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From: General Secretariat of the Council

To: Permanent Representatives Committee/Council

Subject: The EU list of non-cooperative jurisdictions for tax purposes

- Report by the Code of Conduct Group (Business Taxation) suggesting amendments to the Annexes of the Council conclusions of 12 March 2019, including the de-listing of two jurisdictions, and the endorsement of a guidance note

1. On 12 March 2019, the ECOFIN Council adopted Council conclusions¹ that revised the EU list of non-cooperative jurisdictions for tax purposes (Annex I) and the state of play with respect to commitments taken by cooperative jurisdictions to implement tax good governance principles (Annex II) initially endorsed by the ECOFIN Council on 5 December 2017² and subsequently modified/updated by the Council on 23 January 2018³, 13 March 2018⁴, 25 May 2018⁵, 2 October 2018⁶, 6 November 2018⁷ and 4 December 2018⁸.

¹ OJ C 114 2019 pages 2-8.
² OJ C 438 2017 pages 5-24.
³ OJ C 29 2018 page 2.
⁴ OJ C 100 2018 pages 4-5.
⁵ OJ C 191 2018 pages 1-3.
⁶ OJ C 359 2018 pages 3-5.
⁷ OJ C 403 2018 pages 4-6.
⁸ OJ C 441 2018 pages 3-4.

2. Furthermore, recalling paragraph 11 of the Council conclusions of 5 December 2017, the Council conclusions of 12 March 2019 confirmed that the Code of Conduct Group (hereafter "COCG") *"should recommend to the Council to update at any time, and at least once a year, the EU list set out in Annex I as well as the state of play set out in Annex II on the basis of any new commitment taken or of the implementation thereof; but, as from 2020 onwards, such updates of the EU list should be done no more than twice a year, leaving sufficient time, where appropriate, for Member States to amend their domestic legislation"* (paragraph 16), thereby agreeing to keep a dynamic process throughout 2019.
3. The EU list of non-cooperative jurisdictions for tax purposes was subsequently modified by the ECOFIN Council on 17 May 2019⁹ and 14 June 2019¹⁰, with the de-listing of Aruba, Barbados, Bermuda and Dominica. Further updates to Annexes I and II of the Council conclusions of 12 March 2019 were also made on the same occasion.

De-listings from Annex I

4. Since then, the Marshall Islands adopted on 15 August 2019 an amendment to its Economic Substance Regulation, 2018 thereby resolving the EU's last area of concern¹¹, i.e. the issue of evidencing tax residence in another jurisdiction, which created a significant risk of circumvention of the substance requirements and related information exchange.

⁹ OJ C 176 2019 pages 2-5.

¹⁰ OJ C 210 2019 pages 8-11.

¹¹ The Marshall Islands had adopted on 21 February 2019 earlier amendments to its Economic Substance Regulations, 2018 but these were not deemed sufficient by the COCG considering this last area of concern and for this reason the Marshall Islands was listed on Annex I by the ECOFIN Council on 12 March 2019.

The COCG subgroup on external issues examined this amendment at its meeting of 4 September 2019 and concluded that the Marshall Islands had now fully implemented its commitment to introduce substance requirements under criterion 2.2 and could therefore be removed from Annex I (delisting). Considering that the Marshall Islands' review by the Global Forum is ongoing and should be released later in September 2019, the subgroup also concluded that the Marshall Islands should however remain in section 1.2 of Annex II (exchange of information on request) pending the result of this review. The COCG confirmed these conclusions at its meeting of 13 September 2019.

5. The United Arab Emirates (UAE) adopted on 30 April 2019 its Economic Substance Regulation through Resolution n°31 of 2019. This Regulation reflected most of the feedback that it had received from the COCG but introduced a general exemption for all entities in which the UAE government, or any of the Emirates of the UAE, had direct or indirect ownership (no threshold) in its share capital. The COCG meeting of 20 May 2019 considered that this created a significant risk of circumvention of the substance requirements and concluded that the UAE was still not compliant with criterion 2.2. However, since then the UAE adopted on 1st September 2019 an amendment to Resolution n°31 of 2019 that introduced a threshold of 51% government ownership (direct or indirect) of share capital.

The COCG subgroup on external issues examined the above draft legislative amendment at its meeting of 4 September 2019 and concluded that, if adopted, it would resolve EU's concerns. The COCG at its meeting of 13 September subsequently received the confirmation of the adoption of the above-mentioned amendment, and concluded that the UAE had now fully implemented its commitment to introduce substance requirements under criterion 2.2 and could therefore be removed from Annex I (delisting).

Updates of Annex II

6. Namibia having joined on 26 August 2019 the Global Forum on transparency and exchange of information for tax purposes, the COCG meeting of 13 September 2019 agreed that it should be removed from section 1.2 of Annex II.
7. Morocco and Serbia having ratified, respectively on 22 May and 30 August 2019, the OECD Multilateral Convention on Mutual Administrative Assistance ("MAC") as amended, the COCG meeting of 13 September 2019 agreed that they should be removed from section 1.3 of Annex II.
8. Costa Rica adopted on 15 May 2019 legislative amendments to its Free Zones regime (CR001). These were reviewed by the OECD Forum on Harmful Tax Practices (FHTP) at its 19-21 June 2019 meeting, which concluded that they are not harmful. The COCG endorsed this conclusion at its meeting of 10 July 2019. Considering that these legislative amendments also addressed the manufacturing activities falling under the free zones regime (CR002), the COCG concluded at its meeting of 13 September 2019 that Costa Rica had fully implemented its commitment to remove the harmful features of its Free Zones regime and should therefore be removed from section 2.1 of Annex II.
9. Mauritius adopted on 25 July 2019 its Finance Bill 2019 and on 16 August 2019 additional regulations that amended the legislation applicable to its Freeport zone (MU012) and Partial Exemption (MU010) regimes.

The COCG meeting of 13 September 2019 examined these amendments and concluded that Mauritius had met its commitment to address the deficiencies identified in these two regimes: whilst the Freeport zone regime is no longer preferential, substance requirements have been introduced in both regimes and the issue of lack of anti-abuse rules has been addressed by the introduction of CFC rules broadly aligned with those of EU's anti tax avoidance directive (ATAD 1). As a result, the COCG concluded that Mauritius should therefore be removed from section 2.1 of Annex II.

10. Switzerland adopted its tax reform in October 2018 but the entry into force and entry into application of the legislation were postponed pending the outcome of the referendum in May 2019 and for this reason Switzerland was granted an additional year to comply with criterion 2.1 "*due to genuine institutional or constitutional issues despite tangible progress in 2018*". Following the positive outcome of this referendum, Switzerland informed the COCG in August 2019 that the official results had been published in the Official Gazette. As a result, the relevant legislation entered into force on 16 July 2019 and will enter into application on 1st January 2020, whilst Switzerland had already announced that its federal regimes CH004 and CH005 had been closed to new entrants as from 1st January 2019.

The COCG meeting of 13 September 2019 reviewed the situation and concluded that Switzerland should therefore be removed from section 2.1 of Annex II on the basis that the necessary reforms had been adopted and gazetted.

11. The COCG meeting of 13 September 2019 also agreed that the deadline of Namibia for complying with criterion 2.1 should be changed from 9 November to end 2019, which requires an amendment to Annex II. The objective is to align the deadline with that of other criteria and jurisdictions and respect national budgetary cycles.
12. Furthermore, Albania, Bosnia and Herzegovina, Eswatini and Namibia having joined the Inclusive Framework on BEPS respectively on 8 August, 11 July, 26 July and 9 August 2019, the Code of Conduct Group agreed on 13 September 2019 that they should be removed from section 3.1 of Annex II.
13. As a result, Albania, Costa Rica, Mauritius, Serbia and Switzerland would be removed entirely from Annex II.

Other issues

14. At its meeting of 13 September 2019, the COCG also reviewed jurisdictions' situation following the end of the "two out of three" exception for tax transparency criteria at the end of June 2019, and concluded that all jurisdictions covered met EU requirements. In particular it concluded that:
- a) In order to meet EU criterion 1.3¹², the USA should have arrangements with all Member States allowing for both automatic exchange of information (AEOI) and effective exchange of information on request (EOIR) considering that that it has signed but not yet ratified the Protocol amending the MAC. For AEOI purposes, the FATCA competent authority agreements (CAA) between the USA and all Member States were deemed sufficient to meet EU's requirement. As for EOIR, the USA has double taxation treaties (DTT) and/or Tax Information Exchange Agreements (TIEA) with all Member States but Croatia. However, Croatia and the USA rely on the 1988 unamended MAC for EOIR purposes and, following a dialogue between the COCG Chair and the US Treasury, it was noted that the EOIR that has taken place to date between Croatia and the USA is effective and satisfactory by both sides. Furthermore, the Minister of Finance of Croatia received on 3 September 2019 an official letter from the US Treasury that stated that it would continue to exchange tax information with Croatia in line with international standards and the respective needs of both sides. As a result, the COCG concluded that the USA can be considered to fulfil the conditions to meet criterion 1.3.
 - b) Niue adopted the necessary primary and secondary legislation for implementing the Common Reporting Standard (CRS) and completed by 2 September 2019 the necessary steps for the activation of AEOI bilateral exchange relationships with all EU Member States. As a result, the COCG concluded that Niue is compliant with criterion 1.1.

¹² The USA were already deemed to meet EU criteria 1.1 and 1.2 in December 2017.

c) Other jurisdictions identified by the COCG as possibly affected by the end of the "two out of three" exception (notably: Israel and Vanuatu) had already complied at an earlier stage by completing the necessary steps for the activation of AEOI bilateral exchange relationships with all EU Member States.

15. The COCG also examined legislative changes that occurred in the Cayman Islands under criterion 2.2 after the ECOFIN Council meeting of 12 March 2019. These amendments were examined by the COCG meeting of 20 May 2019 and COCG subgroup meetings of 5 July and 4 September 2019, which expressed concerns that the Cayman Islands introduced features that could be considered as not compliant with EU requirements.

Further legislative changes, gazetted on 10 September 2019¹³, were examined by the COCG meeting of 13 September, at which the Group concluded that the Cayman Islands remains compliant with EU criterion 2.2 (except for what concerns collective investment funds¹⁴).

16. The COCG meeting of 13 September 2019 also agreed on a new guidance on 'foreign source income exemption regimes' set out in Annex 2 to this note.

The ECOFIN Council of 12 March 2019 had noted with concern the replacement of harmful preferential tax regimes by such measures of similar effect in certain jurisdictions. These jurisdictions took commitments to amend or abolish these measures by the end of 2019 and, since then, bilateral exchanges at technical level have taken place. This guidance therefore aims at formalising the requirements set by the EU as well as to provide transparency on the approach adopted by the COCG in respect of these regimes.

¹³ <http://www.gov.ky/portal/pls/portal/docs/1/12852496.PDF>

¹⁴ The Cayman Islands committed to addressing the concerns relating to economic substance in the area of collective investment funds and adapt its legislation by end 2019.

Way forward

17. The Permanent Representatives Committee is therefore invited to suggest that the ECOFIN Council in October 2019:
- adopt the updated Annexes I and II to the Council conclusions of 12 March 2019 set out in Annex 1 to the present note, which reflect the developments described above, as an "A" item on the agenda,
 - agree on their publication in the Official Journal,
 - endorse the conclusion reached by the COCG in respect of the end of the "two out of three exception" for tax transparency criteria, and Cayman Islands under criterion 2.2,
 - endorse the guidance on foreign source income exemption regimes attached to the present note (Annex 2).

With effect from the day of publication in the *Official Journal of the European Union*, Annexes I and II of the Council conclusions of 12 March 2019 on the revised EU list of non-cooperative jurisdictions for tax purposes¹⁵, as amended on 22 May 2019¹⁶ and 21 June 2019¹⁷, are replaced by the following new Annexes I and II:

The EU list of non-cooperative jurisdictions for tax purposes

1. American Samoa

American Samoa does not apply any automatic exchange of financial information, has not signed and ratified, including through the jurisdiction they are dependent on, the OECD Multilateral Convention on Mutual Administrative Assistance as amended, did not commit to apply the BEPS minimum standards and did not commit to addressing these issues.

2. Belize

Belize has not yet amended or abolished one harmful preferential tax regime.

Belize's commitment to amend or abolish its newly identified harmful preferential tax regime by the end of 2019 will be monitored.

¹⁵ OJ C 114, 26.03.2019, pp. 2-8.

¹⁶ OJ C 176, 22.05.2019, pp. 2-5.

¹⁷ OJ C 210, 21.06.2019, pp. 8-11.

3. Fiji

Fiji has not yet amended or abolished its harmful preferential tax regimes.

Fiji's commitment to comply with criteria 1.2, 1.3 and 3.1 by the end of 2019 will continue to be monitored.

4. Guam

Guam does not apply any automatic exchange of financial information, has not signed and ratified, including through the jurisdiction they are dependent on, the OECD Multilateral Convention on Mutual Administrative Assistance as amended, did not commit to apply the BEPS minimum standards and did not commit to addressing these issues.

5. Oman

Oman does not apply any automatic exchange of financial information, has not signed and ratified the OECD Multilateral Convention on Mutual Administrative Assistance as amended, and has not yet resolved these issues.

6. Samoa

Samoa has a harmful preferential tax regime and did not commit to addressing this issue.

Furthermore, Samoa committed to comply with criterion 3.1 by the end of 2018 but has not resolved this issue.

7. Trinidad and Tobago

Trinidad and Tobago has a “Non-Compliant” rating by the Global Forum on Transparency and Exchange of Information for Tax Purposes for Exchange of Information on Request.

Trinidad and Tobago's commitment to comply with criteria 1.1, 1.2, 1.3 and 2.1 by the end of 2019 will be monitored.

8. US Virgin Islands

US Virgin Islands does not apply any automatic exchange of financial information, has not signed and ratified, including through the jurisdiction they are dependent on, the OECD Multilateral Convention on Mutual Administrative Assistance as amended, has harmful preferential tax regimes, did not commit to apply the BEPS minimum standards and did not commit to addressing these issues.

9. Vanuatu

Vanuatu facilitates offshore structures and arrangements aimed at attracting profits without real economic substance and has not yet resolved this issue.

State of play of the cooperation with the EU with respect to commitments taken to implement tax good governance principles

1. Transparency

1.1 Commitment to implement the automatic exchange of information, either by signing the Multilateral Competent Authority Agreement or through bilateral agreements

The following jurisdictions are committed to implement automatic exchange of information by end 2019:

Palau and Turkey

1.2 Membership of the Global Forum on transparency and exchange of information for tax purposes ("Global Forum") and satisfactory rating in relation to exchange of information on request

The following jurisdictions, which committed to have a sufficient rating by end 2018, are waiting for a supplementary review by the Global Forum:

Anguilla, Marshall Islands and Curaçao.

The following jurisdictions are committed to become member of the Global Forum and/or have a sufficient rating by end 2019:

Jordan, Palau, Turkey and Vietnam.

1.3 Signatory and ratification of the OECD Multilateral Convention on Mutual Administrative Assistance (MAC) or network of agreements covering all EU Member States

The following jurisdictions are committed to sign and ratify the MAC or to have in place a network of agreements covering all EU Member States by end 2019:

Armenia, Bosnia and Herzegovina, Botswana, Cabo Verde, Eswatini, Jordan, Maldives, Mongolia, Montenegro, Namibia, Republic of North Macedonia, Palau, Thailand and Vietnam.

2. Fair Taxation

2.1 Existence of harmful tax regimes

The following jurisdiction, which committed to amend or abolish its harmful tax regimes covering manufacturing activities and similar non-highly mobile activities by end 2018 and demonstrated tangible progress in initiating these reforms in 2018, was granted until end 2019 to adapt its legislation:

Morocco.

The following jurisdictions, which committed to amend or abolish their harmful tax regimes by end 2018 but were prevented from doing so due to genuine institutional or constitutional issues despite tangible progress in 2018, were granted until end 2019 to adapt their legislation:

Cook Islands and Maldives.

The following jurisdictions are committed to amend or abolish harmful tax regimes by end 2019:

Antigua and Barbuda, Australia, Curaçao, Morocco, Namibia, Saint Kitts and Nevis, Saint Lucia and Seychelles.

The following jurisdiction is committed to amend or abolish a harmful tax regime by end 2020:

Jordan.

2.2. Existence of tax regimes that facilitate offshore structures which attract profits without real economic activity

The following jurisdictions, which committed to addressing the concerns relating to economic substance in the area of collective investment funds, have engaged in a positive dialogue with the Group and have remained cooperative, were granted until end 2019 to adapt their legislation:

Bahamas, Bermuda, British Virgin Islands and Cayman Islands.

The following jurisdiction is committed to addressing the concerns related to economic substance by end 2019:

Barbados.

3. Anti-BEPS Measures

3.1 Membership of the Inclusive Framework on BEPS or commitment to implementation of OECD anti-BEPS minimum standards

The following jurisdictions are committed to become member of the Inclusive Framework on BEPS or implement OECD anti-BEPS minimum standards by end 2019:

Jordan and Montenegro.

The following jurisdictions are committed to become member of the Inclusive Framework on BEPS or implement OECD anti-BEPS minimum standards if and when such commitment will become relevant:

Nauru, Niue and Palau.

Guidance on

FOREIGN SOURCE INCOME EXEMPTION REGIMES

On 20 May 2019, the Code of Conduct Group (COCG) agreed on an approach to assess foreign sourced income exemption regimes. Based on this approach, these guidelines should provide direction for jurisdictions that have already taken a commitment to amend their foreign source income exemptions, due to harmful features identified by the COCG. The guidelines will also serve as a basis for the screening of other jurisdictions with similar regimes before the end of 2019.

Foreign source income exemption regimes, or regimes that charge corporate tax on a territorial basis are not, in themselves, problematic. In fact, exempting foreign profits is acceptable and even recommendable, in certain cases, to prevent double taxation. However, problems arise when such regimes not only prevent double taxation, but also create situations of double-non taxation. This is particularly the case for regimes that have (i) an overly broad definition of the income excluded from taxation, notably foreign source passive income without any conditions or safeguards, and/or (ii) a nexus definition that is non-compliant with the definition of a permanent establishment in the OECD Model Tax Convention.

The COCG has assessed such regimes in the past and has drawn on COCG precedents as the basis of this guidance. Past assessments will not be affected by this guidance. Regimes that have not been reviewed by the COCG can be reviewed on the basis of this guidance and the criteria of the Code of Conduct. The current procedure for reopening past assessments remains valid.

Passive Income

In 2017, the COCG found that a tax system that fully excludes passive income with a foreign link from taxation, without any conditions, is harmful. This is the case even if the profits are determined using internationally established principles, as the end effect is the same as a regime providing beneficial treatment. for low/no substance offshore companies.

Foreign source exemption regimes that are broad enough to include passive income, without any conditions, can result in ring-fencing and a lack of substance. Ring-fencing arises because the receipt of passive income generally requires a transaction with a non-resident. Passive income is generally not coupled with economic substance requirements. The COCG has found that the exemption of passive income without clear conditions (e.g. explicit link to some real activity in the jurisdiction) contravenes the principles of the Code.

Active Income

The COCG agreed that the assessment of foreign source income regimes should focus primarily on the exemption of passive income. However, it also agreed that it was essential to consider specific features of these regimes linked to active income – in particular, whether and how active income is taxed.

In particular, regimes that extend the exemption to active income from foreign operations should also be carefully considered, as this can trigger cases of double non-taxation.

The analysis will therefore focus on the definition of the income deemed to have its source in the jurisdiction, as this will determine whether or not the business income is taxed according to international principles. This analysis will look at whether the jurisdiction applied a definition of Permanent Establishment in line with that of the OECD Model Tax Convention. This is the internationally agreed principle to assess the economic presence of an entity in another jurisdiction, to determine the allocation of the right to tax.

Options for remedying harmful foreign income exemption regimes

Jurisdictions with foreign source income exemptions regimes that are considered harmful should either abolish the regimes in question or amend them to remove the harmful features.

Jurisdictions should either:

- Introduce taxation of passive income; or
- if they exclude from taxation certain types of passive income:
 - o implement adequate substance requirements to the entities concerned, in line with the EU's Code of Conduct (Business Taxation)¹⁸;
 - o have robust anti-abuse rules in place; and
 - o remove any administrative discretion in determining the income to be excluded from taxation.

Furthermore, jurisdictions should ensure the application of international principles in relation to the taxation of active income, notably with regard to the definition of permanent establishment provided by the OECD Model Convention on Double Tax Treaties (including by amending the definition of permanent establishment in a DTA in place already that does not respect international principles) and the consequent income allocation.

¹⁸ Where jurisdictions are being assessed under Criterion 2.1, the substance requirements in the COCG guidance on the interpretation of the third criterion (doc. 10419/18) should apply. Where jurisdictions are being assessed under Criterion 2.2, the substance requirements in the COCG scoping paper on criterion 2.2 (doc. 10421/18) should apply.

As each of these regimes has its own specificities, the COCG agreed that the Commission services should work with the jurisdictions in question to clarify the areas of concern. Solutions should be developed based on the guidelines above, to address the specific issues identified by the COCG for each regime. Accordingly, this Guidance should not be treated as a stand-alone document and should be accompanied by technical advice and interaction with the jurisdictions under review.

Review

The countering of harmful tax measures is an ongoing process. This guidance note will therefore be periodically reviewed by the COCG to ensure that it reflects future developments.
