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OUTCOME OF PROCEEDINGS

From: General Secretariat of the Council
To: Code of Conduct Group (Business Taxation)
Subject: Morocco's Free Trade Zones regime (MA003)
– Final description and assessment

ROLLBACK REVIEW PROCESS (JANUARY 2020)

On 14 December 2019 Morocco published the Finance Law 2020 No 70-19 (see doc. 7426/20 ADD 1-10). That law amends the Free Trade Zones (FTZ) regime (MA003).

The Code of Conduct Group (business taxation) (COCG) meeting of 4 February 2020 assessed the amendments as follows:

	1a	1b	2a	2b	3	4	5
Morocco – Free Trade Zones (renamed "zones d'accélération industrielle")	X	?	X	?	X	X	X

V = harmful

X = not harmful

This conclusion was endorsed by the ECOFIN Council on 18 February 2020.

7426/20 ADD 1-10: Finance Law 2020 No 70-19

7427/20 ADD 1: Framework law No 18-95 of 3 October 1995

Annex 1: Assessment of the MA003 regime in 2017 (standstill)

Explanation

Gateway criterion - Significantly lower level of taxation

“Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code”

Following the adoption of the Finance Law 2020 No 70-19, the Free Trade Zones regime still provides for a lower tax rate than then general rate. Although the rate has been raised from 8,75% to 15%, it is still significantly lower than the 28% rate applied outside the regime.

The regime thus passes the gateway criterion.

Criterion 1 – Targeting non-residents

“whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents”

The FTZ regime has been amended so that it no longer targets activities with foreign entities/markets, as the tax advantages are granted in respect of all transactions (not only on export income).

Therefore, the regime is no longer caught by criterion 1a and cross (“X” – not harmful) is inserted for criterion 1a.

Since there is no information yet on the ‘de facto’ effect of the measure we propose a “?” for criterion 1b.

Criterion 2 – Ring-fencing

“whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base”

By analogy to the assessment against criterion 1a/b the regime is not considered harmful under criterion 2a and has a question mark “?” under criterion 2b.

Criterion 3 - Substance

“whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages”

The measure does not include any express requirement for real economic activity or substantial economic presence. However, the regime does not apply to the independent provision of services. In order for a taxpayer to access the regime, they need to demonstrate the number of employees, added value to be generated and the form of financing the project, among other information, in order to be approved to benefit from the regime. It should also be considered that the beneficiaries of the regime are companies carrying out industrial and manufacturing activities, which de facto have economic substance.

For this reason a cross (“X”) is added for criterion 3.

Criterion 4 – Internationally accepted principles

“whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD”

A tax exemption does not contradict any internationally agreed principle. Therefore a cross (“X”) is added for criterion 4.

Criterion 5 - Transparency

“whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way”

The measure is fully set out and published in the relevant legislation and the practice should not involve any administrative discretion. A cross (“X”) is added for criterion 5.

Overall assessment

“Without prejudice to the respective spheres of competence of the Member States and the Community, this code of conduct, which covers business taxation, concerns those measures which affect, or may affect, in a significant way the location of business activity in the Community”

In light of the assessment made under all COCG criteria the Free Trade Zones regime is overall not harmful.

Grandfathering

Section V.1 “Dispositions transitoires” of the Finance Law 2020 No 17-19 stipulates a grandfathering period of 20 years for existing beneficiaries, in addition to any time remaining on the general 5-year exemption for new companies.

The reason for this is that the taxpayers have been granted the beneficial tax treatment for a fixed time period of 20 years by the Moroccan government. The beneficial tax treatment expires at the latest in 2046 for all entities. According to the Moroccan government, a decision to cut this period short would be considered as a measure of retroactive tax legislation, which would be contrary to Articles 6, 132, 133 and 134 of the Moroccan Constitution. This would be a sufficient basis for taxpayers to open litigation, which would most likely be successful and have serious economic repercussions on the state budget.

The Moroccan authorities have entered into agreements with the companies concerned, on the basis of the previous provisions in the regime. The provisions covering these agreements can be found in Article 23 of Loi-cadre no 18-95 of 3 October 1995 (see doc. 7427/2020 ADD 1).

According to information provided by Morocco, 317 companies currently benefiting from the Free Zones regimes could avail of the above grandfathering. 12 of these companies realise 70% of the total turnover and one of those companies realise on its own 40% of the total turnover. The Moroccan authorities have stated that each year around 20 of these 317 companies will no longer benefit from the regime and move to the generally applicable conditions.

Against this background, Morocco satisfies the conditions to apply an extended grandfathering for the companies that benefitted from the Free Trade Zones regime before 1 January 2020. As such, the grandfathering arrangement for the regime is in line with the COCG requirements.

Assessment of the MA003 regime in 2017 (standstill)**Export Free Zones (EFZ) or Free Trade Zones (FTZ) (MA003)****a. Description**

This regime applies to industrial, commercial and service activities geared towards export and carried on in EFZs or FTZs by residents or non-resident individuals or legal entities. The benefit of EFZ or FTZ regime is granted provided that

- the final product is exported and
- the transfer of merchandise between different EFZs or FTZ follows customs regulations.

Sources: IBFD

b. Preferential features

Profits derived by companies during the first 5 years of activities in EFZs or FTZs are exempt from corporate tax and are subject to corporate tax at the reduced rate of 8,75% for the following 20 years. Dividends and similar income distributed by companies in EFZs or FTZs are exempt from the 15% withholding tax when paid to non-resident individuals or legal entities.

c. Possible concerns

A regime limited to foreign tax payers and/or to operations outside the territory of the jurisdiction does not meet criteria 1 and 2 of the Code of Conduct which forbid this type of ring fencing. The regime applies to companies whose business is geared towards export (the final product must be exported).

d. Assessment

	1a	1b	2a	2b	3	4	5
Morocco – Export Free Zones or Free Trade Zones	V	V	V	V	V	X	X

Gateway criterion - Significantly lower level of taxation:

“Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code”

The normal tax rate is progressive from 10% up to 31%.

Profits derived by companies during the first 5 years of activities in EFZs or FTZs are exempt from corporate tax and are subject to corporate tax at the reduced rate of 8,75% for the following 20 years. Dividends and similar income distributed by companies in EFZs or FTZs are exempt from the 15% withholding tax when paid to non-resident individuals or legal entities.

The measure therefore provides for a significantly lower level of taxation and is potentially harmful under the Code.

Criterion 1 – Targeting non-residents:

“whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents”

The EFZ or FTZ regime seems targeted for activities with foreign entities/markets since tax advantages are granted only in respect of transactions carried out with non-residents (only on export income). Therefore, we consider that the measure is clearly caught by criterion 1a. We therefore propose a tick (“V” - harmful) for criterion 1a. Since the measure is not available for transactions with persons resident in Morocco, we would also propose a tick (“V” - harmful) for criterion 1b.

Criterion 2 – Ring-fencing:

“whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base”

The EFZ or FTZ regime seems targeted at activities with foreign entities/markets since tax advantages are granted only in respect of transactions carried out with non-residents (only on export income). Since the income of non-resident persons are not taxable in Morocco, the advantages are ring-fenced from the domestic market and thus, do not affect the national tax base. By analogy to the assessment against criterion 1a/b we would propose a tick (“V” - harmful) for criterion 2a/2b.

Criterion 3 - Substance:

“whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages”

The measure does not include any express requirement for real economic activity or substantial economic presence. We would therefore propose a tick (“V” - harmful) for criterion 3.

Criterion 4 – Internationally accepted principles:

“whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD”

A tax exemption does not contradict any internationally embraced principle. We would therefore propose a cross (“X”) for criterion 4.”

Criterion 5 - Transparency:

“whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way”

The measure is fully set out and published in the relevant legislation and the practice should not involve any administrative discretion. We would therefore propose a cross (“X”) for criterion 5.

Overall assessment:

“Without prejudice to the respective spheres of competence of the Member States and the Community, this code of conduct, which covers business taxation, concerns those measures which affect, or may affect, in a significant way the location of business activity in the Community”

In light of the assessment made under all Code criteria, the regime should be considered overall harmful from a Code of Conduct point of view.
