presented and explained provisions of the proposal in detail and Member States had the opportunity to raise concrete questions, including on legal issues.

21. The Hellenic Presidency held two Council Working Party meetings in order to clarify important aspects of the imposition of the tax and progress the discussions. First of all, the interaction of the Proposal for a Directive on FTT with the current reform on the regulatory legal framework of the financial sector was examined. Moreover, clarifications on various aspects of the monetary policy of the Eurosystem and the possible interaction with the FTT were given by representatives of the European Central Bank, including on specific aspects of short-term financing instruments that could be taken into account in the final design of the tax. Finally, technical questions relating to the definitions and the scope of the Proposal of the Directive were discussed. The Council Legal Service gave its opinion on a number of aspects of the proposal.

22. Following discussions at the HLWP on 14 April 2014, the Council (ECOFIN) held an exchange of views on 6 May 2014, on the state of play of the Directive implementing enhanced cooperation in the area of FTT on the basis of a presidency note. The Presidency took note of the comments raised, also by non-participating States and of the joint Statement made by 10 participating Member States on how they see further work on this file.

23. Following this political discussion, the Hellenic Presidency intends to continue work at technical level as necessary before the end of June 2014.

VAT: Treatment of Vouchers

24. The Commission put forward a proposal in May 2012 to provide for common EU rules for the VAT treatment of vouchers. These changes are considered necessary to support businesses operating cross-border and to ensure that instances of double and non-taxation do not occur.

25. From discussions in the Working Party, it became clear that Member States agree on the real need for common rules on the treatment of VAT. It was also evident that agreement on the proposal would be desirable before the introduction of new 'B2C place of supply rules' in 2015, given the high proportion of sales transacted via vouchers for e-services and telecommunications.

26. During the Hellenic Presidency, the Working Party, in four meetings, continued to pay specific attention to definitions and the distribution of vouchers in a chain. On the basis of Presidency compromise texts, priority was given to the clarification of concepts and to reaching a common understanding on the definition of vouchers. The Working Party also discussed the practical application of the proposed legal provisions, taking into account the different business models. Although substantial progress was made in the definitions of different kinds of vouchers and the tax treatment of Single Purpose Vouchers, further work at technical level would still be necessary to smoothen out the different views of Member States on the tax treatment of Multi Purpose Vouchers and on the rules for their distribution in a chain.

VAT: Standard VAT Return

27. In October 2013 the Commission tabled a proposal for common EU rules regarding the standard VAT return. The proposal foresees a uniform set of requirements for businesses, when filing their VAT returns, which will replace the diverse national VAT returns. The aim of the proposal is to reduce administrative burden for businesses and particularly SMEs and remove divergences which are an obstacle to EU trade, whilst on the same time promoting voluntary compliance.

28. During the Hellenic Presidency the proposal has been examined at four meetings of the Working Party on Tax Questions and the first reading of the proposal has been completed, on a basis of a presidency note analysing the principles and the legal provisions of the proposal.

29. The Presidency presented a compromise proposal at the meeting of the Working Party on Tax Questions on 24 April 2014, addressing concerns of Member States, in particular as regards their needs for flexibility on the payment, the methods for electronic submission, corrections of the VAT return as well as annual VAT returns, taking into account potential cost, fight against tax fraud and budgetary consequences. Regarding the content of the VAT return, the Presidency proposed that the obligatory and optional information of the Standard VAT return should be defined in the Council and restricted the conferral of implementing powers to the Commission only to purely technical issues. The Presidency compromise proposal received ample support, although issues that remained problematic for Member States, were in particular: the conferral of implementing powers to the Commission, the proposed threshold for SMEs to submit quarterly returns, the need of some Member States to request monthly returns in any case and the need to require additional information from business, for control purposes, according to the individual needs of each Member-State. Some Member States raised the issue of the need of evaluation of the costs and benefits of the proposal, taking also into account already implemented changes in the field of administrative cooperation for combatting fraud. The actual content of the standard VAT return will be thoroughly analysed in the Working Party of Tax Questions.

30. [The ECOFIN Council adopted a Presidency progress report and Conclusions on the Standard VAT Return on 20 June 2014.]

VAT: Mandate for Commission to open negotiations for agreement between EU and Norway, and EU and Russia, on administrative cooperation, combating fraud and recovery of claims in the field of VAT.

31. The European Council of 1/2 March 2012 invited the European Commission to develop concrete ways rapidly to improve the fight against tax fraud and evasion, including in relation to third countries. The Commission in its action plan on tax fraud and evasion included the possibility of negotiating mutual assistance agreements on VAT with certain third countries.

32. In February 2014, the Commission tabled two recommendations for two Council decisions to authorize the Commission to open negotiations for agreement between the European Union and (a) Norway and (b) Russia on administrative cooperation, combating fraud and recovery of claims in the field of VAT.

33. The Hellenic Presidency examined in two meetings the draft recommendations and presented compromise proposals. Work will continue with a view to progressing on the remaining issues.

VAT: Commission reports.

34. The Seventh report under Article 12 of Regulation (EEC, Euratom) no 1553/89 on VAT collection and control procedures and the Report on the application of Council Regulation (EU) no 904/2010 concerning administrative cooperation and combating fraud in the field of value added tax were discussed at the WPTQ of 11 April 2014.

Proposal for a Directive amending Directive 2011/16/EU on administrative cooperation in the field of taxation (DAC)

35. Following the European Council conclusions of 22 May 2013, the Commission presented on 12 June 2013 a proposal for the Revision of Directive 2011/16/EU. The aim is to upgrade and broaden automatic exchange of information in the area of direct taxation, especially for financial income, by aligning EU law with the new OECD standard (the Common Reporting Standard), providing tax administrations with a very powerful new tool to tackle cross-border tax evasion and non-compliance.

36. On 19/20 December 2013, the European Council called on the Council "to reach unanimous political agreement on the Directive on Administrative cooperation in early 2014" and, in its Conclusions on 20/21 March 2014, it invited the Council "to ensure that, with the adoption of the Directive on Administrative Cooperation by the end of 2014, EU law is fully aligned with the new global standard".

37. In line with the Council Conclusions, the Presidency continued to play an active and constructive role in the completion of the work on the global standard at OECD level and made efforts at EU level to ensure that international developments can be rapidly taken into account by EU law, also with a view to minimising the administrative burden for European financial institutions and tax administrations.

38. So far discussions at the Working Party on Tax Questions have focused on aligning the scope of the automatic exchange of information with the emerging single global standard. On that basis, the work undertaken by the OECD has been analysed during WP technical meetings. This also resulted in a letter by the Council Presidency to the OECD Secretariat outlining the points of concern that Member States' experts had discussed, with a view to providing input to ongoing discussions at the OECD.

39. During the Council High Level Working Party in April, the Hellenic Presidency highlighted the issue of aligning the implementation timetables for the Directive on Administrative Cooperation and the global standard as envisaged by the "early adopters". Agreement could not be reached, due to some reservations.

40. The work on the Proposal for a Directive amending Directive 2011/16/EU on administrative cooperation in the field of taxation concerning its correlation with the Common Reporting Standard developed by OECD continued at the Council's Working Party on Tax Questions.

Proposal for a Directive amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States

41. On 25 November 2013, the Commission submitted a proposal to amend Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States. In substance the proposal aimed at tackling hybrid loan mismatches within the scope of the PSD and introducing a general anti-abuse rule in order to protect the functioning of this directive.

42. In its conclusions on 19/20 December 2013, the European Council stated that "progress should also be made quickly towards agreement on amending the Parent-Subsidiary Directive".

43. The Presidency launched various technical discussions at the Working Party on Direct Taxation, aiming at finding a tangible solution to the issue of "double non taxation". During the technical debate it became apparent the wide support for closing the hybrid loan mismatch loophole as quickly as possible whereas the part of the proposal dealing with the general anti-abuse rule required more work.

44. At its meeting on 8 April 2014, the Hellenic Presidency circulated a compromise text which splits the proposal. It suggests to reach an early agreement on the hybrid loan mismatch, while clarifying in a statement to be added to the Council Minutes that the Council will continue to work on the remaining elements of the proposal. The intention of the incoming Italian Presidency to allow for a more in-depth discussion of further cases of double non-taxation in the Council was noted.

45. Against this background the Presidency submitted the amendment on the Parent Subsidiary Directive in the agreed by a vast majority at technical level to the Council (ECOFIN) on 6 May 2014 in view of reaching a political agreement. The political agreement could not yet be reached due to reservations by two delegations. Therefore the Presidency organised an experts meeting in order to clarify the text as necessary but the Working Party on Tax Questions could not reach agreement on the remaining issues. This file was submitted to Coreper on 28 May 2014 with a view to reaching political agreement at the Council (ECOFIN) in June.

46. [The Council (ECOFIN) adopted the PSD Directive on 20 June 2014.]

B. Tax Policy Coordination

Important work in the area of Tax Policy coordination (outside of EU tax legislation) has been taken forward during the Hellenic Presidency.

a) Code of Conduct Group (Business taxation)

In December 2013, the Council welcomed the report on the progress of the work of the Code of Conduct Group during the Lithuanian Presidency (16656/13 FISC 226) and encouraged the Group to continue work on the basis of the Work Programme approved in 2011 (doc. 18398/11 FISC 167). On that basis, the Group met three times under the Hellenic Presidency and continued work on rollback and standstill of harmful tax regimes and the Work Programme. Moreover, the Council invited the Commission to continue and conclude the dialogue with Switzerland and invited the Group to analyse the third criterion of the Code of Conduct as contained in the existing mandate, both by the end of June 2014.
A new six-monthly report has been prepared during the Hellenic Presidency and submitted to the Council, together with the Council conclusions.[8] The work of the Group will continue on the basis of the Work programme approved in 2011.

b) Code of Conduct Group – Anti Abuse Subgroup on hybrid mismatches

The Anti Abuse Subgroup launched its work on hybrid mismatches during the Irish Presidency. [The report incorporating a proposal for draft guidance on intra-EU hybrid entity mismatches to the Code of Conduct Group of 3 June 2014, was welcomed]. On that basis, during the Hellenic Presidency, the Anti Abuse Subgroup, which met twice continued considering solutions to tackle undesirable effects of mismatches involving intra-EU hybrid entities. The Subgroup also continued discussions on mismatches involving intra-EU hybrid permanent establishments with a view to preparing a draft guidance. The Subgroup has reported to the Code of Conduct Group on its progress [and submitted draft guidance].

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8 Docs /13 FISC , /13 FISC 230.

c) Other tax coordination issues

The Hellenic Presidency has continued work on new areas already identified by previous Presidencies for possible tax policy coordination in the HLWP:

i) EU/OECD: Base Erosion and Profit Shifting (BEPS)

- Paragraph 6 of the Council conclusions of 14 May 2013 relates to coordination and cooperation with the OECD and G20 on BEPS:

  "6. SUPPORTS further efforts at OECD level on Base Erosion and Profit Shifting (BEPS) and RECALLS the European Council Conclusions of 13 and 14 March 2013 on the need for close cooperation with the OECD and the G20 to develop internationally agreed standards for the prevention of base erosion and profit shifting and in particular NOTES the European Council call for the European Union to coordinate its positions. NOTES that this coordination will take place through the appropriate Council bodies including the High Level Working Party and WELCOMES that progress at international level in this area is being monitored. To this end, the EU should closely monitor its legal framework and identify where common solutions would best ensure effectiveness and efficiency."

- In Paragraph 27 of its conclusions of 19/20 December 2013, the European Council states the following:

  "27. Recalling its conclusions of May 2013, the European Council calls for further progress at the global and EU levels in the fight against tax fraud and evasion, aggressive tax planning, base erosion and profit shifting (BEPS) and money laundering. The European Council welcomes work undertaken in the OECD and other international fora to respond to the challenge of taxation and ensure fairness and effectiveness of tax systems, in particular the development of a global standard for automatic exchange of information, so as to ensure a level playing-field."

- Member States were informed by the Presidency on the state of play on the ongoing work in the OECD, as well as the next steps for each of the fifteen BEPS actions, with reference, where appropriate to the corresponding EU actions, with a view to ensuring coordination and consistency at EU level.
- Moreover, during the HLWP meeting on 19 November 2013, the importance of a concerted action on BEPS in connection with European Tax legislation was discussed. Incoming Presidencies were invited to address this issue by setting up a BEPS/EU legislation focused working programme and the results and interim results of this work should be reported by the Council at the end of each Presidency's term.
- Following its intention indicated to take this issue forward and to ensure timely monitoring, while using the HLWP as a focal point and reporting to the Council as appropriate, the Hellenic Presidency examined BEPS in the EU context, on a basis of a note by five Member States. This note proposed that work at EU level begins by identifying specificities of the EU tax legislation which can favour BEPS through a fact findings approach, starting from examples of aggressive tax planning techniques. It was suggested, in the note by the five Member States, that this exercise could be conducted by the Member States with the assistance of the Commission, with the aim of reporting back to the HLWP. Moreover, the importance of identifying the constraints deriving from the EU legal framework, including as interpreted by the European Court of Justice, the areas of major concerns and the possible solutions to ensure that the responses to BEPS issues can be in line with EU principles, were indicated.
- Although the importance of the issue raised by the note by the five Member States was acknowledged, several issues emerged from the discussions including the need to prioritise work. The Commission indicated its intention to assist Member States and organise a discussion in the context of the Working Party IV (Direct Taxation) starting with a discussion on the interaction between the EU Treaty Freedoms and BEPS. At the HLWP on 23 May 2014, the Commission briefly informed Member States that a discussion had taken place at the Working Party IV on the interaction between EU Treaties and the Limitation of Benefit clause. The Hellenic Presidency invites the incoming Presidency to consider the above issues further.

ii) Tax fraud, avoidance and aggressive tax planning: exchange of best practices

The Hellenic Presidency gave Member States the opportunity to exchange best practices/reforms regarding the fight against fraud, tax avoidance and aggressive tax planning in the framework of the Council HLWP. Croatia made a detailed presentation on its national approach to these issues.

iii) Tax in non tax dossiers

On 19 November 2013, the HLWP agreed that tax provisions leading to any changes in Member States' tax laws or administrative practices or having other consequences on taxation should fall under an alert mechanism at the earliest possible stage. The Hellenic Presidency continued this effort and, on the basis of a Presidency note, the HLWP agreed on an informal Early Alert Mechanism to be followed in order to raise awareness on tax provisions included in non-tax dossiers.

iv) Digital economy: Follow-up to the European Council on 24/25 October 2013

- The HLWP discussed the follow-up of the European Council conclusions of 24/25 October 2013, covering tax aspects linked to the digitalisation of the economy:

  "4. The ongoing work to tackle tax evasion, tax fraud, aggressive tax planning, tax-base erosion and profit shifting is also important for the digital economy. Member States should further coordinate their positions where appropriate in order to achieve the best possible solution for Member States and the EU in the OECD/BEPS (Base Erosion and Profit Shifting) framework. In its ongoing VAT review, the Commission will also address issues which are specific to the digital economy, such as differentiated tax rates for digital and physical products. The European Council welcomes the Commission's initiative to set up an expert group on taxation of the digital economy. The European Council will return to taxation-related issues at its December 2013 meeting."

- The potential link between the digitalisation of the economy and ongoing work in the Council on tackling tax evasion, tax fraud and aggressive tax planning and in the context of the VAT review was stressed.

- The Commission was invited to report back on its work to the Council by the end of the Hellenic Presidency.

- The Hellenic Presidency held discussions on the basis of a paper providing the background information and describing the main issues in the area of international direct taxation, as well as the approaches chosen in the past (i.e. before the work on these issues was re-opened under the BEPS Action Plan in 2013). In the area of indirect taxation, main emerging issues and orientations for future work were also examined. Moreover, there were presentations on the state of play of the ongoing work undertaken in the OECD Task Force on the Digital Economy and the Commission Expert Group on Taxation of the Digital Economy. Finally, the French delegation provided its reflection on a possible solution to address the issue of taxation of the digital economy at the EU level.

v) HLWP updates on other issues:

- The HLWP was updated on FATCA agreements at the meeting on 4 February 2014.

- Following discussions during the Irish Presidency, where there was a very positive engagement and agreement that the Commission would be invited to present on an annual basis the tax aspects of the European Semester process, the issues raised from a tax policy perspective in the Annual Growth Survey 2014 were discussed.