GLOBAL TAX SERIES

European Tax Handbook 2025

European Tax Handbook 2025

Why this book?
The 2025 European Tax Handbook includes surveys on 49 countries and jurisdictions. The surveys have been updated to reflect the laws applicable in 2025. A chapter on the European Union (together with the most important tax directives) and descriptions of seven of the most important Swiss cantons are included.

Title:	European Tax Handbook 2025
Date of publication:	May 2025
ISBN:	9789087229757 (print), 9789087229771 (PDF), 9789087229764 (e-pub)
Type of publication:	Book
Number of pages:	1571
Terms:	Shipping fees apply. Shipping information is available on our website.
Price (print/online):	EUR 530 | USD 600 (VAT excl.)
Price (eBook: e-Pub or PDF):	EUR 355 | USD 400 (VAT excl.)

Order information
To order the book, please visit www.ibfd.org/shop/book. You can purchase a copy of the book by means of your credit card, or on the basis of an invoice. Our books encompass a wide variety of topics, and are available in one or more of the following formats:

- IBFD Print books
- IBFD eBooks – downloadable on a variety of electronic devices
- IBFD Online books – accessible online through the IBFD Tax Research Platform

European Tax Handbook 2025

IBFD

Global Tax Series

Editors:
Mery Alvarado
Madalina Cotrut
Francesco De Lillo
Filip Krajcuska
Magdalena Olejnicka
Andreas Perdelwitz
Marnix Schellekens

IBFD

Visitors' address:
Rietlandpark 301
1019 DW Amsterdam
The Netherlands

Postal address:
P.O. Box 20237
1000 HE Amsterdam
The Netherlands

Telephone: 31-20-554 0100
Email: info@ibfd.org
www.ibfd.org

ISBN 978-90-8722-975-7 (print)
ISBN 978-90-8722-976-4 (eBook, ePub); ISBN 978-90-8722-977-1 (eBook, PDF)
ISSN 1872-6747 (print); 2590-1044 (electronic)
NUR 826

Preface

IBFD is pleased to present the *thirty-sixth* edition of the *European Tax Handbook*.

The 2025 *European Tax Handbook* covers surveys on 49 countries and jurisdictions. All information on the European tax systems has been updated to reflect, as much as possible, the laws applicable in 2025.

As before, the *European Tax Handbook* includes in addition to the country level surveys, a chapter on EU Direct Taxation (together with the most important tax directives), as well as descriptions of seven of the most important Swiss cantons, i.e. Basel-Stadt, Bern, Geneva, Schwyz, Vaud, Zug and Zurich.

All the country chapters of this book are also available in the online collection Country Surveys of the IBFD Tax Research Platform, which contains descriptions of the tax systems of 53 European countries and, in addition, descriptions of the tax systems of all 26 Swiss cantons. The online title is *European Tax Explorer (Plus)*. It also includes the texts of income tax treaties concluded by all European countries. The online collection Country Surveys has quarterly updates; the chapters are revised as new information becomes available.

More comprehensive coverage of the majority of the jurisdictions can be found in the online collection Country Analyses. A combination of Country Surveys, Country Analyses and the texts of income tax treaties concluded by countries worldwide is offered via the online title *Global Tax Explorer Plus* and regional subsets of this title on Africa, Asia-Pacific, Europe, Latin America and the Caribbean, and the Middle East. Countries in North America can easily be ordered via the online title *Tax Explorer – Country Select*, which enables you to choose the exact countries for which you need coverage on the essentials on international tax. It also offers the possibility to extend this with the very detailed Country Analyses on major economies like Canada and the United States.

For the latest tax developments, see IBFD's daily *Tax News Service* online. More information about IBFD, its various activities and products is available at www.ibfd.org.

The Editors

April 2025

External contributors:

Ms P. Bak, Netherlands (chapter on Ireland)
Ms K. Balogová, Bratislava (chapter on Slovak Republic)
Mr B. Büchel, Fiscal Authority of the Principality of Liechtenstein, Vaduz (chapter on Liechtenstein)
Mr P. Burg, France (chapters on France, Monaco)
Dr R. Cadosch, Cadosch Rechtsanwälte AG, Bern (chapter on Switzerland)
Mr R. Curtis, United Kingdom (chapter on United Kingdom)
Dr G. Czoboly, Corvinus University and PwC Hungary, Budapest (chapter on Hungary, Individual Taxation)
Ms G. Erdös, Corvinus University, Budapest (chapter on Hungary, Corporate Taxation)
Mr V. Foltea (chapter on Moldova)
Mr E. Furuseth, BI Norwegian Business School, Oslo (chapter on Norway)
Mr M. Herm, ATTELA Law Firm, Tallinn (chapter on Estonia)
Mr M. Kamaladdin oğlu Majidli (chapter on Azerbaijan)
Mr L. Khalatyan, Alias LLC, Yerevan (chapter on Armenia)
Ms T. Kogut, Luxembourg (chapter on Russia)
Mr C. Kypris, Kypris and Associates AE (member of PrimeGlobal), Athens (chapter on Greece, Individual Taxation)
Ms I. van der Maas, Mazars, Amsterdam (chapters on Croatia, North Macedonia)
Mr A. Maher, Cautela Pros d.o.o., Ljubljana (chapter on Slovenia)
Mr S. Melnyk, Alvarez & Marsal, United Kingdom (chapter on Ukraine)
Ms L. Nakasheva, Ms S. Pandelieva and Ms G. Ahtchieva, AFA OOD, Sofia (chapter on Bulgaria)
Mr P. Pace Ross and Ms G. Demanuele Bianco, KPMG Malta (chapter on Malta)
Dr S. Papademetriou and Mr G. Kerameus, KPP Law Firm, Athens (chapter on Greece, Corporate Taxation)
Mr N. Papapanayiotou, Costas Tsielepis & Co Ltd, Cyprus (chapter on Cyprus)
Mr B. Rodriguez, IKEA Supply AG, Basel (chapter on Spain)
Ms Y. Schuchter and Mr A. Kras, Leitner + Leitner, Salzburg (chapter on Austria)
Ms N. Shamugia, ECOVIS Georgia, Tbilisi (chapter on Georgia)
Ms V. Sigurvaldadóttir, Marel hf, Gardabaer (chapter on Iceland)
Mr I. Soldatovic, KPMG Belgrade (chapters on Montenegro, Serbia)
Mr V. Strachuk, Minsk (chapter on Belarus)
Mr M. Teixeira, CS Associados, Lisbon (chapter on Portugal)
Ms A. Uruçi, Boga & Associates, Tirana (chapter on Albania)
Ms T. Vaičiulienė, Vilnius (chapter on Lithuania)
Prof. Dr B. Yaltı, Koç University, Istanbul (chapter on Türkiye)

IBFD country specialists:

Ms M. Alvarado (chapters on Gibraltar, Guernsey, Isle of Man, Jersey)
Ms L. Ambagtsheer-Pakarinen (chapters on Denmark, Finland, Sweden)
Ms G. Gallo (chapter on Italy)
Ms L. Gerzova (chapter on Latvia)
Mr F. Krajcuska (chapter on Czech Republic)
Dr R. Offermanns (chapters on Belgium, Luxembourg)
Ms M. Olejnicka (chapter on Poland)
Mr A. Perdelwitz (chapter on Germany)
Ms O. Popa (chapter on Romania)
Mr M. Schellekens (chapter on Netherlands)
Ms C. Valério and Mr D. Arsenovic (chapter on European Union)

Table of Contents

European Union 9
Appendices:
– Merger Directive 55
– Parent-Subsidiary Directive (recast) 63
– Interest and Royalties Directive 69

Albania 75

Armenia 93

Austria 111

Azerbaijan 153

Belarus 183

Belgium 205

Bulgaria 259

Croatia 287

Cyprus 305

Czech Republic 337

Denmark 363

Estonia 399

Finland 421

France 457

Georgia 505

Germany 527

Gibraltar 561

Greece 581

Guernsey 621

Hungary 639

Iceland 683

Ireland 709

Isle of Man 749

Italy 767

Jersey 805

Latvia 827

Liechtenstein 861

Lithuania 877

Luxembourg 909

Malta 953

Moldova 983

Monaco 1013

Montenegro 1025

Netherlands 1041

North Macedonia 1079

Norway 1095

Poland 1123

Portugal 1155

Romania 1199

Russia 1227

Serbia 1267

Slovak Republic 1285

Slovenia 1317

Spain 1341

Sweden 1381

Switzerland and selected cantons 1413

Türkiye 1457

Ukraine 1493

United Kingdom 1515

European Union

Direct Taxation

Introduction

The European Union comprises the following 27 Member States: Austria, Belgium, Bulgaria, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, the Slovak Republic, Slovenia, Spain and Sweden. The United Kingdom was part of the European Union until 31 January 2020 when the withdrawal process from the European Union was concluded (*see* details below).

Member States, Norway, Iceland and Liechtenstein form the European Economic Area (EEA) from 1 January 1994, by the conclusion of the Agreement of 13 December 1993 on the European Economic Area (94/1). The Agreement covers company law directives, customs and social security legislation and all primary and secondary legislation regarding the Treaty on the Functioning of the European Union (TFEU) treaty freedoms (*see* section 1.1.). The European Union has also concluded several agreements with Switzerland on, inter alia, the free movement of persons as well as the automatic exchange of financial account information, which includes an exemption for cross-border payments of dividends, interest and royalties (Amending Protocol to the European Union-Switzerland Agreement (2015)).

A common currency, the euro, has been introduced in Austria, Belgium, Croatia, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, the Slovak Republic, Slovenia and Spain.

The following is an overview of the most significant of both the adopted and proposed EU regulations and directives covering direct tax. Topical tax developments at EU level are also covered, including Brexit (*see* below), State aid (*see* section 1.6.), implementation of global minimum taxation (Pillar Two) (*see* section 3.5.), taxation of the digitalized economy, including the reallocation of taxing rights (Pillar One) (*see* section 5.1.), the financial transaction tax (*see* section 5.2.) and the windfall tax for energy companies (*see* section 5.3.). Relevant case law of the Court of Justice of the European Union on fundamental freedoms is covered in section 4.

Brexit

Following a referendum held on 23 June 2016 (the so-called Brexit), the United Kingdom voted to leave the European Union and triggered the formal process of leaving the European Union by invoking article 50 of the Treaty on European Union (TEU) on 29 March 2017. The United Kingdom formally withdrew from the European Union at midnight CET on 31 January 2020. From that date until 31 December 2020, the United Kingdom entered into a transition period, regulated under the Withdrawal Agreement, in which the United Kingdom was not represented in EU institutions, agencies, bodies and offices, but EU law still applied under certain conditions (*see* details below).

During the transition period, the European Union and the United Kingdom negotiated the terms of their future partnership in the framework of the political declaration of 17 October 2019. On 30 December 2020, the United Kingdom and the European Union signed a Trade and Cooperation Agreement (TCA) (*see* details below).

The Withdrawal Agreement

The Withdrawal Agreement was concluded on 30 January 2020 by the Council of the European Union (the Council), after the United Kingdom completed the ratification process on 23 January 2020.

The Withdrawal Agreement contains a transitional period during which the European Union treats the United Kingdom as if it were a Member State (with certain procedural exceptions). Such transitional period ended on 31 December 2020.

The most important aspects of the Withdrawal Agreement relating to direct taxation are the following:
– EU social security regulations (*see* section 6.) will remain applicable to EU and UK citizens that, at the end of the transition period, were residents or were subject to the legislation of the United Kingdom or European Union, respectively, as well as to their family members and survivors;
– the Recovery Directive (2010/24) will apply until 5 years after the end of the transition period between Member States and the United Kingdom for, inter alia, claims that relate to amounts that became due or transactions that took place before the end of the transition period;
– for State aid granted before the end of the transition period, for a period of 4 years after the end of the transition period, the European Commission (the Commission) will be competent to initiate new administrative procedures on State aid governed by Council Regulation (EU) 2015/1589 concerning the United Kingdom. The Commission will continue to be competent after the end of the 4-year period for procedures initiated before the end of that period;
– the ECJ remains competent for all judicial procedures (including appeals and referrals) concerning the United Kingdom registered before the end of the transition period, and those procedures should con-

tinue until a final and binding judgment is given in accordance with EU rules;
- within 4 years from the end of the transition period, the ECJ will still have jurisdiction over infringement cases against the United Kingdom concerning breaches of EU law that occurred before the end of 2020;
- within 4 years from the end of the transition period, the United Kingdom may also bring before the ECJ cases of non-compliance with an administrative decision of an EU institution or body taken before the end of the transition period or, for certain procedures identified in the Withdrawal Agreement, after the end of the transition period; and
- ECJ decisions made before the end of the transition period are still binding. Retained EU law should be interpreted by domestic courts in accordance with previous ECJ case law and any retained general principles of EU law.

The Trade and Cooperation Agreement (TCA)

The Trade and Cooperation Agreement (TCA) lays down a free trade agreement, a partnership on citizens' security and a governance framework for regulating the relations between the European Union and the United Kingdom as from 1 January 2021. The TCA was ratified by UK Parliament on 30 December 2020, and, after the consent of the European Parliament on 27 April 2021, by the Council on 29 April 2021 (OJ L 149, 30.4.2021). The TCA, which applied provisionally from 1 January 2021, entered into force on 1 May 2021.

The Agreement covers trade in goods and services as well as other areas in the European Union's interest, such as investment, competition, State aid, tax transparency, air and road transport, energy and sustainability, fisheries, data protection and social security coordination.

As regards direct taxation, the TCA provides for:
- subsidy control provisions replacing the EU State aid rules, which set forth principles that must be respected for the granting of subsidies and that oblige the parties to establish control, transparency and recovery mechanisms;
- a commitment to applying base erosion and profit shifting (BEPS) minimum standards and international standards for the fight against tax avoidance and tax evasion;
- a minimum level of protection based on OECD standards on anti-avoidance (interest limitation, controlled foreign company (CFC) rules and anti-hybrid rules) and tax transparency (exchange of information on financial accounts, cross-border tax rulings, country-by-country (CbC) reports between tax administrations, and potential cross-border planning arrangements); and
- coordination on social security benefits related to sickness, maternity, paternity, invalidity, old-age, survivors, accidents at work and occupational diseases, death grants, unemployment, and pre-retirement benefits. For these benefits, the TCA establishes non-discrimination between Member States and between EU/UK citizens and own nationals; equal treatment of benefits, income, facts and events; aggregation of periods to determine the entitlement to benefits; and exportability of cash benefits (except for disability and unemployment benefits) in the case of individuals moving to a Member State or the United Kingdom.

The European Parliamentary Research Service (EPRS) published a study (The EU-UK Trade and Cooperation Agreement two years on: Unpacking early evidence – European Implementation Assessment) on the implementation of the TCA on 9 August 2023. The study includes details of UK legislation to end the application of retained EU laws within the United Kingdom (and retained EU Law, with the consequence that general principles of EU law cease to form part of UK law. As regards taxation, it mentions the call for scrutiny to ensure that the TCA does not contain loopholes that allow UK Crown Dependencies (Guernsey, Jersey and the Isle of Man) and UK Overseas Territories (which include Anguilla, Bermuda, the British Virgin Islands, Gibraltar and the Turks and Caicos Islands) to be used as counterparts for developing new harmful tax schemes impacting the functioning of the internal market (given that these territories are excluded from the TCA). It also highlights that taxation is one of the areas where no arrangements were made between the European Union and United Kingdom in the context of the TCA, as taxation is not subject to dispute settlement provisions nor to rebalancing measures.

1. General Principles of EU Law and Taxation

EU law enjoys priority over national laws of Member States. There are three sources of EU law:
- primary law (*see* section 1.1.);
- secondary law (*see* section 1.2.); and
- supplementary law (*see* section 1.3.).

1.1. *Primary law*

Primary law is the supreme source of law within the European Union. It consists of the treaties establishing the European Union, namely:
- the Treaty on European Union (TEU) (2007); and
- the Treaty on the Functioning of the European Union (TFEU) (2007).

These two treaties, which became effective in 2009, consist of the EU founding treaties (the Treaty of Paris (1951), the Treaty of Rome (1957) and the Maastricht Treaty (1992)), as amended by subsequent treaties (the Single European Act (1986), the Treaty of Amsterdam (1997), the Treaty of Nice (2001) and the Treaty of Lisbon (2007)). Under the Treaty of Lisbon, the Maastricht Treaty was renamed the Treaty on the European Union and the Treaty of Rome was renamed the TFEU.

These treaties distribute competences between the European Union and Member States, and lay down the powers of the European institutions (i.e. determine the legal framework within which the EU institutions may operate).

Nationals and legal entities of a Member State can rely on the directly applicable provisions of the TEU and the TFEU.

As regards taxation, the TFEU is the most relevant as its main objectives are establishing a functioning internal market, as well as an economic and monetary union. These objectives cannot be reached if, inter alia, the four fundamental freedoms (*see* section 4.) are hindered. As such, any national tax measures that violate these principles must be abolished.

Primary law also includes the accession treaties of new Member States and the Charter of Fundamental Rights of the European Union.

1.2. *Secondary law*

Secondary sources of EU law are legal instruments that are based on the European Union's primary law (i.e. the treaties, *see* section 1.1.). Secondary law can be divided into two categories:
– unilateral acts: this comprises regulations, directives (e.g. the Parent-Subsidiary Directive (2011/96), *see* section 3.1.), decisions, opinions and recommendations, and in some cases other acts such as communications and White and Green papers; and
– conventions and agreements: this includes international agreements, agreements between Member States and agreements between EU institutions.

Regulations are legal instruments of general application and are binding and directly applicable in each Member State.

Directives are binding in respect of the result to be achieved, but – unlike regulations – the manner of their implementation and enforcement is a matter left for the national authorities to determine. In accordance with the ECJ case law stemming from *van Duyn v Home Office* (Case 41-74), a directive is directly enforceable within a Member State only if:
– that Member State fails to (properly) execute the directive by a designated deadline; and
– the provisions of the directive are unconditional and sufficiently clear (theory of *acte clair*).

If these conditions are fulfilled, the provisions of a directive may have a direct effect, and may be invoked before a court, including those provisions which grant rights to companies and individuals, against Member States.

Decisions are binding upon those to whom they are addressed, and are directly applicable. Recommendations and opinions are not binding.

1.3. *Supplementary law*

These sources of EU law, which are not specifically mentioned in the treaties, comprise ECJ case law, international law and general principles of law.

The decisions of the ECJ are official, legally binding interpretations of EU law. The interpretation of EU law by the ECJ plays a major role in the absence of harmonization in the field of direct taxation. In this regard, the interpretation of the four fundamental freedoms (i.e. the free movement of goods, the free movement of persons (including the free movement of EU citizens, the free movement of workers and the freedom of establishment), the freedom to provide services and the free movement of capital and payments) and the interpretation of State aid rules, both regulated under the TFEU, have resulted in an extensive body of case law aimed at preventing cases of discrimination against cross-border activities of companies and distortions in the internal market (*see* section 4.).

Fundamental rights, as guaranteed by the Convention for the Protection of Human Rights and Fundamental Freedoms, as well as those that result from the constitutional traditions common to Member States, are recognized as general principles of EU law.

1.4. *European Union's (shared) competence to legislate on direct tax matters*

According to article 4(2)(a) of the TFEU, the European Union shares competence with the Member States in certain areas such as the internal market – which encompasses taxation. It is a shared competence with pre-emption, which means that if the European Union exercises the shared competence in a certain area, the Member States lose the competence to do so or contradict what was regulated by the European Union in that area. For example, as the European Union has laid down rules against tax avoidance by taxpayers that are subject to corporate tax through the ATAD, the Member States are prevented to legislate against the standards established therein.

In the area of direct taxation, Member States maintain broad sovereignty rights. The recurring legal basis for the Union to legislate on direct tax matters is article 115 of the TFEU, which establishes a special legislative procedure (consultation procedure) for the approximation of legislation that directly affects the establishment or functioning of the internal market. Such procedure requires unanimity among Member States for the adoption of such acts by the Council of the European Union (*see* section 1.4.) and consultation of the European Parliament and the European Economic and Social Committee.

Even when the European Union has not exercised its competence to legislate, Member States must nevertheless exercise their taxing powers consistently with EU law (*see* section 1.1.) and, in particular, with State aid rules (*see* section 1.6.) and the fundamental freedoms (*see* section 4.).

1.5. *Decision-making with regard to tax policy*

Currently, taxation is one of the few policy areas where decision-making requires unanimity among Member States.

Examples of difficulty in achieving unanimity in tax policies, e.g. the attempt to introduce a common consolidated corporate tax base (CCCTB) or a digital services tax (*see* section 5.1.), have opened the discussion on alternative decision-making mechanisms in the area of taxation.

The EU treaties provide for possibilities such as:
– the "enhanced cooperation" procedure, foreseen in article 20 of the TEU and articles 326 to 334 of the TFEU, which can be initiated where the Council fails to secure the necessary level of agreement, but a

group of nine or more Member States submit a request to the Commission indicating they want to undertake action in the relevant area. If the Commission agrees, it may submit a proposal to the Council, which has the power to authorize Member States to proceed with the enhanced cooperation after obtaining the consent of the European Parliament. The acts adopted within this framework only apply to participating Member States. Enhanced cooperation will generally only come into play when the discussions have halted, but significant agreement exists between a substantial number of Member States on the type of rules that they would like to see introduced. However, this mechanism is seen as a last resort since it still results in fragmentation within the single market;

– the use of general *passerelle* clauses under article 48(7) of the TEU. The clause provided in the first subparagraph allows for the shift from unanimity to qualified majority voting. The second subparagraph allows shifting from a special legislative procedure – such as the consultation procedure under article 115 of the TFEU, typically followed for direct tax proposals – to the ordinary legislative procedure. The activation of any of the general *passerelle* clauses require a unanimous decision by the European Council, after obtaining the consent of the European Parliament. Moreover, any Member State's national parliament may oppose the decision, which in essence constitutes a veto, preventing its adoption; and
– article 116 of the TFEU, which can be used if the differences between Member States legislation cause distortions of competition in the internal market, which cannot be removed in concertation with Member States. This provision allows for a qualified majority voting under the ordinary legislative procedure, but its use is limited by strict conditions. Consequently, this provision is not the adequate legal basis for tax law initiatives addressing general tax policy issues. It could, however, be used for initiatives targeting aggressive tax planning, tax avoidance and tax evasion that are liable to affect the functioning of the single market.

Within the options available under the treaties, the Commission proposed a gradual shift to qualified majority voting (QMV) (COM(2019) 8 final of 15 January 2019). In particular, the Commission suggested that QMV be initially introduced for measures designed to improve cooperation and mutual assistance between Member States in fighting tax fraud and evasion, as well as for administrative initiatives which would benefit EU businesses (e.g. harmonized reporting obligations) and those in which taxation supports other policy goals (e.g. fighting climate change, protecting the environment or improving public health). The Council could subsequently consider extending the QMV (from 2025) to measures designed to modernize already harmonized EU rules (e.g. VAT and excise duty rules), or to major tax projects such as the above-mentioned CCCTB and a new system for the taxation of the digital economy.

On 9 June 2022, the European Parliament adopted a resolution proposing the abolition of unanimity in the Council (2022/2705(RSP)). On 11 July 2023, it proposed the use of the *passerelle* clauses while EU Treaties are not amended (2022/2142(INI)).

According to the programme of the Spanish Presidency of the Council for the second semester of 2023, the Spanish presidency had planned to advance the debate on *passerelle* clauses to extend the use of qualified majority voting on essential EU policies, such as taxation. However, no relevant progress was achieved on this point. In this regard, the European Parliament reiterated its call to amend the EU treaties in a resolution adopted on 22 November 2023, by which it sent a proposal to the Council and the Commission, as well as to the parliaments and governments of the Member States (2022/2051(INL)).

On 20 March 2024, the Commission adopted a communication on pre-enlargement reforms and policy reviews (COM(2024) 146 final), stressing the increased challenges in achieving unanimous decisions in the context of an enlarged European Union. The Commission notes how the autonomous use of *passerelle* clauses has been unsuccessful in tackling current limitations – as its activation itself requires a unanimous decision from the Council of the European Union or the European Council – and proposes its activation in combination with "appropriate and proportionate safeguards" to accommodate "strategic national interests".

1.6. *Harmful tax competition and forbidden State aid*

Tax measures introduced by Member States are subject to State aid rules regulated under the TFEU. Any aid granted by a Member State or through State resources that distorts competition and trade within the European Union by favouring certain companies or the production of certain goods is incompatible with the internal market. Furthermore, Member States must notify the Commission of all new aid measures, and wait for the Commission's decision before they put the measure into effect (*see State Aid procedures* below). Aid granted without the Commission's prior authorization constitutes unlawful State aid.

In some circumstances, government interventions are necessary for a well-functioning economy. Accordingly, the TFEU, in article 107(2) and (3), also leaves room for some policy objectives for which State aid can be given that is considered compatible with the internal market. Examples of such aid include financial compensation for the damages caused by natural disasters or exceptional occurrences or to remedy a serious disturbance in the economy of a Member State. In this regard, the Commission adopted the State aid Temporary Framework to enable Member States to grant several types of aid, including (selective) tax advantages to mitigate the adverse effects of the COVID-19 pandemic. For instance, Member States could decide to take measures, such as implementing wage subsidies and suspending payments of corporate and value added taxes or social contributions. The Framework was amended seven times and was in place until, at the latest, 31 December 2023. Similarly, the Commission adopted a State aid Temporary Crisis Framework to enable Member States to support the economy in the context of Russia's invasion of Ukraine until 31 December 2022 (OJ C 131I/1, 24.3.2022), which was extended until 30 June 2024.

In other instances, State aid plans are moving towards a longer-term basis. The European Commission adopted the Temporary Crisis and Transition Framework (OJ C 101/3, 17.03.2023, amended by OJ C C/2023/1188, 21.11.2023 and OJ C C/2024/3113, 2.5.2024) to support measures in key sectors for the transition to a net-zero economy, in line with the Green Deal Industrial Plan. The new Temporary Crisis and Transition Framework, in addition to amending and prolonging in part the State aid Temporary Crisis Framework related to Russia's invasion of Ukraine (until 30 June 2024 in general, but until 31 December 2024 for agriculture, fishery and aquaculture sectors), also introduced other measures to accelerate investments in key sectors for the transition towards a net-zero economy (until 31 December 2025).

Another example of State aid which can be considered compatible with the internal market is the framework for research, development and innovation (RDI Framework), which sets out the rules under which Member States can grant State aid to companies for RDI activities, while ensuring a level playing field (C(2022) 7388 final). Under the RDI Framework, Member States can provide aid for R&D projects, feasibility studies, construction of research facilities and testing and experimentation infrastructures and innovation activities. Member States must notify this type of aid to the Commission.

In addition, the Commission has issued many regulations, notices, frameworks, guidelines and communications in respect of State aid.

State aid rules only apply to measures that meet all of the following criteria:
– there is a transfer of state resources;
– an economic advantage is conferred on a firm;
– the measure is selective or specific; and
– the measure affects competition and trade.

With effect from July 2023, the European Commission is also able to investigate subsidies granted by non-EU public authorities to companies operating in the European Union under the Foreign Subsidies Regulation (2022/2560). To support its implementation, the European Commission adopted rules establishing certain practical aspects of the proceedings (Implementing Regulation (EU) 2023/1441) and issued non-binding clarifications on the application of articles 4(1), 6 and 27(1) (SWD(2024) 201 final).

Transfer of state resources

In order to qualify as State aid, the advantage must be granted:
– by a Member State;
– through Member State resources (including national, regional and local bodies; and public institutions (such as banks and foundations)) – *see Germany v. Commission*, Case C-248/84, (1987) ECR 4013; or
– by private or public intermediate bodies appointed by a Member State.

Transfer of state resources can take many forms, including fiscal expenditures (e.g. grants and subsidies or state capital investments), a loss of tax revenues (e.g. via accelerated depreciation allowances or reduced tax rates) or otherwise (e.g. loan guarantees; provisions of a legislative, regulatory or administrative nature; or the practices of tax authorities).

Economic advantage conferred on a firm

The (tax) measure should give the recipient an economic advantage that they would not have received in the normal course of business. The advantage may be provided through a reduction in the undertaking's tax burden in several ways, including:
– a reduction in the tax base (e.g. special deductions or accelerated depreciation);
– a partial or total reduction in the amount of tax (e.g. tax exemptions or tax credits); and
– deferment, cancellation or rescheduling of tax debt.

Examples of economic advantages can be:
– an undertaking buys or rents publicly owned land for less than the fair market price;
– an undertaking is granted a loan by a private party (bank) with a state guarantee;
– an undertaking is selling products, services or assets to a Member State for a price exceeding the fair market price;
– an undertaking receives capital injections from a Member State under conditions that are not at arm's length;
– an undertaking receives public services at fees that are not at arm's length; or
– an undertaking receives a tax payment deferral not based on the applicable domestic law.

A measure does not constitute unlawful State aid in cases where a Member State makes funds available to an undertaking under the same terms and conditions that would be provided in the normal course of events by a private investor applying ordinary commercial criteria (the so-called Market Economy Operator Principle) (Case C-278/92, *Spain v. Commission*, [1994] ECR I-4103).

Selectivity or specificity

The aid measure must be specific or selective in that it favours certain undertakings, thereby affecting the balance between certain undertakings and their competitors, or the production of certain goods.

Tax measures that are open to all undertakings in a Member State are in principle "general measures", and do therefore not constitute State aid. To qualify as such, general measures must be effectively open to all undertakings on an equal-access basis, and they may not in effect be reduced in scope through, for example, a discretionary power (that goes beyond the simple management of tax revenue) of the Member State to grant them or via other factors that restrict their practical applicability – *see France v. Commission (Kimberly Clark Sopalin)* (C-241/94).

The criterion of "selectivity" is also met if the relevant measure only applies to part of the Member State's territory, as is the case for regional, local and sectorial measures. In the same way, measures that only favour:
– national products which are exported – *see* Joint Cases 6/69 and 11/69 *Commission v. France* [1969] ECR 561;

- sectors that are subject to international competition;
- an entire sector of the economy;
- undertakings with special (legal) status (e.g. public versus private undertakings); or
- undertakings with a specific function (e.g. holding and/or finance functions),

may constitute State aid.

Nevertheless, Member States may still choose the economic and tax policy they consider most appropriate and spread the tax burden across different industry sectors in a way they feel is most beneficial (intersectoral measures). If they apply without distinction to all undertakings and to the production of all goods and services, the following measures are examples of measures that do not constitute State aid:

- tax measures of a pure technical nature (e.g. tax rates, depreciation rules, deferment schedules, tax exemptions and tax credits, and use of losses regulations); and
- measures pursuing general economic policy objectives through a reduction of the tax burden related to certain production costs (e.g. in respect of R&D, employment, and investments in environment).

Effect on competition and trade

State aid must have a potential effect on the competition and trade between Member States. It is sufficient in this respect if it can be shown that the recipient undertaking carries on an economic activity and that this undertaking operates in a market in which there is trade between Member States.

In the opinion of the Commission, small amounts of aid (*de minimis* aid) do not affect competition and trade.

From 1 January 2024, the ceiling for aid covered by the *de minimis* rule is, in general, EUR 300,000 in a 3-year period – *see* Commission Regulation (EU) 2023/2831 of 13 December 2023.

State aid procedures

After receiving a notification or information concerning alleged unlawful aid, the Commission may start a preliminary investigation to determine if:

- the measure is not aid under EU law (and so it may be implemented);
- the measure constitutes aid that is compatible with EU law; or
- there are serious doubts as to the compatibility of the notified measure with EU State aid rules.

If the Commission has serious doubts (or faces procedural difficulties in obtaining relevant information) about the compatibility of a Member State's aid with EU State aid rules, it must open a formal in-depth investigation under article 108(2) of the TFEU.

The decision to initiate this procedure is then sent to the relevant Member State. This decision contains a summary of the factual and legal bases for the investigation, and includes a preliminary assessment of the measure's compatibility with EU State aid rules. The Member State concerned has the opportunity to respond to this decision.

At the end of the formal investigation, the Commission adopts a final decision. There is, however, no legal time frame within which the in-depth investigation must be completed. The possible outcomes of the investigation are: (i) a positive decision (there is no aid or the aid is compatible); (ii) a conditional decision (the aid is in principle compatible, but implementation must fulfil conditions stated in the decision); or (iii) a negative decision (aid is incompatible and cannot be implemented).

If a negative decision is related to aid that has already been paid out, the Member State must recover that aid (with interest) from the beneficiary (unless such recovery would be contrary to EU law). In this way, the undue advantage granted to a beneficiary is reversed. The Commission then opens a "recovery" case to enforce the implementation of its decision – *see* Commission Notice on the recovery of unlawful and incompatible State aid C/2019/5396, OJ C 247, 23.7.2019.

As regards taxation, incompatible State aid may, however, exist in the following situations (Commission Notice C/2016/2946):

- a preferential treatment of undertakings for collective investments;
- rulings misapplying domestic tax law – available only for certain companies – or providing a more favourable tax treatment compared to other taxpayers which are in a similar factual and legal situation (tax rulings);
- tax settlements that disproportionately reduce the tax due without a clear justification;
- depreciation incentives for certain types of assets or undertakings, if they are not based on the guiding principles for the depreciation rules; and
- reduced excise duties.

Some of the more notable procedures and decisions (many of which concern tax rulings) regarding State aid include *UK CFC Group Financing Exemption* (Case SA.44896 – T-363/19 and T-456/19; Joined Cases C-555/22 P, C-556/22 P and C-564/22 P), *Gibraltar corporate income tax regime* (Case SA.34914 (2013/C) – T-37/23), *IKEA* (Case SA.46470), *Nike* (Case SA.51284 – T-648/19), *McDonald's* (Case SA.38945), *Amazon* (Case SA.38944 – T816/17 and T318/18; C-457/21 P), *Starbucks* (Case SA.38374 – T-760/15), *Apple* (Case SA.38373 – C-465/20 P) and *FIAT* (Case SA.38375 – T-755/15 and T-759/15; C-885/19 P). For details on the decisions covering TP issues, *see* section 7.

2. Harmonization of Company Law

Company Law is partially harmonized in the European Union. A large part of the harmonized legislation was codified under Directive 2017/1132 relating to certain aspects of company law. This directive covers issues such as formation, capital and disclosure requirements, and operations (such as mergers and divisions) of companies. Directive 2017/1132 was amended by:

- Directive 2019/1151 as regards the use of digital tools and processes in company law;
- Directive 2019/2121 on cross-border conversions, divisions and mergers; and
- Directive 2019/1023 on restructuring and insolvency, to allow Member States to allow exceptions

from certain articles of Directive 2017/1132, when this is necessary to establish preventive restructuring frameworks.

The European Parliament and the Council are currently negotiating a further amendment to the Directive, to expand and upgrade the use of digital tools and processes in company law (COM(2023) 177 final).

EU company law also regulates corporate governance issues, notably under Directive 2007/36, as amended, on the exercise of certain rights of shareholders in listed companies. It abolishes the main obstacles to a cross-border vote in listed companies that have their registered office in a Member State and establishes certain rights for shareholders.

Additionally, there are several types of legal entities that can be formed under European law, coexisting with national ones. Specifically, these are:
– the European company (*Societas Europaea*, SE) (*see* section 2.1.);
– the European economic interest grouping (EEIG) (*see* section 2.2.); and
– the European cooperative society (*Societas cooperativa Europaea*, SCE) (*see* section 2.3.).

Additionally, the European Commission has proposed new rules to establish a new legal form of non-profit associations specifically designed for cross-border purposes, the European cross-border association (ECBA) (COM(2023) 516 final). To become effective, the proposal needs to be adopted by European Parliament and the Council. Once adopted, Member States will have 2 years to transpose the Directive into national law.

2.1. *European company*

Under Council Regulation 2157/2001/EC of 8 October 2001 (SE Regulation), effective from 8 October 2004, it is possible to form an SE. The SE is intended to facilitate cooperation within the European Union and the cross-border reorganization of companies within the EEA across the frontiers of Member States. The SE Regulation applies not only to Member States, but also to EEA states. The name of an SE must be preceded or followed by the abbreviation SE.

Under the SE Regulation, an SE can be established by a merger, by the formation of a holding company or by the creation of a joint subsidiary. The minimum share capital is EUR 120,000. The SE Regulation does not contain provisions concerning groups of companies.

An SE is resident in the Member State of its real seat, which is not necessarily the Member State of its statutory seat.

For tax purposes, SEs are treated the same as public limited liability companies that are formed under the national laws of a Member State. Losses of an SE's foreign permanent establishment can be offset against the SE's profits. If, however, such a permanent establishment becomes profitable later, those profits may be taxed in the Member State of the SE up to the amount of losses previously deducted. The SE Regulation does not contain any provisions on the tax treatment of losses suffered by subsidiaries.

2.2. *European economic interest grouping*

Under Council Regulation (EEC) 2137/85 of 25 July 1985, fully effective from 1 July 1989, it is possible to form a European economic interest grouping (EEIG).

The purpose of an EEIG is to facilitate or develop the cross-border economic activities within the European Union of its members, and to improve or increase the results of these activities.

An EEIG may not be formed for the purpose of making profits for itself. In the event that an EEIG earns profits as an ancillary result of its activities, the taxation system applicable to such profits is comparable to that commonly applied to partnerships; the EEIG itself is not to be taxed, but its profits may be taxed in the hands of its members.

2.3. *European cooperative society*

Under Council Regulation (EC) 1435/2003 of 22 July 2003, effective from 18 August 2006, it is possible to form a European cooperative society (SCE). Like SEs (*see* section 2.1.), SCEs may be established in EU Member States, Iceland, Liechtenstein and Norway (i.e. in the EEA).

An SCE has legal personality (with subscribed capital divided into shares), and must have members from (at least) two different Member States. The amount of capital or number of members is variable.

Each Member State must treat an SCE as a cooperative formed in accordance with the laws of the Member State where its registered office is located.

For tax purposes, an SCE is treated the same as a cooperative society that is formed under the national laws of a Member State.

3. Harmonization of Corporate Taxation

There are six directives that seek to harmonize certain tax provisions in the field of direct taxation among different Member States. These are:
– the Parent-Subsidiary Directive (2011/96) – which aims to, inter alia, eliminate tax obstacles to cross-border distributions of intra-group profits (*see* section 3.1.);
– the Interest and Royalties Directive (2003/49) – which aims to eliminate withholding taxes on cross-border interest and royalty payments between related companies (*see* section 3.2.);
– the Merger Directive (2009/133) – which aims to eliminate tax hurdles to cross-border corporate reorganizations (*see* section 3.3.);
– the Anti-Tax Avoidance Directive (2016/1164) (ATAD) and the Amending Directive to the 2016 Anti-Tax Avoidance Directive (2017/952) (ATAD2) – which contain anti-abuse measures against common forms of aggressive tax planning (*see* section 3.4.);
– the Minimum Taxation Directive (2022/2523) – which introduces a minimum-level taxation for large groups in the European Union (*see* section 3.5.); and

- the Directive on Faster and Safer Relief of Excess Withholding Taxes (2025/50) (FASTER) – which provides for the relief of excess withheld tax and the issuance of a digital tax residence certificate (*see* section 3.6.).

In addition, there are several proposed directives, such as:
- a directive to tackle the misuse of shell companies (ATAD 3 – *see* section 3.7.1.);
- a directive introducing an allowance on equity (*see* section 3.7.2.);
- a directive to develop a common corporate tax framework in the internal market (BEFIT), which replaced the CCCTB proposal (*see* section 3.7.3.); and
- directives to tax the digitalized economy (*see* section 5.1.).

3.1. *Parent-Subsidiary Directive*

A directive aimed at reducing the differences between taxation rules for nationally organized groups of companies and taxation rules for EU-wide groups was adopted by the Council on 23 July 1990 (90/435) – the Parent-Subsidiary Directive (90/435). This directive had two purposes:
- to ensure that the Member State of the parent company either refrains from taxing the profits distributed by a subsidiary that is resident in another Member State or, if taxing such profits, authorizes the parent company to deduct from the amount of tax due the corporate income tax paid by the subsidiary in the other Member State; and
- to exempt from withholding tax profit distributions by the subsidiary to the parent company.

The implementation deadline of the directive for Member States was 1 January 1992.

The Parent-Subsidiary Directive (90/435) was amended by Amending Directive to the Parent Subsidiary Directive (2003/123), which extended its application to cases in which profit distributions by subsidiaries in one Member State are received by permanent establishments of companies situated in another Member State.

In the interest of clarity, a recast version of the directive and its successive amendments was adopted on 30 November 2011, Parent-Subsidiary Directive (2011/96) (the Directive). The recast version repealed the previous versions of the Directive, and entered into force on 20 December 2011. The implementation deadline for Member States was 1 January 2012.

Scope

The Directive applies to the following distributions:
- distributions of profits received by a parent company in one Member State from a subsidiary in another Member State;
- distributions of profits by a subsidiary in one Member State to its parent company in another Member State;
- distributions of profits, received by a permanent establishment situated in one Member State, of a company established in another Member State, which are made by a subsidiary established in a Member State other than the Member State where the permanent establishment is situated; and
- distributions of profits by a company of a Member State to a permanent establishment situated in another Member State of a company of the same Member State as the company making the distribution.

Definition of "company of a Member State"

The Directive defines "company of a Member State" as any company that:
- takes one of the *forms* listed in Part A of Annex I to the Directive;
- is considered to be a *resident* of a Member State for tax purposes according to the national laws of that Member State, and is not considered to be a resident for tax purposes outside the European Union under the terms of a tax treaty with a non-EU Member State; and
- is *subject* to one of the taxes listed in Part B of Annex I to the Directive, or to any other tax that may be substituted for any of the expressly mentioned taxes, without the possibility of an option or of being exempt.

All of the three above-mentioned criteria must be cumulatively met.

Dual resident companies can still qualify for the Directive where, generally, taxing rights remain in a Member State, specifically:
- a company incorporated under the laws of a Member State but having its effective place of management and control in another Member State;
- a company incorporated (and fully taxable) under the laws of a Member State but having its effective place of management and control in a state outside the European Union (and therefore being fully taxable in that state) while no tax treaty has been concluded between these two states;
- a company incorporated (and fully taxable) under the laws of a state outside the European Union but having its effective place of management and control in a Member State (and therefore being fully taxable in that Member State) while no tax treaty is concluded between these two states; and
- a company incorporated (and fully taxable) under the laws of a Member State but having its effective place of management outside the European Union, where between these two states a tax treaty is concluded that allocates the taxing rights to the Member State.

Private and public companies limited by shares, as well as SEs (*see* section 2.1.) and cooperatives (*see* section 2.3.) are under the scope of the application of the Directive. Otherwise, it is left to each Member State to decide which entity forms are covered. Some Member States expressly included in Part A of Annex I to the Directive an exhaustive list of all national entity forms covered. Other Member States have not included an express list of all possible national entity forms in the Annex, but they have determined broadly that all national company forms incorporated under the law of the State concerned fall under the scope of the Directive, provided that the other two criteria set forth are met.

Qualifying shareholding

A qualifying parent-subsidiary relationship exists if the parent company holds at least 10% of the issued shares of the subsidiary. Member States are allowed to replace, by means of bilateral agreement, this criterion by that of a holding of voting rights. Additionally, Member States are also permitted to require a minimum holding period not exceeding 2 years, but they are not allowed to require that the minimum holding period has already come to an end at the time when the profit distribution is made – *see Denkavit I* (Case C-283/94). Member States are free to define procedures under their own national law to assure that the 2-year holding period is met.

Tax treatment

When a parent company (or permanent establishment thereof) receives distributed profits from a qualifying subsidiary established in another Member State, the Member State of that parent (or permanent establishment) must either:
– not tax such distributions (i.e. exempt them); or
– relieve any economic double taxation by way of a(n) (indirect) credit for the fraction of the corporation tax paid by the qualifying subsidiary – or any qualifying lower-tier subsidiary – in relation to the profits distributed.

Member States may consider part of the distributed income as "management costs relating to the holding", and not exempt that part from taxation. Where these costs are fixed as a flat rate, the fixed amount may not exceed 5% of the profits distributed by the subsidiary. France, Germany, Italy, Slovenia and Spain have fixed these (management) costs at 5% of the dividends received. As a consequence, these countries in fact only exempt 95% of the dividends received.

The Member State of the parent company may also refuse the deduction of a subsidiary's losses (from the taxable profits of the parent company) resulting from the distribution of the subsidiary's profits.

These possibilities may be exercised only in accordance with the EU fundamental freedoms and within the limits of the Directive. In particular, Member States may not generally deny the deductibility of costs related to a holding in another Member State until the profits from the shareholding are taxable – *see Bosal* (Case C-168/01). Likewise, Member States may not deny the deductibility of the interest paid by a parent company when such interest does not relate to the financing of the holding – *see Argenta Spaarbank NV* (Case C-39/16). Member States cannot impose the liability to make an advance payment which exceeds the 5% threshold on a parent entity when redistributing profits received by its subsidiaries to its shareholders (even if such profits have not been subject to corporate income tax at the regular corporate income tax rate) – *see Schneider Electric and Others* (Case C-556/20).

In addition, under the Amending Protocol to the European Union-Switzerland Agreement (2015), dividends paid by subsidiaries to parent companies, whereby one is established in the European Union and the other in Switzerland, are exempt if the parent company maintains a direct minimum holding of 25% for at least 2 years in the subsidiary (paying) company.

Anti-abuse

The Parent-Subsidiary Directive (2011/96) has been amended by two directives to address double non-taxation concerns and abuse.

Directive 2014/86

On 8 July 2015, the Council adopted Amending Directive to the 2011 Parent-Subsidiary Directive (2014/86) to prevent double non-taxation through the use of hybrid financing arrangements. Member States had to implement this directive by 31 December 2015 at the latest.

Under the amending directive, Member States must refrain from taxing qualifying profit distributions to the extent they are not deductible by the subsidiary.

This anti-hybrid rule aims to prevent groups of companies from structuring their intra-group payments, through the use of hybrid instruments, to realize mismatches and double non-taxation outcomes. Such mismatch might occur if the Member State of the borrower qualifies a payment as debt, while the Member State of the parent company qualifies the payment as equity. As a result, the amount paid (qualifying as interest) would be deductible in the first Member State and not taxable in the other (qualifying as dividend). The anti-hybrid rule prevents this effect.

Directive 2015/121

On 27 January 2015, the Council adopted the Amending Directive to the 2011 Parent-Subsidiary Directive (2015/121), which introduced a general anti-abuse provision (GAAR) into the Parent-Subsidiary Directive (2011/96). Member States had to implement this directive by 31 December 2015 at the latest.

Under the GAAR, Member States shall not grant the benefits of the Parent-Subsidiary Directive (2011/96) to an arrangement (or series of arrangements) which (i) has been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the Directive (the subjective test or the main purpose test); and (ii) is not genuine, having regard to all relevant facts and circumstances (the objective test).

The subjective test is not met if the tax advantage of the structure is not derived from the Directive (e.g. avoidance of withholding tax on dividends) or no tax advantage is gained at all. The wording of the main purpose test is largely consistent with the principal purpose test set out in Action 6 of the BEPS Action Plan, which denies treaty benefits if the structure that is set up has tax avoidance as one of its main purposes.

An arrangement (or series thereof) is "not genuine" to the extent that it is not put into place for valid commercial reasons which reflect economic reality. In order to be treated as genuine, the company invoking the Directive should have sufficient substance (e.g. it conducts a material business enterprise).

Application of the GAAR requires an individual examination of the whole operation at issue. The competent authorities may not, therefore, confine themselves to applying predetermined general criteria. The imposition of a general tax measure that automatically excludes certain categories of taxable persons from the tax advantage without the tax authorities having to provide evidence of fraud and abuse, would go further than what is necessary for preventing fraud and abuse. For example, the mere fact that a company residing in a Member State is directly or indirectly controlled by residents of third states does not, in itself, indicate the existence of abuse – *see Deister and Juhler* (Joined Cases C-504/16 and C-613/16) and *Eqiom and Enka* (Case C-6/16).

Nevertheless, the tax authorities may consider some situations as indications of abuse. For example, abuse may be present if dividends received are passed on wholly or partially shortly after they are received (even where no legal obligation to pass on such dividends exists), the recipient lacks substance, or the recipient is interposed to obtain the benefits of the Parent-Subsidiary Directive (2011/96). Accordingly, domestic safe harbours (e.g. a minimum level of substance in order for a structure not to qualify as abuse) may not hold – *see T-Danmark* (Cases C-116/16 and C-117/16).

Member States must deny treaty benefits if an arrangement constitutes abuse of rights, even if the Member State has not implemented any specific anti-avoidance legislation in its domestic law. This requirement flows from the general EU anti-abuse principle – *see Z-Denmark v. Skatteministeriet* (C-299/16) and *T-Danmark* (C-116/16 and C-117/16).

The GAAR does not preclude the application of domestic or agreement-based provisions required for the prevention of tax evasion, tax fraud or abuse.

3.2. *Interest and Royalties Directive*

Scope

On 3 June 2003, the Council adopted Interest and Royalties Directive (2003/49) to eliminate withholding taxes on interest and royalty payments between related companies of different Member States (the Directive). The implementation deadline for Member States was 1 January 2004.

Definition of "company of a Member State"

The Directive defines "company of a Member State" as any company that:

- takes one of the *forms* listed in the Annex to the Directive;
- is considered to be a *resident* of a Member State for tax purposes according to the national laws of that Member State, and is not considered to be a resident for tax purposes outside the European Union under the terms of a tax treaty with a non-EU Member State; and
- is *subject* to one of the taxes listed in article 3(a) of the Directive, or to any other tax that may be substituted for any of the expressly mentioned taxes, without the possibility of an option or of being exempt. Based on the wording of the article, only the (recipient) company seems to be required to be subject to tax, without the interest or royalty income being effectively subject to tax in the Member State of residence. However, the ECJ noted in *N Luxembourg 1* (Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16) that to the extent that the interest received by an entity (in this case by Luxembourg resident SICAR) is exempt from profits tax in Luxembourg, this entity does not qualify as a "company of a Member State".

All of the three above-mentioned criteria must be cumulatively met.

Qualifying shareholding

As mentioned above, the Directive applies to interest and royalty payments between related companies. Companies are "related" if:

- one company has a direct holding of at least 25% of the capital of the other company (or vice versa). Member States can opt to replace the minimum shareholding requirement with that of a minimum holding of voting rights; or
- a third company has a direct holding of at least 25% of the capital of each of the two companies. The third company (holding at least 25% of the capital of two qualifying companies) does not seem to be required to be a resident of a Member State.

A Member State may decide not to apply the Directive if the 25% shareholding requirement has not been maintained for at least 2 years.

Moreover, before applying the Directive, the Member State in which the payment arises may request that an attestation be submitted stating that the requirements set out in the Directive are met (e.g. the 25% shareholding, residence of the recipient, beneficial ownership). Inability to provide such attestation may lead to the relevant Member State refusing to apply the Directive. The attestation must be valid for at least 1 year, but no more than 3 years.

If both the payer and the recipient are residents of the same Member State, the Directive does not apply.

Tax treatment

Under the Directive, interest or royalty payments that arise in a Member State are exempt from any taxes imposed on such payments in that State if the beneficial owner of the interest or royalties is a related company of another Member State (or a permanent establishment thereof).

The beneficial owner is not a formally identified recipient, but rather the entity that economically benefits from, and has the freedom to use and enjoy, the interest and/or royalties. In this regard, the OECD Model Tax Convention on Income and on Capital: Commentary on Articles 11 and 12 is relevant for interpreting the term "beneficial owner" – *see N Luxembourg 1* (Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16).

A permanent establishment can be considered the beneficial owner of the interest and/or royalties provided two requirements are met:

- the receivable, the right, or the use of information in respect of which the interest and/or royalties are

received can be allocated to this permanent establishment (because they are instrumental in the business carried on by the permanent establishment based on the internationally accepted allocation rules); and
– the interest and/or royalties are subject to a profit tax in the country where the permanent establishment is located. The Directive does not prescribe a minimum level of taxation in the Member State where the permanent establishment is located.

The Directive aims to eliminate double taxation in the source Member State at the level of the recipient of the interest and/or royalties and therefore only eliminates legal double taxation. Member States may, accordingly, limit the deductibility of the payment from the debtor's tax base – *see Scheuten Solar Technology* (Case C-397/09).

In relation to Switzerland, under the Amending Protocol to the European Union-Switzerland Agreement (2015), Member States must exempt interest and royalty payments to companies resident in Switzerland, and vice versa, under essentially the same conditions as those laid down in the Interest and Royalties Directive (2003/49).

Anti-abuse

The Interest and Royalties Directive (2003/49) does not preclude the application of domestic or agreement-based provisions that aim to prevent fraud or abuse. Where the principal motive or one of the principal motives of the transaction is tax evasion, tax avoidance or abuse; Member States can withdraw or refuse application of the Directive. The terms "evasion", "avoidance" and "abuse" are not defined in the Directive.

Application of this rule requires an individual examination of the whole operation at issue. The competent authorities may not, therefore, confine themselves to applying predetermined general criteria – *see Deister* and *Juhler* (Joined Cases C-504/16 and C-613/16) and *Eqiom and Enka* (Case C-6/16).

Nevertheless, the tax authorities can consider some situations as indications of abuse. For example, abuse may be present if the interest and/or royalties received is passed on wholly or partially shortly after it is received (even where no legal obligation to pass on such interest and/or royalties exists), the recipient lacks substance, or the recipient is interposed solely to obtain the benefits of the Directive. Accordingly, domestic safe harbours (e.g. a minimum level of substance in order for a structure not to qualify as abuse) may not hold.

The general principle of EU law, according to which EU law cannot be relied on for abusive or fraudulent purposes, requires that the taxpayer be refused the benefits under the Directive and fundamental freedoms, even where no domestic or agreement-based provisions exist upon which such a refusal may be based. Proof of abuse requires a combination of objective and subjective elements – *see N Luxembourg 1* (Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16).

3.3. *Merger Directive*

The Merger Directive (2009/133) (the Directive), which constitutes a codified version of the previous Merger Directive (90/434) and its amendments, aims to facilitate cross-border reorganizations within the European Union. The Directive provides for the deferral of the taxation on unrealized capital gains on certain cross-border reorganizations. Such transactions should not cause immediate direct tax consequences (i.e. corporation taxes, income taxes and capital gains taxes) to the participating companies and their shareholders. The related taxation is deferred up to the moment in which such assets are retransferred.

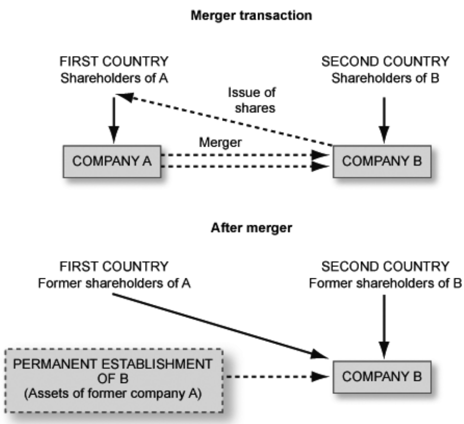
The objective of Merger Directive (90/434) is to facilitate cross-border mergers, divisions and similar transactions between companies established in Member States. The implementation of Merger Directive (90/434) enables groups of companies to reorganize their activities into the most appropriate structure for operating within the European Union without incurring the tax costs which would otherwise generally apply to such transactions.

Scope

The Directive covers the following five types of corporate reorganizations:
– *Mergers* in which one or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to another existing or new company. In exchange, the shareholders of the transferor companies receive shares in the capital of the transferee company and, if applicable, a related cash payment not exceeding 10% of the nominal value of those shares. This also includes the situation where a wholly owned subsidiary transfers all its assets and liabilities to the parent company.

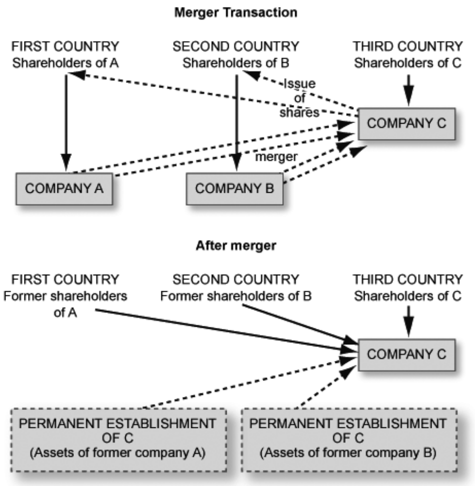
First alternative

One or more companies are merged into another already existing company.



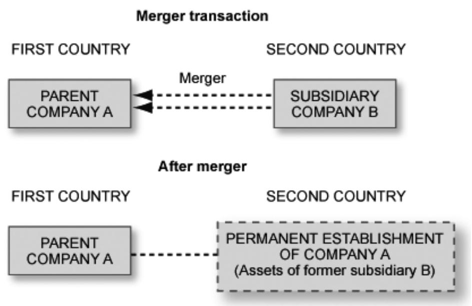
Second alternative

Two or more companies are merged into another new company.

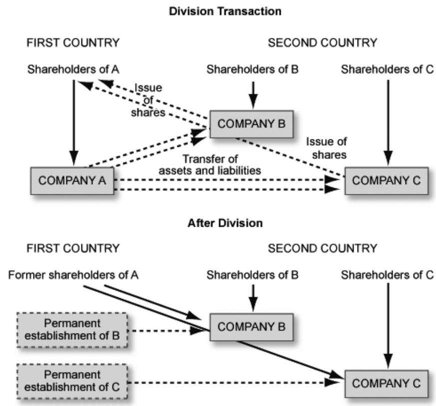


Third alternative

A company transfers all of its assets and liabilities to its parent company which owns 100% of the shares.

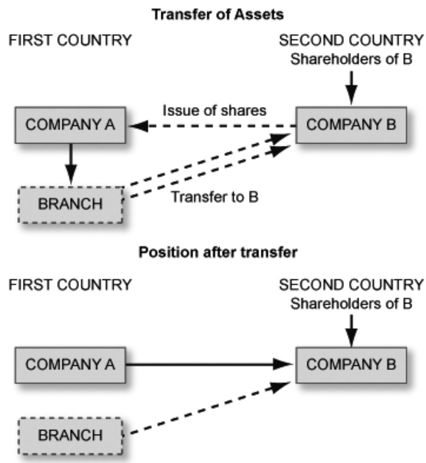


– *Divisions* of companies in which a company, on being dissolved without going into liquidation, transfers assets and liabilities to two or more existing or new companies. In exchange, the shareholders of the transferor company receive shares in the capital of the transferee companies and, if applicable, a related cash payment not exceeding 10% of the nominal value of those shares.

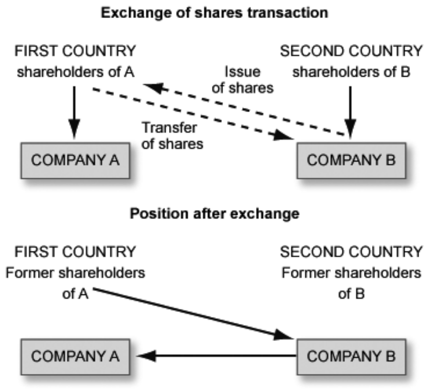


– *Partial divisions* in which a company, without being dissolved, transfers one (or more) branches of activity to one (or more) existing or new companies, and at least one branch of activity remains with the transferring company. In exchange, the transferring company receives securities and possibly a cash payment of up to 10% of the nominal value or, in the absence of a nominal value, of the accounting par value of those securities. This cash payment has practical reasons, as computing an exact amount of shares to be exchanged for other shares can be difficult.

– *Transfers of assets* in which there is a transfer of one or more branches of a company's activities to another company in exchange for shares in the capital of the transferee company.



– *Exchanges of shares* in which a company acquires a holding in the capital of another company such that it obtains the majority of the voting rights in that company. The Directive also covers a transaction whereby a company already holding such a majority, acquires a further holding. The acquiring company issues to the shareholders of the acquired company securities that represent the capital of the acquiring company in exchange for their securities. As with mergers and divisions, a cash payment of up to 10% of the nominal value or, if there is no nominal value, of the accounting par value of the securities issued may be included in the transaction.



The Directive also applies to split-offs and to the conversion of branches to subsidiaries.

Branch of activity

A branch of activity is defined as all the assets and liabilities of a division of a company which from an organizational point of view constitute an independent business, i.e. an entity capable of functioning by its own means.

The independent operation of the transferred business must be determined primarily from a functional and only secondarily from a financial point of view. The assets transferred must be capable of operating as an independent undertaking without requiring additional investment. The fact that a company receiving a transfer takes out a bank loan under normal market conditions cannot in itself mean that the transferred business is not independent, even if the loan is guaranteed by its shareholders. However, if the financial situation of the receiving company as a whole would inevitably point to the conclusion that it would not be able to survive by its own means, the transferred business might not be regarded as independent. Such assessment as to whether or not a business is independent must be left to the national court, having regard to the particular circumstances of each case – *see Andersen og Jensen* (Case C-43/00).

As emphasized by the ECJ, the Directive does not grant EU Member States the discretion to introduce conditions beyond the ones outlined in the directive itself. Accordingly, the Merger Directive precludes legislation of an EU Member State that makes the benefit of tax neutrality in case of a partial division subject to conditions (in the case at hand, e.g. reductions in the shareholding or share capital) that are not specified in the Directive (*see GE Infrastructure Hungary Holding* (Case C-318/22)).

Definition of "company of a Member State"

For the purposes of the Directive, "company of a Member State" means a company meeting the following three requirements:

- The company takes one of the company forms listed in the Annex to the Directive for the country in which it is established.
- The company must be resident in a Member State under the tax laws of that Member State. However, a company does not qualify if, on the basis of a tax treaty with a third (i.e. non-EU) state, the company results in being resident of that third state. Dual resident companies are excluded from the scope of the Directive to prevent such treaties from being used to avoid ultimate tax liabilities within Member States. For example, without this provision, assets might be transferred under a merger transaction to a receiving company such that the taxation otherwise arising on capital gains relating to the assets transferred is deferred in accordance with the reliefs under the Directive. When, however, the receiving company finally disposes of the assets transferred to it (at which stage the gains on which taxation has been deferred would normally be brought into charge to tax), a tax treaty may prevent the Member State of the receiving company from taxing the gains on the grounds that (i) the receiving company is resident in a country outside of the European Union under the terms of a tax treaty; and (ii) the treaty reserves the right to tax such gains to that non-EU Member State.
- The company must be subject to one of the taxes listed in the Annex to the Directive, without the option of being exempt.

The Directive also applies to SEs (*see* section 2.1.), cooperatives, mutual companies, certain non-capital-based companies, savings banks, funds and associations engaged in a business.

Tax treatment

The Directive provides that capital gains (i.e. the differences between the "real values" of the assets and liabilities transferred and their values for tax purposes) arising in relation to the transfer of assets and liabilities in a merger, division or transfer of assets are not subject to tax. The term "value for tax purposes" is defined as the value on the basis of which any gain or loss would have been computed for tax purposes in the transferring company if the assets or liabilities had been independently sold at the time of the transaction. Taxation is deferred up to the moment when a subsequent transfer of the assets takes place.

The scope of the reliefs available under the Directive is, however, limited to assets and liabilities of the transferring company which become effectively connected with a permanent establishment of the receiving company in the Member State of the transferring company and play a part in generating the profits or losses taken into account for tax purposes of that receiving company. As such, the existing book values of the transferred assets and liabilities are maintained by the permanent establishment of the receiving company in the Member State of the transferring company. A future realization of a capital gain upon the alienation of assets and/or liabilities for which in the past tax deferral was granted, will constitute taxable income of the permanent establishment in the Member State that granted the tax deferral. The purpose of these restrictions is to ensure that the Member State of the transferring company retains the assets and liabilities within its taxing jurisdiction even though no tax has been charged on the transfer to the receiving company. In this way, the financial interests of the Member State of the transferring company are safeguarded.

A further prerequisite for the tax deferral is that the receiving company continues the depreciation method and computation method for any gains and/or losses with respect to the assets and liabilities transferred, as used by the transferring company. Consequently, if under the tax laws of a Member State the receiving company may opt for a step-up in basis, relief does not apply to the assets and liabilities for which such option is exercised.

The Directive also addresses the situation where the transferring company in a merger, division or transfer of assets has provisions or reserves on its balance sheet that are partly or wholly exempt from tax. Without a specific relief, a merger, division or transfer of assets would often create a tax charge in respect of tax-exempt reserves and provisions present in the transferring company. The Directive therefore imposes a requirement on Member States to provide relief from such taxation. The relief takes the form of a deferral of taxation rather than a permanent relief in that the provisions or reserves may only be carried over with the same tax exemption by a permanent establishment of the receiving company situated in the Member State of the transferring company. The receiving company is furthermore required to assume the rights and obligations of the transferring company. Accordingly, the Member State of the transferring company will have a future opportunity to tax the receiving company in respect of the reserves or provisions if and when they are released.

If the domestic tax laws of a Member State provide – in pure domestic mergers, divisions and asset transfers – for the possibility of carrying over the tax losses not yet exhausted from the transferring company to the receiving company, such carry-over of losses should also be extended to the equivalent transactions under the Directive. Consequently, in that instance, the Member State of the transferor company would have to permit the permanent establishment of the transferee company to carry forward prior losses of that same business.

However, Member States may restrict the transfer of losses if the disappearing company is a resident of another Member State while allowing the transfer of losses between domestic companies, to the extent that the losses are not “final”. In this sense, Member States must give the domestic receiving company the possibility to show that the disappeared, transferring company of the other Member State has exhausted all possibilities to use these losses itself, and that no other company can use these losses in the future – *see Veronsaajien oikeudenvalvontayksikkö and Valtiovarainministeriö v. Oy A* (C-123/11). As such, the receiving company should be allowed to deduct the losses of the transferring company only if it can demonstrate that it is impossible to use the losses in the disappearing company’s jurisdiction in future years. In this respect, it is not sufficient – nor decisive – that such losses cannot be transferred upon a merger, as there can be other ways that these losses may be offset against future profits in the transferring jurisdiction (e.g. through a sale of the transferring entity to a third party) – *see Memira Holding AB v. Skatteverket* (C-607/17).

The Directive provides for relief from the taxation that would otherwise arise to the shareholders of the transferor company on the exchange of shares arising in connection with a merger, division or an exchange of shares. However, the relief is provided by means of a “rollover” so that the taxation of such gains is deferred until the shares acquired are disposed of.

A cash payment, however, may be taxed in the hands of the shareholders even if the payment does not exceed the 10% maximum, provided the shareholder attributes to the securities received a higher value for tax purposes than the value the securities exchanged had immediately before the merger, division or exchange of shares.

Gains earned by the transferee company upon the cancellation of a substantial participation, held by the transferee company in the capital of the transferor company prior to the reorganization, are not taxed under the provisions of the Directive.

If the Commission’s BEFIT proposal (*see* section 3.7.3.) was to be adopted, the tax treatment of the Merger Directive would also be applicable. In case of a reorganization in the context of the Merger Directive, the BEFIT group member that disposes of the assets and liabilities will exclude any resulting gain or loss from the computation of its preliminary tax result and the BEFIT group member that acquires the assets and liabilities will determine its preliminary tax result, in that fiscal year and the following fiscal years, by using the value for tax purposes, as it stands at the time of the transfer and as it is defined under article 4 of the Merger Directive.

Anti-abuse

The Directive allows Member States to deny the benefits of the Directive where the reorganization has as its principal objective, or as one of its principal objectives, tax evasion or tax avoidance. The fact that a transaction is not carried out for valid commercial reasons may constitute a presumption that the transaction has tax evasion or avoidance as one of its principal objectives.

Due to the general nature of this anti-abuse clause, many Member States have introduced additional anti-abuse provisions in their domestic laws. As Member States hold different views on what is abusive, this has led to referrals to the ECJ, which was asked to decide whether such additional domestic conditions are in line with the Directive.

General rules that automatically exclude certain categories of operations from the benefits of the Directive on the basis of general criteria – e.g. the acquiring company does not carry on business by itself; the same person wholly owns all companies involved; or there is no joining of businesses – irrespective of whether tax evasion or tax avoidance takes place, go further than necessary for preventing tax evasion or tax avoidance and undermine the aim pursued by the Directive. None of these criteria can be considered decisive on their own – *see Leur-Bloem* (Case C-28/95).

Where the motive for a transaction is solely tax based, the benefits of the Directive may not be obtained, as "a valid commercial reason" is a concept involving more than the attainment of a purely fiscal advantage – *see Leur-Bloem* (Case C-28/95). In addition, if more objectives are involved, tax objectives may not be predominant. In this context, a valid commercial reason is not present where the cost savings resulting from restructurings and rationalizations are marginal compared to the level of tax benefits (e.g. the use of tax losses incurred by the merged company) – *see Foggia* (Case C-126/10).

However, it is not abusive under EU legislation to structure the transaction in the most tax-beneficial way if sound commercial reasons are available – *see Eurowings* (Case C-294/97).

Nevertheless, the benefits of the Directive may not be denied if the main purpose of a merger is the avoidance of a tax that is not covered by the Directive. In this sense, the anti-abuse rule does not cover transactions which, although primarily undertaken for tax purposes, aim at avoiding a tax that does not fall within the scope of the Directive – *see Zwijnenburg v. Staatssecretaris van Financiën* (Case C-352/08).

Cross-border reorganizations may lead to cases of double taxation where one Member State considers a transaction legitimate (therefore allowing the transaction to take place based on book values), while another Member State considers the same transaction abusive (as a result of which a deferral of tax is not granted). Under such circumstances, the applicable tax treaty (if any) or the Arbitration Convention (90/436) may oblige the Member States concerned to avoid the double taxation.

3.4. *Anti-Tax Avoidance Directive*

On 21 July 2016, the Anti-Tax Avoidance Directive (2016/1164) (ATAD) was adopted. This directive, which applies to all taxpayers subject to corporate income tax (including permanent establishments in Member States of companies based in third countries), contains anti-avoidance rules such as (i) a limitation on the deduction of interest expense; (ii) exit taxes; (iii) a general anti-abuse rule; (iv) controlled foreign company (CFC) rules; and (v) hybrid mismatch rules.

The ATAD was amended by Amending Directive to the 2016 Anti-Tax Avoidance Directive (2017/952) (ATAD 2) – adopted by the Council on 29 May 2017 – to address hybrid mismatches involving third countries. Member States had to implement ATAD 2 by 31 December 2018, which was extended to 31 December 2019 for the implementation of the exit tax provisions and hybrid mismatches, and to 31 December 2021 for reverse hybrid mismatches.

By 1 January 2023, almost all Member States had implemented the ATAD's rules, except for some countries that already had similar provisions in place under their domestic law deemed equally effective as the ATAD's rules. The hybrid mismatch rules of ATAD 2 have been implemented by all Member States.

On 19 August 2020, the Commission adopted the first report on the implementation of the ATAD, which included an overview of the implementation of the interest limitation, and general anti-abuse and CFC rules across Member States (COM(2020) 383 final). In July 2024, the Commission launched a call for evidence to evaluate the implementation of the ATAD. This new evaluation aims to gather views from stakeholders on the implementation of ATAD in the Member States; the functioning of ATAD, in particular, the assessment of the effectiveness of the measures as a minimum standard to address aggressive tax planning; and ATAD's continued relevance in light of the Minimum Taxation Directive (2022/2523). The adoption of the evaluation report is planned for the third quarter of 2025.

3.4.1. Interest limitation rules

Interest limitation rules, under which net borrowing costs in a taxable period, are only deductible up to the higher of (i) 30% of the taxpayer's earnings before, interest, tax, depreciation and amortization (EBITDA); or (ii) EUR 3 million. Member States can allow a full deduction of interest expenses for standalone entities.

The net borrowing costs are equal to the interest expenses, economically equivalent costs and costs incurred for the raising of finance less taxable interest income and economically equivalent income.

Member States may allow companies belonging to a consolidated group for financial accounting purposes to calculate their deductible expenses using group ratios. Accordingly, companies showing that their equity over asset ratio is equal to or higher than the equivalent group ratio may also fully deduct the interest. This is deemed to be the case if the equity over asset ratio is not more than 2% lower than the equivalent ratio of the worldwide group and all assets and liabilities are valued using the same method.

Alternatively, Member States may allow a higher deduction calculated in two steps. First, the group ratio must be determined by dividing the excess borrowing costs towards third parties by the group EBITDA. Thereafter, the group ratio must be multiplied with the EBITDA of the company concerned.

With respect to non-deductible interests, Member States may introduce carry-forward and carry-back possibilities for an unlimited period or a maximum of 3 years, respectively. With respect to unused interest capacity, Member States can also opt to implement a carry-forward provision for a maximum of 5 years.

Member States may exclude financial undertakings from the scope of these rules, even where such financial undertakings are part of a consolidated group for financial accounting purposes. Excess interest expenses incurred on loans which were concluded before 17 June 2016 and loans used to fund certain long-term public infrastructure projects can also be excluded.

Member States that had sufficient special target rules could postpone the implementation of the interest limitation rule until 1 January 2024.

3.4.2. Exit taxes

The exit tax rules cover certain cross-border transfers of assets or residence of companies to EU or non-EU countries. The following transactions are taxed:

- transfer of assets from the head office to a permanent establishment located in another Member State or in a third country to the extent that the Member State of the head office no longer has the right to tax the transferred assets;
- transfer of assets from a permanent establishment in a Member State to its head office or another permanent establishment located in another Member State or third country;
- transfer of the tax residence of a company to another Member State or third country, unless the assets remain connected with a permanent establishment in the Member State of origin; and
- transfer of the business carried out in a permanent establishment to another Member State.

In the aforementioned cases, the difference between the fair market value of the assets and the tax value is taxed.

Besides immediate taxation, Member States must also provide for the possibility to defer the payment to five instalments in the event of transfers to Member States or third countries that belong to the EEA and that concluded an agreement equivalent to the Recovery Directive (2010/24). Interest may be charged on deferred exit tax and the deferral may be subject to guarantee arrangements in the case of demonstrable and actual risk of non-recovery to ensure proper tax collection. The deferral of payment can be immediately discontinued and the tax debt can become recoverable under certain circumstances (e.g. transfers to third countries or bankruptcy of the taxpayer).

Certain temporal transfers of assets are excluded from these provisions (e.g. assets related to the financing of securities, collaterals, capital requirements or liquidity management).

A step-up rule is introduced for certain taxable transactions between Member States. Accordingly, Member States must accept the exit value established by the Member State of origin unless the exit value does not reflect the market value under certain circumstances.

3.4.3. General anti-abuse rule (GAAR)

Under the GAAR, non-genuine arrangements or series thereof with the main purpose or one of the main purposes of obtaining a tax advantage which is against the object or purpose of the applicable law are ignored for the purposes of determining the corporate tax liability.

Arrangements or series thereof are regarded as non-genuine to the extent that they are not based on valid commercial reasons, which reflect economic reality.

3.4.4. Controlled foreign company rules

CFC legislation applies to entities or permanent establishments that meet the following conditions:

- taxpayers holding alone or together with associated enterprises a direct or indirect participation of more than 50% of the voting rights or capital or that are entitled to more than 50% of the profits of that entity; and
- the entity or permanent establishment is subject to an effective tax rate of less than 50% of the effective tax rate that would have been charged in the Member State of the taxpayer.

The non-distributed income of a CFC must be included in the taxable income of a taxpayer. Member States may opt between the following approaches:

- inclusion of interest; dividends; income from the disposal of shares; royalties; income from financial leasing; income from banking, insurance and other financial activities; and income from invoicing associated enterprises as regards goods and services where there is no or little economic value added. In EEA situations the income does not have to be included: (i) if the CFC carries on substantive economic activities supported by staff, equipment, assets and premises; (ii) if the income of the CFC consists for one third or less of the specific types of listed income; or (iii) for financial undertakings (under conditions). This rule may be extended to third countries; or
- inclusion of non-distributed income arising from non-genuine arrangements put in place mainly to obtain a tax advantage. The included income is limited to the income attributable to the significant people functions carried out by the controlling company. Member States may introduce exceptions for CFC entities or permanent establishments with accounting profits not exceeding EUR 750,000 and non-trading income not exceeding EUR 75,000 or with accounting profits not exceeding 10% of their operating costs for the taxable period.

The income to be included under the CFC rules must be calculated in accordance with the rules of the Member State where the taxpayer resides. Double taxation relief is granted through a credit for the underlying corporate tax paid by the CFC and, in the case of profit distributions and disposals of the participation in the CFC, through the deduction of the income previously included in the tax base as CFC income from the taxpayer’s taxable income.

3.4.5. Hybrid mismatches

The goal of the provisions on hybrid mismatches is to neutralize the effects of arrangements that exploit differences in the tax treatment of an entity or instrument under the laws of two or more jurisdictions.

Under the ATAD (as amended by ATAD 2), hybrid mismatches concern situations in which an entity or transaction is treated differently – for tax purposes – under the laws of two Member States (or of a third country), and this difference results in:

- a double deduction of the same payment, expense or loss; or
- a deduction of a payment without the inclusion of the corresponding income for tax purposes in the payee jurisdiction.

The hybrid mismatches covered by the ATAD are related to entities, financial instruments and permanent establishments. Specifically, the ATAD covers hybrid mismatches resulting from (i) payments under a financial instrument; (ii) payments to a hybrid entity, permanent establishment or a disregarded permanent establishment; (iii) payments made by a hybrid entity to its owners; (iv) deemed payments between the head office and permanent establishment or between two or more permanent establishments; and (v) payments made by a hybrid entity or a permanent establishment. Additionally, the ATAD includes specific rules for dealing with dual residence mismatches, hybrid transfers, imported mismatches and reverse hybrid mismatches.

The personal scope of application of the provisions is restricted to payments between associated enterprises, between permanent establishments and their head offices and payments made under structured arrangements.

The ATAD establishes primary and secondary rules under which mismatches are neutralized by one Member State. For example, when the mismatch results in a double deduction, the Member State of the investor must deny the deduction. Failing this, the deduction must be denied in the Member State of the payor jurisdiction.

3.4.6. Impact on investment funds

The impact of the ATAD on investment funds may be limited. In particular, the ATAD contains an option for Member States to exclude financial undertakings from application of certain anti-avoidance rules to prevent that, amongst others, investment banks are adversely impacted. Specifically, the interest limitation rule and the CFC rules do not apply to financial undertakings.

For banks, there is an exception to the hybrid mismatch provisions for financial instruments. Until 31 December 2022, Member States could exclude certain financial instruments (from banks) from this regime. These included so-called “contingent convertibles” (CoCos), which are a mixture of equity and debt and are widely used by banks to meet Basel III capital requirements. However, this exception did not give Member States a carte blanche: point 17 of the preamble to ATAD 2 states that the scheme is without prejudice to the rules on State aid.

The reverse hybrid rule does not apply to collective investment vehicles with a diversified securities portfolio that are subject to financial supervision. Qualifying investment vehicles for the exception are (i) those referred to in article 1 of the UCITS Directive (2009/65); and (ii) alternative investment funds referred to in article 4(1)(k) of the Alternative Investment Fund Managers Directive (2011/61), as well as Regulations (EC) 1060/2009 and (EU) 1095/2010. Such collective investment undertakings will therefore not be affected by the reverse hybrid measure. However, this does not mean that the other hybrid mismatch provisions do not apply to such investment funds.

3.5. *Minimum Taxation Directive*

The Minimum Taxation Directive (2022/2523) was adopted on 14 December 2022 to implement the OECD Pillar Two Global Anti-Base Erosion (GloBE) rules. The Minimum Taxation Directive was published in the Official Journal of the European Union on 22 December 2022 (ST/8778/2022/INIT, OJ L328 (2022)). On the same date, the European Commission published a non-binding document with an Frequently Asked Questions on Pillar Two Directive.

The Minimum Taxation Directive aims to ensure that large groups in the European Union pay a minimum tax rate in every jurisdiction in which they operate. It provides for a minimum effective tax rate of 15% for domestic and international groups with a consolidated group revenue of more than EUR 750 million a year during two of the last four tax periods, and with either a parent company or a subsidiary situated in an EU Member State. If the group is not taxed at such a minimum effective rate on a jurisdictional basis, a top-up tax is triggered to reach the 15% minimum effective tax rate.

Calculation of the top-up tax

Where the effective tax rate (ETR) for the entities in a particular jurisdiction is below 15%, the group must pay a top-up tax to bring its rate up to 15%. The ETR is calculated as the ratio of the aggregate amount of covered taxes paid in a jurisdiction to the aggregate amount of qualifying income in each jurisdiction. The amount of qualifying income is based on consolidated accounting results, as a starting point, with specific GloBE adjustments (e.g. exclusion of dividends from certain portfolios, timing differences, exclusion of shipping income).

In the application of a substance-based carve-out, the calculation of qualifying income is reduced by an amount equal to 5% of the value of tangible assets and 5% of payroll that the group employs in the jurisdiction (with a 10-year transitory regime with increased carve-out percentages).

The amount of covered taxes does not include indirect taxes, payroll and property taxes. It is calculated from the accounting tax expense with specific GloBE adjustments.

Allocation rules of the top-up tax

The Minimum Taxation Directive provides two rules for allocating the top-up tax:

– an income inclusion rule (IIR) in accordance with which a parent entity of a multinational enterprise (MNE) group or of a large-scale domestic group computes and pays its allocable share of top-up tax in respect of the low-taxed constituent entities of the group; and
– an undertaxed profit rule (UTPR) in accordance with which a constituent entity of an MNE group has an additional cash tax expense equal to its share of top-up tax that was not charged under the IIR in respect of the low-taxed constituent entities of the group. The allocation of tax under the UTPR is based on the number of employees and tangible assets in the relevant jurisdiction.

Taxpayers

The directive establishes the following types of taxpayers based on a top-down approach:

– Ultimate parent entities, which are located in the European Union, incur the primary obligation to apply the IIR to their allocable share of top-up tax relating to all low-taxed constituent entities of the MNE group, whether they are located in or outside the European Union. In the case of domestic groups, the ultimate parent entity must apply the IIR to the entire amount of top-up tax.

– Intermediate parent entities located in the European Union must apply the IIR up to their allocable share of the top-up tax when the ultimate parent entity is an excluded entity or is located in a third-country jurisdiction that has not implemented the OECD Model rules or equivalent rules.
– Partially owned parent entities located in the European Union that are more than 20% owned by interest holders outside the group are obliged to apply the IIR up to their allocable share of the top-up tax, regardless of whether the ultimate parent entity is located in a jurisdiction that has a qualified IIR (unless they are wholly owned by another partially owned parent entity which is required to apply the IIR).
– Other entities located in the European Union must apply the UTPR to any residual amount of top-up tax that has not been subject to the IIR and the top-up tax corresponding to the ultimate parent entity which is located in low-taxed jurisdictions.

Special rules apply for restructuring transactions and the transfer of assets. CFC rules and distribution regimes are also specifically treated.

Qualified domestic top-up tax (QDMTT)

The directive allows EU Member States to exercise the option to apply a domestic top-up tax to low-taxed domestic subsidiaries. This option will allow the top-up tax due by the subsidiaries of the multinational group to be charged locally, within the respective Member State, and not at the level of the parent entity.

Exclusions

A transitory exemption applies for MNE groups that are at the initial phase of their international activity for a period of 5 years, provided that the MNE group does not have constituent entities in more than six jurisdictions and the value of all assets of the group located outside the Member State does not exceed EUR 50 million. Domestic groups can also be excluded for a transitional period of 5 years under the same conditions.

The rules also provide for an exclusion of minimal amounts of income to reduce the compliance burden. According to the *de minimis* exclusion, no top-up tax will be charged when average revenues are less than EUR 10 million and an average qualifying income (or loss) is less than EUR 1 million in a jurisdiction.

Additionally, Member States in which very few groups are headquartered (i.e. less than 12 ultimate parent entities of groups within the scope of this directive are located in the jurisdiction) have the option to not apply the IIR and the UTPR for 6 years. Estonia, Latvia, Lithuania, Malta and the Slovak Republic have communicated their intention to delay the application of the IIR and UTPR for 6 consecutive fiscal years, beginning from 31 December 2023 (PUB/2023/1760, OJ C C/2023/1536).

Transposition deadlines

Member States had to bring into force the laws, regulations and administrative provisions necessary to transpose the directive by 31 December 2023, with the exception of the UTPR for which the transposition deadline is 31 December 2024.

In January 2024, the European Commission sent letters of formal notice to Estonia, Greece, Spain, Cyprus, Latvia, Lithuania, Malta, Poland and Portugal for failure to communicate national measures transposing the Directive. The infringement procedure was taken to the second stage on 23 May 2024, with reasoned opinions addressed to Spain, Cyprus, Latvia, Lithuania, Poland and Portugal. Later, on 3 October 2024, the Commission decided to refer Cyprus, Poland, Portugal and Spain to the ECJ.

By 4 October July 2024, most Member States had, fully or partially, transposed the Directive, whereas Cyprus, Poland, Portugal and Spain had not enacted implementing legislation.

Importance of OECD works

In the recitals, the directive refers to the OECD Model rules and the explanations and examples in the Tax Challenges Arising from the Digitalisation of the Economy – Commentary to the Global Anti-Base Erosion Model Rules (Pillar Two) released by the OECD/G20 Inclusive Framework on BEPS, as well as the GloBE Implementation Framework, including its safe harbour rules, as a source of illustration or interpretation in order to ensure consistency in application across Member States of the Minimum Taxation Directive. The recitals of a Directive are not legally binding.

The OECD continues working on the implementation package. On 15 December 2022, the Inclusive Framework on BEPS agreed on a transitional safe harbour based on the CbC reporting information to exclude operations in lower-taxed jurisdictions provided that in the jurisdiction (i) the *de minimis* exclusion applies; (ii) the ETR (calculated on a simplified basis) is at least 15% (16% for 2025 and 17% for 2026); or (iii) the pre-tax profit is less than the amount resulting from the substance-based exclusion. A transitional penalty relief regime, which requires careful consideration by tax authorities for applying penalties or sanctions where an MNE has taken reasonable measures to ensure the correct application of the GloBE rules, was also approved. Both sets of rules were published in the document Safe Harbours and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two). Together with this publication, the OECD launched a public consultation on the GloBE Information Return and dispute prevention and resolution mechanisms (Tax certainty for the GloBE rules).

On 1 February 2023, Administrative Guidance on the model rules was approved by the OECD Inclusive Framework on BEPS. Along with new details on the standardized GloBE Information Return, a second set of Administrative Guidance was published on 17 July 2023 to cover, among other things, safe harbours for states designing QDMTTs and a transitional UTPR safe harbour. A third set of Administrative Guidance was published on 18 December 2023, notably clarifying the application of the GloBE rules and issuing further guidance on the transitional CbCR Safe Harbour Rules and on the allocation of blended CFC taxes. On 25 April 2024, the OECD published the Consolidated Commentary to the Global Anti-Base Erosion Model Rules, which includes the Administrative Guidance released until date. An updated version of the Examples illustrating the application of the Model Rules was also published on the same date.

On 17 June 2024, a fourth set of Administrative Guidance concerning the application of the recapture rule applicable to deferred tax liabilities, cross-border allocation of current and deferred taxes, and rules applicable to flow-through entities and securitization vehicles was published.

Jurisdictions facing a specific issue of interpretation or application of the GloBE rules may refer it to the Inclusive Framework on BEPS for clarification. It is, therefore, expected during the recurring release of Administrative Guidance.

3.6. *FASTER (Faster and Safer Tax Excess Relief)*

Legislative procedure and transposition deadline

The European Commission adopted a proposal of a Council Directive on a new EU system for the avoidance of double taxation and prevention of tax abuse in the field of withholding taxes on 19 June 2023 (COM(2023) 324 final). This system is known as FASTER (Faster and Safer Tax Excess Relief).

On 14 May 2024, EU Member States reached a political agreement on a compromise text presented by the Belgian presidency (9786/24), which guaranteed additional flexibility in the implementation of the Directive.

The European Parliament adopted a first opinion on the Commission's proposal during the plenary session of 28 February 2024 (P9_TA(2024)0102). However, considering the substantial differences between the Commission's proposal and the presidency compromise text, the European Parliament was reconsulted. On 14 November 2024, the European Parliament confirmed its support of the Council's draft (P10_TA(2024)0033).

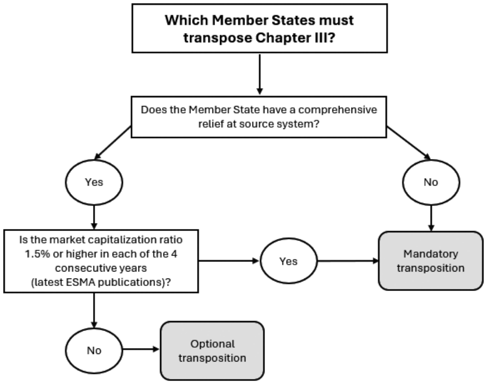
The Directive on Faster and Safer Relief of Excess Withholding Taxes (2025/50) (FASTER) was formally adopted on 10 December 2024 and published in the Official Journal of the European Union on 10 January 2025.

Member States will have to transpose the Directive by 31 December 2028 and the new framework will apply from 1 January 2030.

Object and scope

The Directive lays down two sets of core rules:
- on the issuance of a digital tax residence certificate by Member States (Chapter II of the Directive). These rules apply to all Member States; and
- on the procedure to relieve excess withholding tax that can be withheld by a Member State on dividends from publicly traded shares and, where applicable, interest from publicly traded bonds paid to registered owners who are not residents in that Member State (Chapter III of the Directive). These rules are mandatory only for Member States that:
  - do not have a comprehensive system of relief of excess withholding tax at source on such dividends; or
  - have a market capitalization ratio equal to or above 1.5% in the last 4 consecutive years.

A Member State with a comprehensive relief-at-source system may voluntarily opt to apply Chapter III of the Directive if its market capitalization ratio is less than 1.5% for at least 1 of the last 4 consecutive years.



The European Securities and Markets Authority will start publishing the market capitalization and market capitalization ratio of each Member State on an annual basis from 2026 at the latest, in respect of at least the preceding year.

Digital tax residence certificate (eTRC)

Individuals and entities will be able to request the issuance of a digital tax residence certificate (eTRC) from the Member State of residence.

eTRCs include information such as the name, tax identification number, address, date of issuance and covered period, tax treaties under which the taxpayer requests to be considered resident and any necessary additional information. The covered period will not exceed the calendar or fiscal year for which it was issued.

Member States will issue eTRCs within 14 calendar days, unless the verification of residence requires additional time.

Withholding tax relief procedures

Registered owners receiving dividends or interests from a resident in a Member State applying Chapter III will be able to authorize the certified financial intermediary (CFI) that maintains their investment account (or another CFI, under conditions) to request withholding tax relief on their behalf.

When doing so, CFIs will be required:
- to obtain a declaration from the registered owner, confirming, notably, the entitlement to the relief and

beneficial ownership (article 12(1) of the Directive); and
- to verify information such as the tax residence or the entitlement to a specific reduced withholding tax rate (article 12(2) of the Draft Directive).

Certified financial intermediaries (CFIs)

Large financial sector entities as defined in the Capital Requirements Regulation, handling payments of dividends or interest on securities issued by a resident in a Member State applying Chapter III, and central securities depositories that are withholding tax agents for such payments, will be required to register as CFIs in that Member State.

Financial intermediaries that are resident for tax purposes in a jurisdiction included in the EU list of non-cooperative jurisdictions or listed as high-risk third country in respect of anti-money laundering and countering the financing of terrorism (*see* Annex of the Commission Delegated Regulation (EU) 2016/1675) will not, however, be able to register as CFIs. Other requirements for registration are listed in article 8 of the Directive. Financial intermediaries may be removed from registers upon request or if they cease to meet the requirements for registration.

Member States applying Chapter III will establish a national register of CFIs and designate a competent authority responsible for maintaining and updating the register. Registers will be publicly available through a dedicated portal (European Certified Financial Intermediary Portal).

CFIs will have to report to the competent authority of the Member State information regarding the person providing such information, the payor of the dividend or interest payment, the dividend or interest payment, and the application of anti-abuse measures. Member States may provide for the obligation to report additional information, specified in headings F and G of Annex II, in their domestic law.

Fast-track procedures

The Directive provides for two fast-track relief procedures:
- a relief at source system under which CFIs may request relief at source on behalf of a registered owner by providing to the withholding tax agent the information about tax residence of the registered owner and the applicable withholding tax rate (article 13); and
- a quick refund system under which CFIs may request a quick refund of the excess withholding tax on behalf of the registered owner, if the CFI provides to the Member State a set of information within 2 months after the payment date of the dividend or interest (article 14). This refund request may be rejected, under conditions provided in article 14(4).

Member States may decide to refuse the access to these procedures if one of the conditions listed under article 11(2) is met. Taxpayers will, in any case, have access to standard domestic relief procedures, which will coexist with (one or both of) the fast-track procedures.

3.7. *Pending proposals*

3.7.1. Misuse of shell entities

The Commission, as part of its business tax agenda for the 21st century for 2021-2023 (COM(2021) 251 final), launched an initiative to tackle the abusive use of shell companies to ensure that legal entities without a substantial business presence do not benefit from tax advantages. The Commission issued a proposal for a Council Directive on 22 December 2021 (ATAD 3, also known as the Unshell Directive) and opened a feedback period which ran from 23 December 2021 to 6 April 2022.

Through the use of objective indicators related to income, personnel and premises, the proposed directive aims to establish transparency standards in relation to the use of shell entities, in order to allow tax authorities to detect and prevent misuse of such entities for tax purposes and deny them certain tax benefits.

As an advisory body in this procedure, the European Parliament adopted its report on the ATAD 3 proposal on 17 January 2023 (COM(2021)0565 – C9-0041/2022 – 2021/0434(CNS))). The report is not legally binding for the ECOFIN but should be taken into account while discussing and voting on the proposal.

According to the June 2024 ECOFIN report to the European Council on tax issues (112887/24), most Member States support the objectives of the proposal, but further important technical work would be necessary before reaching an agreement. On 11 June 2024, the Belgian presidency presented a possible way forward but further discussions are needed to reach compromise solutions on outstanding issues.

3.7.2. Debt-equity bias reduction allowance

The Commission, as part of its business tax agenda for the 21st century for 2021-2023 (COM(2021) 251 final), launched an initiative to address the debt-equity bias in corporate taxation through a debt-equity bias reduction allowance (DEBRA) (i.e. an equity allowance). To this end, the Commission issued a proposal for a Council Directive on 11 May 2022 (COM(2022) 216 final) and opened a feedback period which ran from 13 May until 8 July 2022.

In short, the DEBRA initiative proposes:
- an allowance on equity of up to 30% of the taxpayer's EBITDA – for a period of 10 consecutive tax periods – with carry-forward for excesses and unused capacity. This allowance will reduce the corporate income tax base. The allowance is calculated by applying a notional interest rate to the allowance base, which is the difference between the net equity at the end of a tax period and the net equity at the end of the preceding tax period; and
- that 15% of the exceeding borrowing costs (i.e. interest paid minus interest received) is non-deductible.

The European Economic and Social Committee (EESC) has recommended to include an exclusion from the rules for small and medium-sized enterprises (SMEs) and micro-enterprises on the grounds that the proposed measures could make EU companies financially weaker and hamper investment, growth and job creation in the European Union (EESC 2022/02917).

The ECOFIN suspended work on DEBRA in light of the many interlinkages with other corporate tax dossiers, e.g. the Minimum Taxation Directive (*see* section 3.5.), ATAD 3 (*see* section 3.7.1.) and BEFIT (*see* section 3.7.3.), which were under discussion in the Council or had been announced by the Commission (*see* Report to the European Council on tax issues (14905/22 LIMITE FISC 227 ECOFIN 1177), as approved on 6 December 2022).

Nevertheless, the Members of the European Parliament (MEPs) continued to exchange views on this proposal with the purpose of reaching a general Parliament opinion. The European Parliament adopted a supportive opinion, while recommending amendments, during the plenary session of 16 January 2024 (2022/0154(CNS).

On 11 March 2024, the Eurogroup in inclusive format issued a statement on the future of the capital markets union inviting Member States to investigate ways to reduce the debt-equity bias through their national systems, and share best practices and plans. The Commission was invited to support this initiative by providing analysis and advice.

The June 2024 ECOFIN report to the European Council on tax issues (112887/24) does not mention this initiative, meaning that the Council is not currently working on this file.

3.7.3. Business in Europe: Framework for Income Taxation (BEFIT)

On 12 September 2023, the European Commission launched a proposal to develop a common corporate tax framework in the internal market (COM(2023) 532 final). This Business in Europe: Framework for Income Taxation (BEFIT) proposal replaced the Commission's Common Corporate Tax Base and Common Consolidated Corporate Tax Base proposals, which were withdrawn (*see* previous versions of this chapter).

The BEFIT proposal aims to implement a common corporate tax framework for EU large-scale groups of companies, which would replace the 27 national systems. The proposal establishes a common set of rules to determine the tax base of companies that are part of a group that prepares consolidated financial statements and are subject to corporate income tax in a Member State. If the proposal is adopted by the Council, Member States will have to implement the BEFIT into their national laws by 1 January 2028 and the new rules will apply from 1 July 2028.

Together with the BEFIT proposal, the European Commission proposed a Council Directive establishing a Head Office Tax system for micro, SMEs, and amending Directive 2011/16/EU (HOT) (COM(2023) 528 final) and a transfer pricing directive – the Council Directive on transfer pricing (COM(2023) 529 final) – to harmonize minimum standards. For details on the latter, *see* section 7.

On 4 December 2023, MEPs of the ECON Committee discussed the draft report on the BEFIT proposal (2023/0321(CNS)). The draft report was scheduled to be voted on 22 February 2024 but was removed from the agenda. The new date for voting at the ECON Committee is yet to be announced.

The national parliaments of four Member States – Ireland, Malta, Poland and Sweden – were of the opinion that the BEFIT proposal does not comply with the principle of subsidiarity and decided to issue reasoned opinions. If reasoned opinions constituted at least one-third of the total votes, the Commission would have to review the proposal. The deadline to submit reasoned opinions was 16 February 2024.

The European Economic and Social Committee (EESC) has expressed its general support towards the BEFIT Directive, while notably recommending a careful assessment of compliance costs associated with its implementation, as well as its alignment with the Pillar Two rules and EU data protection rules (C/2024/4059).

According to the ECOFIN report to the European Council on tax issues of 24 June 2024 (112887/24), Member States have expressed concerns regarding the operation of the BEFIT Directive with national corporate tax rules, Pillar Two rules and with existing EU acquis in the area of taxation. Further reflection and technical work will be necessary to determine the next steps in the negotiations of the proposal.

Scope

The BEFIT rules foresee a hybrid scope. On one side, a mandatory scope comprises (domestic and multinational) groups which (i) prepare consolidated financial statements, (ii) had annual combined revenues of at least 750 million in at least 2 of the preceding 4 fiscal years and (iii) the ultimate parent entity holds at least 75% of the ownership rights or the rights giving entitlement to profit. Additionally, if the group is headquartered outside the European Union, the EU sub-set will need to additionally raise at least 5% of group revenues in the European Union or the amount of EUR 50 million annual combined revenues in at least 2 of the preceding 4 fiscal years. In-scope groups include the entities that meet the 75% ownership framework.

On the other side, a voluntary scope comprises smaller groups that prepare consolidated financial statements. When a group opts in for this regime, the BEFIT rules apply to all EU entities and permanent establishments that meet the ownership threshold of 75%. In this case, they are bound for a minimum period of 5 years.

Although the rules would cover all sectors, certain sector-specific characteristics are included, such as a carve-out from the BEFIT tax base (which is discussed below) for shipping income covered by a national tonnage tax regime.

Computation and allocation of the tax base

The taxable base is calculated at the single entity level of the relevant group company. These tax bases are then aggregated at the EU group level and ultimately reallocated to the relevant EU Member State.

The starting point for calculating single tax bases is the accounting result from the financial accounts. Then, it foresees tax adjustments by which some items are added back in case they were deducted (e.g. financial assets held for trading, certain borrowing costs, fines, penalties, corporate taxes) or subtracted from the financial net income or loss if they were in the financial accounts (e.g. dividends and capital gains from qualifying participations, profits or losses from permanent establishments). The preliminary tax result is also adjusted to consider depreciation, timing and quantification issues. Tax depreciation rules aim to remain closer to financial accounting than national tax depreciation rules.

The proposal includes special rules for dealing with the tax bases and losses of entities entering or leaving the BEFIT group. These rules also deal with business reorganizations, maintaining the benefits of the Merger Directive while applying an anti-abuse rule to ensure that capital gains are taxed when assets are finally sold out of the group. In this regard, the capital gains that arise from a reorganization within the BEFIT group would normally benefit from a tax exemption, but such exemption would be refused if the company is subsequently sold outside the BEFIT group unless the transaction was carried out for valid commercial reasons. The proposal also accommodates distribution-based tax systems by introducing specific rules.

The preliminary tax results of all members of the BEFIT group are aggregated into a single pool at EU level (called the BEFIT tax base). Among other benefits, the aggregation would allow cross-border tax relief and avoid withholding taxation on transactions such as interest and royalty payments within the BEFIT group insofar as the beneficial owner of the payment is a BEFIT group member.

Income and losses from extractive activities are separated from the BEFIT tax base (they are allocated to their jurisdiction of origin). Results from shipping which is not covered by a tonnage tax regime or from air transport are also excluded.

The aggregated tax base is then allocated to the Member State of each BEFIT group according to a transition rule. The transition allocation rule is calculated as the average of taxable results in the previous three fiscal years. The transition rule would be in place for 7 years (i.e. until 30 June 2035 at the latest). Upon allocation, Member States remain free to further apply any deductions, tax incentives or base increases to their allocated parts, insofar as these adjustments are in line with the rules laid down in the Minimum Taxation Directive (2022/2523) (*see* section 3.5.).

Administration

The proposal provides a common administrative framework by introducing a one-stop shop regime for BEFIT groups. Under the one-stop shop regime, the filing entity will generally be the ultimate parent entity which will file an information return for the whole BEFIT group to its domestic administration. The tax administration will share the BEFIT Information Return with the other Member States in which the BEFIT Group operates. After filing the Information Return, a team of representatives of each relevant tax administration will examine the completeness and accuracy of the filled information.

Additionally, each entity forming the BEFIT group will also file an individual tax return to its local administration to apply the domestically set adjustments to their allocated part.

In principle, individual Member States remain competent to perform tax audits. It will, however, be possible for Member States to request joint audits with other Member States. The latter is obligated to accept such a request.

Appeals against the content of the BEFIT Information Return may be brought to an administrative body of the Member State of the filing entity. Appeals of an individual BEFIT group member against an individual tax return may be brought to its tax administration.

3.7.4. HOT (head office tax system for SMEs) proposal

On 12 September 2023, the European Commission launched a new proposal to create a head office tax system (HOT) for SMEs (COM(2023) 528 final). Under this proposal, SMEs that operate cross-border through permanent establishments will have the option to interact with only one tax administration (i.e. the administration of the head office) instead of having to comply with multiple tax systems. It aims to increase certainty and reduce compliance costs by filing one single tax return and calculating tax liability based on the applicable rules of the Member State of its head office. If adopted by the Council, Member States will have to transpose it into their national laws by 31 December 2025 and the new rules will apply from 1 January 2026.

The European Parliament adopted its opinion on the HOT proposal, which is supportive but recommends significant amendments, during the plenary session of 10 April 2024 (2023/0320(CNS)).

According to the ECOFIN report to the European Council on tax issues of 24 June 2024 (112887/24), a large number of delegates raised serious concerns as regards several aspects of the proposal (aggressive tax planning, effects on tax revenues, competitiveness, among others). A number of Member States hold the view that a general discussion should take place before further technical progress can be made. The December 2024 ECOFIN Report (16673/24) tuned out to conclude that the Commission proposal cannot be supported by Member States due to fundamental concerns of principle.

3.8. *Other developments*

SAFE (Securing the Activity Framework of Enablers)

The European Commission has released a new initiative to tackle the role that enablers can play in facilitating arrangements or schemes that lead to tax evasion or aggressive tax planning involving third countries. The European Commission published a report which summarizes the contributions made by stakeholders during the feedback period (that ran from 6 July to 12 October 2022) on 31 January 2023. This initiative is known under the acronym SAFE (Securing the Activity Framework of Enablers). The adoption of the legislative proposal by the European Commission was expected for the first quarter of 2023, but has not yet been scheduled. According to the meeting of the Committee on Economic and Monetary Affairs of the European Parliament held on 28 June 2023, work on the SAFE proposal will depend on the progress of the negotiations of ATAD 3 (*see* section 3.7.1.).

Code of Conduct list of preferential tax regimes

The Code of Conduct Group (Business Taxation) regularly publishes an overview of preferential tax regimes in (i) the European Union; (ii) dependent or associated territories of Member States to which EU treaties do not apply; and (iii) other jurisdictions.

On 8 November 2016, the ECOFIN set out criteria for screening jurisdictions with the purpose of establishing an EU list of non-cooperative jurisdictions (14166/16). The ECOFIN agreed on a Revised Code of Conduct for Business Taxation on 8 November 2022 (14452/22 FISC 214 ECOFIN 1131) which broadened the scope of the tax measures under scrutiny and clarified the review process in the Code of Conduct Group.

The screening focuses on the following three areas:
– tax transparency: implementation of, or commitment to, exchange of information under various standards, e.g. the Common Reporting Standard, OECD Exchange of Information on Request and the OECD Multilateral Convention on Mutual Administrative Assistance. The inclusion of an additional criterion on beneficial ownership information is currently under discussion;
– fair taxation: the existence of harmful preferential regimes, the facilitation of offshore structures and arrangements attracting profits that do not reflect real economic activity in the jurisdiction and, from 2022, tax features of general application which can be considered as harmful if they lead to double non-taxation or the double/multiple use of tax benefits; and
– implementation of BEPS measures: implementation of, or commitment to, the agreed OECD anti-BEPS minimum standards.

Jurisdictions that, after screening, do not meet all three criteria are placed on the list of EU non-cooperative jurisdictions. The list, first adopted on 5 December 2017, is generally updated twice a year and currently contains the following jurisdictions (last updated on 8 October 2024): American Samoa, Anguilla, Fiji, Guam, Palau, Panama, Russian Federation, Samoa, Trinidad and Tobago, the US Virgin Islands and Vanuatu.

Countries taken off the non-cooperative list may be moved to a separate category of jurisdictions subject to close monitoring (the so-called grey list).

4. The Fundamental Freedoms and Their Impact on Direct Taxation

In relation to direct taxation, Member States retain, in principle, their sovereignty to regulate issues related to income taxation, such as the residency test, the rules on taxable base, rates, loss relief, exemptions or depreciation.

However, the exercise of this sovereignty in direct tax matters must be aligned with the principles established under EU treaties. In this regard, EU law prevents Member States from imposing rules that restrict companies in exercising their fundamental freedoms or that result in unlawful discrimination between resident and non-resident companies.

The four fundamental EU freedoms – i.e. the free movement of goods, the free movement of persons (including the free movement of EU citizens, the free movement of workers and the freedom of establishment), the freedom to provide services and the free movement of capital and payments – as well as the principle of non-discrimination, all regulated under the TFEU, form immediately applicable law and constitute individual and enforceable rights for every single individual or enterprise in the European Union (subject to the procedural requirements of national courts or the ECJ). Accordingly, in view of the fact that there has been little progress harmonizing direct taxation, the direct application of the TFEU's provisions continues to form the most important source of EU law in that area.

The ECJ has assessed the compatibility of national measures on direct taxation with EU law by determining whether:
– the domestic measure distinguishes between cross-border and internal situations;
– there is an *objective difference* between the cross-border and the internal situation that makes them comparable in light of the object and purpose of the concerned measure;
– the restriction can be *justified* by a legitimate aim (i.e. a mandatory requirement of public interest) such as the prevention of abuse or safeguarding the tax base integrity; and
– the measure's restrictive effect is *proportionate* to the legitimate aim.

For legislation to be regarded as a restriction on EU freedoms, it is sufficient to establish that such legislation *could* restrict the exercise of the freedom(s) in question in a Member State by companies established in another Member State, without having to establish that the legislation in question has *actually* restricted that (those) EU freedom(s).

The sections below summarize the ECJ's conclusions on the most relevant aspects related to corporate and individual taxation.

4.1. *Corporate taxation*

4.1.1. Treatment of cross-border transactions

Member States generally provide some reliefs to mitigate or eliminate juridical and economic double taxation that can arise from cross-border investments.

In some cases, the Parent-Subsidiary Directive (2011/96) and the Interest and Royalties Directive (2003/49) regulate such relief mechanisms (*see* sections 3.1. and 3.2.). In cases not falling within the scope of these (or other) directives, such relief mechanisms may be limited, by domestic rules, to resident recipients or domestic income.

Domestic rules under both cases must be compatible with EU freedoms. EU law provides for:
– home state neutrality, i.e. the right not to be hindered to earn income abroad (national tax treatment of

foreign-source income should not be less advantageous than that applied to resident taxpayers deriving similar income from domestic sources); and

– host state neutrality, i.e. equal treatment of non-residents and residents as regards their tax base.

Home state neutrality: Taxation of resident companies receiving foreign-source income

In general terms, resident companies receiving foreign-source income should be treated the same way as resident companies receiving domestic income, provided they are in an objectively comparable situation. This applies unless the disparate treatment is justified by an overriding reason of public interest. For example, legislation of a Member State under which certain reliefs aimed at mitigating the risk of double taxation do not apply where the income arises from foreign sources is often found incompatible with EU law.

Member States are free to choose a method for avoiding a series of charges to tax. For example, the method to relieve double taxation may be different for domestic dividends (exemption method) than it is for inbound foreign dividends (credit method). This is not an issue as long as the latter are not treated less favourably than the former. As both categories of dividends are comparable as concerns the risk of economic double taxation, a Member State must mitigate such double taxation on inbound foreign dividends to the same extent as it does for domestic dividends. Accordingly, the tax rate applied to foreign-source dividends cannot be higher than the rate applied to nationally-sourced dividends, and the tax credit granted should be at least equal to the amount paid in the Member State of the company making the distribution – *see FII Group Litigation* (Case C-446/04) and *CFC and Dividend Group Litigation* (Case C-201/05).

In this regard, allowing full neutralization for the add-back of a proportion of costs and expenses (equal to 5% of the net dividends received) only for group domestic subsidiaries but not for foreign subsidiaries – *see Groupe Steria* (Case C-386/14) – is incompatible with the freedom of establishment.

Likewise, denying a carry-forward of credit to subsequent years (when the company receiving dividends has recorded an operating loss for the year in which it received the foreign-source dividends), while a resident company can carry-forward losses and apply an exemption to domestic dividends – *see Haribo and Salinen* (Case C-436/08) – is incompatible with the free movement of capital. The refusal to grant a tax credit to resident shareholders receiving domestic-source dividends, where those dividends originated from foreign-source profits – *see The Trustees of the BT Pension Scheme* (Case C-628/15) – is also in breach of the free movement of capital. Also, Member States cannot provide a tax advantage exclusively with respect to dividends attached to shares listed on the stock exchange of that Member State while denying dividends attached to shares listed on foreign stock exchanges such an advantage – *see Real Vida Seguros* (Case C-449/20).

Further, applying an exemption and allowing for the set off of withholding tax against corporation tax payable for resident investment companies and non-resident investment companies with a permanent establishment in the Member State, while disallowing non-resident investment companies with no permanent establishment in the Member State this same treatment – *see Commission v. Belgium* (Case C-387/11) – constitutes unlawful restrictions of both the freedom of establishment and the free movement of capital.

The application of the credit system to foreign dividends can imply administrative burdens that fall on the taxpayer. In this regard, Member States are allowed to require evidence with regard to foreign-source dividends, insofar as that evidence is not (virtually) impossible or excessively difficult to obtain – *see Accor* (Case C-310/09). Possible justifications for imposing this administrative burden include ensuring the effectiveness of fiscal supervision and combating tax avoidance.

In particular, Member States can make relief for foreign-source dividends contingent on the existence of a treaty containing an exchange-of-information clause with the source state – *see A* (Case C-101/05); *Pharol, SGPS, SA v. Autoridade Tributária e Aduaneira* (C-67/22). However, requiring an agreement for mutual assistance not only at the administrative level but also with regard to enforcement can be deemed disproportional – *see Haribo and Salinen* (Case C-436/08). In the same way, legislation of a Member State that makes the application of a tax credit conditional upon the provision of a specific tax certificate, without any opportunity for the shareholder to prove, by means of other factors and relevant information, payment of the tax, is also disproportional – *see Meilicke II* (Case C-262/09).

Member States cannot require that the application of a participation exemption to foreign dividends be dependent on the condition that the distributing entity derives its gross profits from active business activities while not requiring the same from domestic-source dividends. Such a requirement cannot be justified based on the need to prevent tax avoidance (as it does not specifically target conduct involving the creation of wholly artificial arrangements that do not reflect economic reality, but provides for an irrebuttable presumption of abuse merely because dividends are distributed out of profits derived from passive income) – *see EV* (Case C-685/16).

Similarly, Member States cannot reject the deduction of the interest paid to an associated company that resides in another Member State on the ground that the principal reason for the debt is for the group to receive a substantial tax benefit, and such tax benefit would not have been deemed to exist if both companies had been resident in the first Member State – *see Lexel* (Case C-484/19). However, Member States may deny the deduction of interest where the debt is considered to constitute a wholly artificial arrangement, even if the conditions of the loan were at arm's length – *see X BV* (C-585/22).

By contrast, Member States are not required to grant a credit for the withholding tax levied on foreign portfolio dividends to prevent juridical double taxation – *see Haribo and Salinen* (Case C-436/08). In this regard, juridical double taxation arising from the parallel exercise of tax competences by different Member States is not contrary to EU law – *see Damseaux* (Case C-128/08). Furthermore, Member States are not obliged to grant a refund for the tax paid by the distributing company at the

The Home of International Taxation

Contact

IBFD Head Office
Tel.: +31-20-554 0100 (GMT+2)
Email: info@ibfd.org

Visitors' Address:
Rietlandpark 301
1019 DW, Amsterdam
The Netherlands

Postal Address:
P.O. Box 20237
1000 HE Amsterdam
The Netherlands