

**11 September 2024**

**BusinessEurope's response to the Call for Evidence for an Evaluation / Fitness Check on the Anti-Tax Avoidance Directive – Council Directive (EU) 2016/11641 of 12 July 2016, as amended by Council Directive (EU) 2017/9522 of 29 May 2017.**

### **Introductory Comments**

BusinessEurope welcomes the European Commission's initiative to evaluate the Anti-Tax Avoidance Directive (ATAD).

We support a cohesive long-term taxation strategy that re-evaluates and streamlines the EU's existing anti-tax avoidance rules which have been introduced over recent years. Rather than adding new anti-avoidance measures and complexities (examples include a third iteration of ATAD and a directive on Securing the Activity Framework of Enablers), the Commission's goal should be to enhance the EU's attractiveness. To achieve this, streamlined tax rules are essential for reducing the administrative burden on companies operating within the EU, fostering a more business-friendly environment that encourages investment and growth.

The ATAD, designed to combat aggressive and undesirable tax practices, has significantly impacted the tax landscape within the European Union (EU) as a result of the minimum standards and options granted in the Directive. As such, the practical positive impact of the ATAD rules requires further assessment. In addition, with the OECD/G20 Inclusive Framework's Pillar II rules now targeting similar policy objectives, it is timely and appropriate to critically assess the necessity and effectiveness of the existing ATAD provisions.

### **Specific Comments**

This paper outlines the key concerns of EU-based businesses and proposes areas for simplification or amendment. The goal is to ensure that tax regulations remain aligned with economic realities and do not impose unnecessary burdens on businesses. Any changes to the existing rules should be based on a quantitative assessment of the behavioural changes that ATAD has achieved in each Member State since its implementation.

#### **A. Controlled Foreign Company (CFC) rules**

##### *Overlap between CFC rules and Pillar II*

The overlap between CFC rules and the Pillar II framework is a primary concern. Pillar II acts as a form of 'super-CFC', targeting profit shifting and ensuring a minimum level of taxation globally.



Businesses subject to both regimes face dual compliance burdens, having to navigate both CFC rules and the new global minimum tax framework. This raises the question of whether CFC rules remain necessary for businesses already in scope of Pillar II. Although CFC rules and Pillar II may differ in their approach, a reassessment of the continued relevance of CFC rules is warranted.

### *Complexity and Uncertainty*

The minimum level of harmonization of the ATAD rules across Member States presents specific challenges for businesses, such as:

- CFC rules can vary significantly between EU Member States and are not well-designed to interact with each other or with other ATAD anti-abuse rules, such as interest limitation or anti-hybrid mismatch rules. This creates complexity and can lead to double taxation issues.
- The complexity of the ATAD rules also complicates risk assessment in cross-border acquisitions, potentially disadvantaging businesses subject to more rigid ATAD rules when compared to their international competitors.
- The definition of embedded royalties under CFC rules is unclear in certain Member States (for example, Denmark), making compliance extremely difficult. The requirement to manually produce baseline data for calculations, often based on assumptions and hard-to-access information, adds no value to businesses but significantly increases their compliance burden.

### *Recommendation*

On this basis, we recommend a thorough assessment of the effectiveness and efficiency of CFC rules across EU Member States. This evaluation should not focus solely on revenue generation, as CFC rules are primarily behavioural in nature. It should also consider how well they achieve their policy goals. Based on this assessment, policymakers should consider deactivating CFC rules for groups already subject to Pillar II rules (such as the Qualified Domestic Minimum Top-Up Tax or Income Inclusion Rule), with a General Anti-Avoidance Rule (GAAR) serving as a safety net.

## **B. Interest Deduction Limitation Rules**

The rules limiting the deductibility of interest expenses have increasingly become a hindrance to business growth and economic recovery, particularly in the current economic climate marked by inflation and rising interest rates.

The economic conditions under which these rules were introduced have drastically changed with refinancing interest rates increasing sharply. This sharp rise in the cost of debt, coupled with the fixed cap on deductible interest expenses has significantly constrained businesses' ability to invest, particularly in substantial and long-term projects such as the green and digital transitions.



A key point often overlooked in the discussion of interest deduction limitations is the taxation of interest income. In situations involving equity capital investment, particularly within groups, dividends are typically not deductible, but often remain untaxed for the recipient. This contrasts with interest, which is taxed, even when its deduction is disallowed, creating a non-neutral and unnecessarily costly situation for businesses.

### *Recommendation*

To address these challenges, we propose increasing the ceiling for deductible expenses periodically to help align the rules with the reality of inflation and the rising cost of debt, supporting business investment and economic growth without undermining the original intent of the rules.

In addition, in cases where non-deductible interest arises from excess leverage, a tax exemption for the corresponding interest income should be assessed. When the denial of interest deduction is justified, it is often because the excess leverage is seen as resembling equity capital (especially in the case of long-term debt) or because interest deduction is perceived as an ‘extra benefit’ facilitating cross-border profit shifting. In both cases, if interest deductions are disallowed, there is a strong case for exempting the taxation of the corresponding interest income to maintain tax neutrality and avoid penalizing companies.

## **C. General Anti-Avoidance Rule (GAAR)**

A key component of the ATAD is the introduction of a GAAR, which targets non-genuine arrangements both domestically and cross-border. While the ATAD GAAR is similar in design to the GAAR in the Parent-Subsidiary Directive (PSD), its broader scope raises questions around the necessity of retaining the PSD GAAR within the European tax framework.

Additionally, the ATAD GAAR lacks clear interpretation guidelines, leading to legal uncertainty for taxpayers and increasing the risk of inconsistent application among Member States.

### *Recommendation*

To simplify tax legislation, we recommend the removal of the PSD GAAR and providing clearer guidance on the application of the ATAD GAAR to ensure consistent interpretation across the EU.

## **Concluding thoughts**

As the global tax landscape continues to evolve, it is crucial that EU tax policy keeps pace by eliminating redundancies, reducing unnecessary burdens, and ensuring that tax rules support, rather than hinder, economic growth.

The areas highlighted in this paper represent key concerns for EU-based businesses that, if addressed, could lead to a more streamlined and effective tax system.

BusinessEurope remains available to engage with the European Commission to ensure this evaluation, and others, result in a simpler and more competitive EU tax framework.