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European Commission
Directorate-General Taxation and Customs Union (DG TAXUD)

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| FROM | Loyens & Loeff N.V. |
| DATE | 23 January 2024 |
| RE | Public consultation – BEFIT Proposal |

Dear Sirs and Madams,

With regard to the Proposal for a Council Directive on Business in Europe: Framework for Income Taxation (**BEFIT**) (released on 12 September 2023) (hereinafter referred as the **BEFIT Proposal**), we would like to express our gratitude for the opportunity to submit comments.

We welcome the efforts of the European Commission to introduce a common framework for corporate income taxation in European Union thereby trying to simplify tax rules, enhance tax certainty and decrease the compliance and administrative burden for MNE groups and tax authorities. The current BEFIT Proposal nonetheless raises various questions which may undermine these objectives.

Our comments to the BEFIT Proposal are divided into four parts and focus on some critical issues that we identified. In the first part, we will focus on some general issues that may hamper achieving the objectives. In the second part of our comments, we address more technical issues regarding specific provisions in relation to scope and administrative procedure. In the third part, we will focus on the transfer pricing clauses. In the fourth part, we elaborate on the negative impact that the interaction with the Pillar Two rules[1] might have.

We trust that our comments and recommendations will support the European Commission to achieve its goals and enhance the BEFIT Proposal. Although more specific recommendations have been included as well, our general recommendations can be summarized as follows:

- Reduce the need to comply with multiple corporate income tax systems: introducing the BEFIT Proposal in its current form would create a variety of corporate tax systems within the EU that would co-exist which hampers the objective to simplify the rules and reduce compliance costs. This is mainly due to the limited scope of the BEFIT group (i.e. the introduction of the 75% threshold) as well as the (apparently unlimited) freedom for Member States to adjust the tax base after allocation. We would therefore suggest extending the

[1] OECD/G20 Base Erosion and Profit Shifting Project Tax Challenges Arising from Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two), 14 December 2021. These rules are implemented in the European Union through Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union. Since the Directive largely follows the OECD Model Rules, both documents are referred to as the Pillar Two rules throughout this document.

scope of the BEFIT group and to specify the limited adjustments that Member States are allowed to make to the allocated taxable basis.

- Align the BEFIT Proposal as much as possible with the Pillar Two Directive: the starting point to limit the scope to groups having consolidated revenues of at least €750m and to rely on financial accounts is similar in both instruments. Significant differences nonetheless remain as regards the scope and the adjustments to be made to the financial net income or loss. Adding an additional corporate income tax system with a different scope and set of rules for calculating the tax base on top of the Pillar Two calculations and the existing national corporate income tax systems increases complexity and uncertainty rather than reducing it. More alignment between the Pillar Two rules and the BEFIT Proposal would therefore seem appropriate (to the extent possible). Moreover, the interaction between the Pillar Two rules (jurisdictional blending) and the BEFIT Proposal (regional blending) can result in over-taxation. These issues should first be discussed with both the OECD as well as all third states that have implemented the Pillar Two rules. Until these issues are addressed globally, we would recommend limiting the BEFIT Proposal to the harmonization of the taxable basis.

- Align the BEFIT Proposal as much as possible with other Directives such as the Accounting Directive, the Parent-Subsidiary Directive and the Interest-Royalty Directive: the BEFIT Proposal differs in several respects from the valuation methods mentioned in the Accounting Directive as further clarified by the CJEU. The BEFIT Proposal should respect the valuation methods used under IFRS and national GAAP as much as possible to avoid too much complexity in calculating the tax base. In addition, the scope of the BEFIT Proposal, the Parent-Subsidiary Directive and the Interest-Royalty Directive is worded differently, for example, with respect to the requirement of tax residency and being subject to tax. Such differences create uncertainties and misalignments. It would therefore be appropriate to align wording as much as possible and to also consider the relevant CJEU case law throughout the BEFIT Proposal.

- Align the BEFIT Proposal as much as possible with double tax treaties: the interaction between the BEFIT Proposal and existing double tax treaties that Member States have concluded with third countries is not elaborated on and raises various questions. The interaction can also result in double taxation or under taxation due to the baseline allocation method and loss-relief within the EU. For purposes of tax certainty and to avoid double taxation or under taxation, the BEFIT Proposal should address the relationship between both instruments and the double tax treaties should be aligned with the mechanism of the BEFIT Proposal to avoid the risk of double taxation or under taxation.

- Include more definitions and technical guidance: at present, the BEFIT Proposal uses various terms that lack a proper definition and introduces rules without further guidance. Many unclarities therefore remain which create uncertainties, more disputes and increased compliance costs. We would therefore recommend to (a) provide more definitions and technical guidance and (b) to clarify whether the terms used have an autonomous EU meaning or whether references should be made to other sources, such as the financial accounting standards, national tax systems or the Pillar Two rules.

- Reconsider the risk assessment framework for intra-BEFIT group transactions: the BEFIT Proposal stipulates that (during the transition phase) the intra-BEFIT group transactions are only presumed to be priced at arm's length if they are considered to be in "a low-risk zone". The "low-risk zone" would cover the expense incurred / income earned by a BEFIT group member from an intra-BEFIT group transaction that increases by less than 10 percent compared to the average amount of the income or expense in the previous three fiscal years. The transaction is presumed not to be arm's length if this threshold is exceeded, unless the BEFIT group member can provide evidence that the relevant intra-BEFIT group transaction was priced in accordance with the arm's length principle. Since this threshold seems too strict and since the reversal of the burden of proof contravenes the commonly implemented legal framework, we recommend aligning the risk assessment framework with common approaches.

- Extend the filing deadline: the BEFIT Proposal requires the filing entity to file a BEFIT information return within four months after the end of the fiscal year. From a practical point of view, it does not seem feasible for all in-scope groups to have audited accounts available in the required financial accounting standard and to prepare and file a BEFIT information return within a four-month timeframe. In this respect, we would also like to emphasize that - depending on the accounting standard – companies might be required to accurately report both (estimated) corporate income taxes and the entire Pillar Two position in their financial accounts. This requires that all computations of Top Up Taxes and Qualified Domestic Top Up Taxes are performed prior to the audit and approval of the accounts. It is a challenge to perform such an exercise in four months, potentially resulting in high penalties for MNEs if this strict deadline cannot be met. We would therefore recommend extending this filing deadline.

- Include a specific dispute resolution mechanism and address unclarities regarding the procedural aspects: although the BEFIT Proposal foresees rules to make an administrative or judicial appeal and thus considers the right to defense, such procedures are often costly and can be very time-consuming. In addition, contradictory outcomes cannot be ruled out if different procedures are running simultaneously in multiple Member States. For legal certainty and simplicity, we recommend adding a dispute resolution mechanism to the BEFIT Proposal. Moreover, various uncertainties remain regarding the procedure that we would encourage to reconsider.

The comments submitted herein are on behalf of Loyens & Loeff N.V. and should not be construed as representing the opinions of any of its clients.

Should you have any question regarding our comments and recommendations, please feel free to contact us:

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Yours faithfully,
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# 1 GENERAL COMMENTS

At present, businesses that operate in all Member States have to comply with 27 different corporate income tax systems and deal with 27 different tax administrations, making it difficult and costly for companies to do business across the European Union (**EU**).[2] The divergent features of these corporate income tax systems and the different tax administration practices create an uneven playing field and increase tax uncertainty and tax compliance costs for businesses operating in more than one Member State.[3] This undermines the competitiveness of the EU.

To simplify the tax rules, stimulate growth and investments and ensure sustainable tax revenues for Member States, the European Commission proposes a common set of rules to determine the corporate income tax base for large groups within the EU and a common approach to transfer pricing. More specifically, the BEFIT Proposal aims to encourage cross-border expansion, to increase tax certainty and fairness and to reduce compliance costs for EU businesses, distortions that influence business decisions, and the risk of double and over-taxation and associated tax disputes.[4]

Several elements in the BEFIT Proposal may, however, hamper these objectives, thereby running the risk for the rules to be inefficient, ineffective, irrelevant and/or incoherent. This is not in line with the guidelines for better regulations[5] and raises proportionality concerns.

We do not intend to address all potential issues that may arise but have highlighted certain areas where we believe that the BEFIT Proposal should be reconsidered to safeguard a.o. the principle of proportionality laid down in article 5, § 4 of the Treaty on European Union (**TEU**) and to better achieve the objectives of the BEFIT Proposal.

## 1.1 Multiple Corporate Income Tax Systems

The current corporate income tax systems within the EU have become highly complex due to amongst others the introduction of various anti-avoidance rules and transparency rules. Both for the taxpayers as well as the tax administration, the associated administrative burden and costs have increased significantly. An initiative that intends to reduce the administrative burden by introducing a new EU corporate tax framework can therefore be supported, but only to the extent it effectively reduces the compliance costs. Although the European Commission estimates that simplified tax rules reduce compliance costs by 32%, it has also been acknowledged that the costs for implementing the BEFIT Proposal cannot be estimated with any precision since no precedent is available.[6] Considering the current design, we believe that the BEFIT Proposal might even further increase (rather than reduce) compliance costs for both taxpayers and tax administrations.

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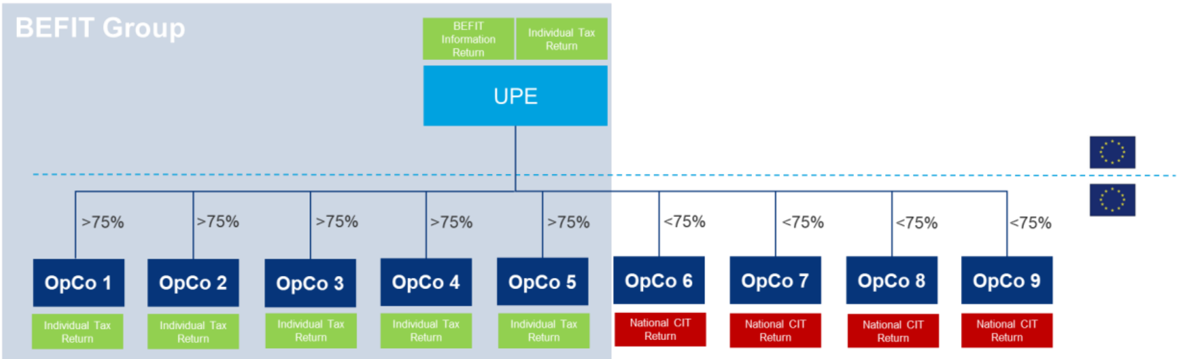
[2] Par. 2 Preamble BEFIT Proposal.
[3] Explanatory Memorandum, p. 1.
[4] Par. 3 and 5 Preamble BEFIT Proposal; Commission Staff Working Document. Impact Assessment Report, SWD (2023) 308 final, p. 23-25.
[5] Commission Staff Working Document. Better Regulation Guidelines, SWD (2021) 305 final, p. 26.
[6] Commission Staff Working Document. Impact Assessment Report, SWD (2023) 308 final, p. 41, 45 and 112.

Assume, for example, a group headquartered in the EU that operates worldwide. In the EU, the Ultimate Parent Entity[7] operates via nine subsidiaries which are all tax resident in different Member States. All subsidiaries are consolidated on a line-by-line basis in the Consolidated Financial Accounts even though the participation held in four subsidiaries is below 75%. This situation can be depicted as follows:




At present, the group files ten corporate income tax returns in different Member States based on ten different corporate income tax systems. After implementation of the BEFIT Proposal this group will need to file (a) four corporate income tax returns according to the existing national corporate income tax systems for the subsidiaries that do not form part of the BEFIT group[8], (b) one BEFIT information return in the Member State of the Ultimate Parent Entity in accordance with the rules laid down in the BEFIT Proposal including the BEFIT tax base[9], and (c) six individual tax returns in each Member State where a BEFIT group member is tax resident whereby again various systems will need to be considered as all Member States seem to be entirely free to adjust the allocated part in accordance with Article 48, §2 of the BEFIT Proposal. The BEFIT Proposal is therefore not *de facto* replacing 27 tax systems for computing the tax base[10], but introduces a corporate income tax system that operates alongside the existing systems within the EU for all entities that fall outside the scope of the BEFIT group. This situation only increases the administrative burden and compliance costs for taxpayers as they need to comply with even more different systems for calculating a tax base. Even if the scope of the BEFIT group would be extended to all EU group entities that form part of the consolidation, the issue remains due to the broad possibility granted to Member States to adjust the BEFIT tax base after allocation. If all subsidiaries in this example would be in scope, the group will still need to file one BEFIT information return and ten individual tax returns with possibly an equal number of different

[7] Article 3 BEFIT Proposal defines an Ultimate Parent Entity as "*a) an entity that owns, directly or indirectly, a controlling interest in any other entity and that is not owned, directly or indirectly, by another entity with a controlling interest in it; or (b) the head office of a group as defined in point (1)(b).*"
[8] According to Article 5 BEFIT Proposal, a BEFIT group is only formed by the Union sub-set of entities that meet the 75% ownership threshold. Entities below this threshold, thus fall outside the scope and remain subject to their national corporate income tax system. For these entities an opt-in does not seem possible pursuant to Article 2, §7 BEFIT Proposal.
[9] Article 57 BEFIT Proposal.
[10] Impact Assessment p 37.

rules. This implies that a taxpayer may still need to deal with ten different tax administrations instead of one.

The current scope of the BEFIT group as well as the (apparently unlimited) freedom for Member States to adjust the tax base after allocation hamper in our view the objective to simplify the rules and reduce compliance costs. In some situations, the BEFIT Proposal will impose a disproportionate compliance burden on certain domestic and/or MNE groups. A solution could be to extend the scope of the BEFIT group and to specify the limited adjustments that Member States are allowed to make to the allocated taxable basis.

### 1.2 Incoherence with other EU Directives

To reach the objectives of the BEFIT Proposal, it is imperative that the rules are consistent with other EU directives/initiatives. The BEFIT Proposal nonetheless seems to contain several inconsistencies with existing EU directives.

*BEFIT Proposal versus Pillar Two Directive*

According to the Explanatory Memorandum, the new rules are aligned as closely as possible with the Two-Pillar approach to reduce compliance costs.[11] The fact that the BEFIT Proposal takes financial accounting statements as a starting point seems sufficient to state that "*the room for discrepancies between BEFIT and Pillar 2 is thus expected to be limited*".[12] Although the starting point to rely on financial accounts is indeed similar, significant differences nonetheless remain as regards the scope and in determining the taxable base. The tax adjustments that need to be made to the financial net income or loss are, for example, not similar in the Pillar Two rules and the BEFIT Proposal.[13] Adding an additional corporate income tax system with a different scope and set of rules for calculating the tax base on top of the Pillar Two calculations and the existing national corporate income tax systems increases complexity and uncertainty rather than reducing it. More alignment between the Pillar Two rules and the BEFIT Proposal would therefore seem appropriate (to the extent possible). Moreover, as will be shown in chapter 4, the interaction between the Pillar Two rules and the BEFIT Proposal can result in over-taxation. Tax Administrations and MNEs in countries all over the world are currently putting a lot of effort and time in understanding and implementing Pillar Two rules and may not have sufficient resources to include this additional layer of complexity at this moment.

*BEFIT Proposal versus Accounting Directive*

The Explanatory Memorandum also mentions that "*the new BEFIT tax base will be primarily based on existing financial accounting rules, which are already accepted under Union law, i.e. either the*

[11] Explanatory Memorandum, p. 6.
[12] Impact Assessment p. 121.
[13] The statement made in the impact assessment that the Pillar Two rules are largely based on the same rules for adjusting the financial accounting statements is simply not correct: Impact Assessment p. 58 and p. 121.

*national generally accepted accounting principles (GAAP) of the Member States, or the International Financial Reporting Standards (IFRS)*."[14] The national GAAP of the Member States are based on the Accounting Directive[15]. According to this Directive, the annual financial statements must give a true and fair view of the undertaking's assets, liabilities, financial position and profit or loss.[16] The Directive also mentions that assets should be valued at their purchase price.[17]

With respect to the valuation method to be used when acquiring an asset free of charge or at a low value, reference can be made to two cases of the Court of Justice of the EU (**CJEU**).[18] In these cases, a Belgian company acquired shares at a very low price or for free. The Belgian company registered the shares for accounting purposes at the acquisition price which was manifestly lower than the real value. The Belgian tax authorities took the view that the company was obliged to depart from the valuation at purchase price since it would be incompatible with the principle that a true and fair view must be given.[19] According to the Belgian tax authorities, the Belgian company should thus have registered the shares at their fair value for accounting purposes. The CJEU judged that the principle of true view and the principle that assets are to be valued at purchase price requires assets to be accounted for at their historical cost and not at their real value.

The BEFIT Proposal seems to contradict these CJEU cases when it rules that "*the depreciation base of an asset received as gift shall be the market value as included in the financial accounts*". Pursuant to this CJEU case law, financial accounts following the accounting principles laid down in the Accounting Directive do not need to value assets at fair market value. More in general, the BEFIT Proposal should respect the valuation methods used under IFRS and national GAAP as much as possible to avoid too much complexity in calculating the tax base, for example with respect to depreciations, stock and work-in-progress. In this respect, it is also not clear why, for example, the LIFO method is not accepted under the BEFIT Proposal whereas this method is accepted under the Accounting Directive.[20]

*BEFIT Proposal versus Parent-Subsidiary Directive/ Interest-Royalty Directive*

Finally, we notice that the scope of the BEFIT Proposal, the Parent-Subsidiary Directive[21] (**PSD**) and the Interest-Royalty Directive[22] (**IRD**) is worded differently, for example, with respect to the requirement of tax residency and being subject to tax. Such differences create uncertainties and

[14] Explanatory Memorandum, p. 6.
[15] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings.
[16] Article 4, §3 Accounting Directive.
[17] Article 6, §1 (i) Accounting Directive.
[18] CJEU 3 October 2013, C-322/12, Gimle; CJEU 6 March 2014, C-510/12, Bloomsbury.
[19] This argument was based on article 2(5) Fourth Council Directive 78/660/EEC of 25 July 1978: "*Where in exceptional cases the application of a provision of this Directive is incompatible with the obligation laid down in paragraph 3, that provision must be departed from in order to give a true and fair view within the meaning of paragraph 3 […]*."
[20] Article 12(9) Accounting Directive.
[21] Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States.
[22] Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States.

misalignments. It would therefore be appropriate to align wording as much as possible and to also consider the relevant CJEU case law, such as the Denkavit-case.[23] Based on the wording and purpose of the PSD, the CJEU confirmed in this case that the tax advantage of the PSD (*in casu* the participation exemption), must be granted if the parent company has a holding in the subsidiary during a certain period of time, without it being necessary that this period should have come to an end at the time when the tax advantage is granted. Since a more stringent approach under BEFIT would not seem appropriate, we propose to align Article 8 of the BEFIT Proposal with this judgement.

### 1.3 Incoherence with double tax treaties

The interaction between the BEFIT Proposal and existing double tax treaties (**DTTs**) that Member States have concluded with third countries is not elaborated on and raises various questions.

Contrary to, for example, the PSD[24] and IRD[25], a company remains in scope of the BEFIT Proposal if it is a tax resident in a Member State, despite the fact that the company is a tax resident of a third state pursuant to a DTT. Including the income of such company into the BEFIT tax base (which is allocated among various BEFIT group members) would be contrary to DTTs and would create double taxation.

The tax treatment of a permanent establishment (**PE**) in the BEFIT Proposal might also potentially give rise to over taxation and under taxation due to conflicts with DTTs. Article 12 of the BEFIT Proposal mentions that the financial accounting net income or loss of a BEFIT group member shall be adjusted to exclude the income or loss that is attributable to a PE. This rule seems to apply irrespective of the country where the PE would be located, and how an existing DTT avoids double taxation.[26] It is not clear whether the DTT would take precedence over Article 12 of the BEFIT Proposal. It is also not clear how the income or loss is to be attributed to a PE and whether the existing DTT should be relied upon.

In the opposite situation, where the head office is located in a third state and the PE in a Member State, difficulties might also arise, for example, if the DTT obliges this third state to provide a tax credit for the taxes paid by the PE or an exemption with a subject to tax requirement. As a result of the baseline allocation, no or little tax might be due in the PE state and the third state might consequently not provide a (full) tax credit or exemption resulting in double taxation.

The BEFIT Proposal further allows a tax credit in line with a DTT or national law if a BEFIT member derives income that has been taxed abroad and taking into account certain calculation rules (e.g. the tax credit is calculated on net basis and not gross basis).[27] Foreign taxes on exempt income received

[23] CJEU 17 October 1996, C-283/94, Denkavit.
[24] Article 2 (a) (ii) PSD.
[25] Article 3 (a) (ii) IRD.
[26] A DTT may, for example, provide for a tax credit, a partial exemption or the exemption might be subject to the condition that the PE profits are effectively taxed.
[27] Article 44 BEFIT Proposal.

by a BEFIT member cannot benefit from a tax credit. Although Article 44, §1 BEFIT Proposal mentions that the tax credit would be given in line with DTTs, the additional requirements that are mentioned in Article 44, §2 and 3 may infringe the provisions on the avoidance of double taxation laid down in existing DTTs and may result in double taxation. In this respect, it is equally not clear how the BEFIT Proposal would deal with, for example, foreign real estate income that is generated without a PE being present and where the DTT foresees an exemption instead of a tax credit.

We believe that the primacy of secondary EU law over DTTs that Member States have concluded with third countries (even after 1958 or after the accession) and that introduce certain rights that taxpayers can rely upon, remains disputable. For purposes of tax certainty and to avoid double taxation, the BEFIT Proposal should address the relationship between both instruments and the European Commission should first discuss potential conflicts with third states.

### 1.4 Timing issues

As shown above, introducing the BEFIT Proposal in its current form would create a variety of corporate tax systems within the EU that would co-exist, i.e. national corporate income tax systems, Pillar Two rules and BEFIT. All these systems have a different scope, different rules to determine the tax base and different procedures to follow. At present, taxpayers and tax administrations are deploying a lot of resources to be compliant with the Pillar Two rules as of 2024 and many practical issues will still need to be resolved in the upcoming years. From a general timing perspective, requiring taxpayers and tax administrations to invest that soon after Pillar Two in another system seems too burdensome. It would be less far-reaching to first allow taxpayers and tax administrations time to gain experience with Pillar Two and, at a later stage, to propose rules for a harmonized tax base taking into account the lessons learned.

More specific timing issues can be raised as well. The BEFIT Proposal requires the filing entity to file a BEFIT information return within four months after the end of the fiscal year.[28] The BEFIT information return a.o. includes the BEFIT tax base which is based on financial accounts prepared on the basis of IFRS or national GAAP of the Member States. A BEFIT team will review the return and will endeavor to achieve consensus on certain aspects of the BEFIT information return within four months after filing the BEFIT information return.[29] If no consensus is reached within this timeframe, a consensus is deemed achieved if consent is given by simple majority within five months after filing the BEFIT information return. The filing entity will be notified. Each BEFIT group member shall subsequently file an individual tax return within three months after such notification.[30] If errors occur in the individual tax return that affect the BEFIT tax base, such errors must be notified within two months after filing the individual tax return. A revised BEFIT information return and, if need be, amended tax assessments must then be issued. Members States must apply the BEFIT Proposal as of 1 July 2028. This entire timeframe raises practical concerns.

[28] Article 57 BEFIT Proposal.
[29] Article 61 BEFIT Proposal.
[30] Article 62 BEFIT Proposal.

First, the timeframe presumes that approved financial statements are available very shortly after the end of the financial year. From a practical point of view, it does not seem feasible for all in-scope groups to have audited accounts available in the required financial accounting standard[31] and to prepare and file a BEFIT information return within a four-month timeframe.[32] In this respect, we would also like to emphasize that - depending on the accounting standard – companies might be required to report both (estimated) corporate income taxes and the entire Pillar Two position in their financial accounts. This requires that all computations of Top Up Taxes and Qualified Domestic Top Up Taxes are performed prior to the audit and approval of the accounts. It is a challenge to perform such an exercise in four months, potentially resulting in high penalties for MNEs if this strict deadline cannot be met.[33] A proposal that proves to be impracticable cannot possibly achieve the envisaged purpose of simplifying tax rules and stimulating growth and investments in the EU.

Furthermore, the Pillar Two rules require companies to report accurate estimates of the corporate income taxes in the financial accounts to avoid that an entire re-computation of the Top Up Tax must be performed.[34] The four-month timeframe increases the risk of errors and thus of material differences between the actual corporate income tax to be paid under BEFIT and the estimated corporate income tax as reported in the accounts. These differences might create enormous additional administrative burdens under Pillar Two for MNEs.

We would therefore recommend extending the filing deadline.

Finally, we would also recommend implementing new rules at the start of a financial year (which is typically 1 January) and not in the middle of a financial year as mentioned in article 78 of the BEFIT Proposal.

## 1.5 Interpretation of terms

[31] If the UPE is a tax resident in a third state, Article 7, §2 BEFIT Proposal requires that the financial accounting income or loss of each BEFIT group member is derived from accounts based on the accounting standard applicable in the Member State where the filing entity is a tax resident. The entities that form part of such a group in the EU may not be familiar with this accounting standard and it may add a layer of complexity and compliance burden. Assume, for example, that a group with a UPE in the United States has various entities in the EU. The group prepares consolidated financial accounts based on US GAAP. The group selects a Belgian group entity as the filing entity. This Belgian entity prepares financial statements in Belgian GAAP. Article 7, §2 seems to imply that all entities that are resident in other EU member States will also be required to prepare accounts in Belgian GAAP for BEFIT purposes only. These entities will probably still need to prepare accounts in their own local GAAP for local accounting purposes and may not be familiar with other local GAAPs in the EU.

[32] Please note that the laws of many Member States allow a longer period to (approve and) publish financial statements, which is also in accordance with Directive 2013/34/EU setting a maximum period of 12 months.

[33] Article 72 BEFIT Proposal.

[34] If the final tax liability in a jurisdiction differs from the amount of Covered Taxes in the accounts (due to errors or incorrect estimates of the tax liability), article 4.6.1 of the Model Rules and article 25 of the Pillar Two Directive require a group to recalculate the ETR and Top Up Tax if the Covered Taxes materially decrease in a jurisdiction.

Various terms are used in the BEFIT Proposal that lack a proper definition. It is, for example, not clear what should be understood by the concepts "revenues"[35], "subject to tax", "demerger", "merger", "permanent establishment"[36], "direct business interest", "beneficial owner" or "short term". There is a need for definitions of terms to ensure a consistent application of a new common corporate income tax system across the EU as this increases tax certainty for taxpayers and tax administrations. In addition, the BEFIT Proposal also lacks guidance on many other aspects thereby leaving multiple questions unanswered and making the application thereof in practice difficult. In this respect, it is for example not clear how to calculate the €750m threshold if no consolidated financial statements are available in the four years preceding the fiscal year, where a dual resident company is a tax resident for purposes of the BEFIT Proposal, what currency conversion rules to apply[37] and how to apply the allocation key if group members reported losses in the past three years.

The BEFIT Proposal intends to create a single set of corporate tax rules to enhance tax certainty and less tax disputes.[38] However, setting clear corporate tax rules is an indispensable condition to achieve these objectives. Vague rules create uncertainties and increase compliance costs for taxpayers since more specialized advice will be needed to ensure compliance or to assist the taxpayer in disputes with tax authorities and may lead to penalties if the interpretation that was adopted appears not to be correct. The many questions currently arising must first be resolved to avoid that the BEFIT proposal becomes ineffective and inefficient.[39]

This gap can be addressed by providing more definitions and technical guidance. In this respect, it should also be clarified whether the terms used have an autonomous EU meaning or whether references should be made to other sources, such as the financial accounting standards, national tax systems or the Pillar Two rules. With respect to the latter, it is apparent that certain wording used in the BEFIT Proposal is derived from the Pillar Two rules, but it is uncertain to what extent the definitions used in the Pillar Two rules and the related explanations given in the OECD commentary and Administrative Guidance can play a role in the interpretation of the BEFIT Proposal. The OECD remains working on further Administrative Guidance to clarify the interpretation and application of the Pillar Two rules. It can be expected that more issues will arise in the future and that more Pillar Two guidance will be prepared in the coming years. Also from this perspective, we believe that the BEFIT

[35] Under Pillar Two it was deemed necessary to further clarify the definition of revenues: Tax Challenges Arising from the Digitalisation of the Economy – Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two), December 2023.
[36] Par. 7 Preamble BEFIT Proposal mentions that one should rely on the existing DTTs and national rules of Member States. First, it is preferred to include a definition in the Directive itself. Second, it remains unclear what this implies if divergent definitions apply in DTTs and national law. Assume, for example, that a PE is not deemed present in a Member State according to a DTT with a third state but is deemed present according to the national law of the Member State. Would this PE be considered subject to a corporate tax in accordance with Article 2, (c) of the BEFIT Proposal? Or would the national law definition only become relevant if no DTT exists?
[37] Although Article 42, §3 does include conversion rules for the preliminary tax result, no conversion rules are included to calculate for example the €750m threshold.
[38] Par. 5 Preamble BEFIT Proposal.
[39] According to the OECD, uncertainty in the tax system has a significant impact on investment decisions by companies: IMF/OESO, *Tax certainty. Report for the G20 finance ministers*, March 2017, www.oecd.org/tax/tax-policy/tax-certainty-report-oecd-imf-report-g20-finance-ministers-march-2017.pdf, 25.

Proposal comes too soon, and businesses and tax administrations should be given some breathing space to become familiar with the complex Pillar Two rules for which Administrative Guidance is currently still an ongoing process at the OECD level. Although reference to the OECD Guidance could be a possibility, we note that this may also raise legitimacy concerns (especially if some Administrative Guidance goes beyond a mere clarification).

## 2 SPECIFIC COMMENTS WITH RESPECT TO THE BEFIT PROPOSAL

Without being exhaustive, we address in this section more technical issues, questions and unclarities with respect to the scope and the administrative procedure of the BEFIT Proposal with the aim to encourage the European Commission to re-examine the intricate technical parts of the entire BEFIT Proposal.

### 2.1 Scope

#### 2.1.1 *Group*

According to Article 3(1) of the BEFIT Proposal, a Group is defined as a "*collection of entities which are related through ownership or control as defined by the acceptable financial accounting standard for the preparation of consolidated financial statements by the ultimate parent entity, including any entity that may have been excluded from the consolidated financial statements of the ultimate parent entity solely based on its small size, on materiality grounds or on the grounds that it is held for sale*."

First, it is not entirely clear in this context what is meant with "acceptable financial accounting standard"[40] and what the consequence would be if the UPE would not use an acceptable financial accounting standard for the preparation of the consolidated accounts, especially in situations where the UPE is a tax resident in a third country.

Second, the BEFIT Proposal applies to companies that are resident in a Member State that belong to a (domestic or MNE) group which prepares consolidated financial statements and has combined revenues of at least €750m. The question arises whether the revenues of entities that are not consolidated due to materiality or size or since they are held for sale should be included to calculate the €750m threshold. Based on a literal reading, it could be argued that this question should be answered in the positive, since these entities belong to a group and the text does not as such refer to the revenues in the consolidated financial statements. Such entities, however, do not appear to be

[40] The BEFIT Proposal only provides a definition of "acceptable accounting standard in the Union" which is limited to IFRS or the general acceptable principles in the Member States.

part of the BEFIT group since they are not consolidated on a line-by-line basis, which is a separate condition laid down in Article 2, §1(b) (iii).

Under the Pillar Two rules, the definition of a group is similar, but the scope is worded slightly differently.[41] Based on the OECD Commentary, it could be argued that only the revenues that are reported in the consolidated financial accounts must be considered for the calculation of the €750m threshold. However, entities that are not consolidated based on their small size, on materiality grounds or on the grounds that they are held for sale are constituent entities under the Pillar Two rules.

The question thus arises whether this opposite result is intentional, and if so, what the underlying reasons for such outcome would be.

### 2.1.2 *Corporate residence*

As part of the scope, Article 2, §1 indicates that the directive applies to companies that are resident for tax purposes in a Member State. Member States often apply multiple criteria to define tax residency, which can lead to a situation that a company is considered a tax resident in more than one Member State (a so-called dual resident company). In addition to the abovementioned issues in relation to the application of DTTs (*supra* section 1.3), it is also not clear how the BEFIT Proposal should apply to dual resident companies. The question arises, for example, how to allocate the tax base to dual resident companies and how to identify the correct filing authority. We suggest explicitly addressing this in the BEFIT Proposal.

### 2.1.3 *Demerger*

As already mentioned above, the meaning of the term ‘demerger’ in the BEFIT Proposal is not clear. The language used in the Pillar Two rules and the BEFIT Proposal are very similar although the wording is not entirely the same which causes some confusion. Moreover, the Pillar Two rules create some uncertainty since the text of the Pillar Two rules is not consistent with the Pillar Two Commentary. It should be avoided that this inconsistency is transferred to the BEFIT Proposal. To explain our concern, we have compared the wording of both instruments and applied the rules to an example for which reference is made to the Annex.

### 2.1.4 *75%-threshold*

As a general observation with respect to the 75%-threshold, we note that it would be logical from a structural point of view to include both article 5 and article 6 in the scope provisions of Chapter I.

From a more substantive perspective, we are curious to understand why this 75% threshold has been introduced. As a result of this threshold, the compliance burden remains high as groups will have to

[41] Article 1.1.1. OECD Pillar Two rules: “*The GloBE Rules apply to Constituent Entities that are members of an MNE Group that has annual revenue of EUR 750 million or more in the Consolidated Financial Statements of the Ultimate Parent Entity (UPE) in at least two of the four Fiscal Years immediately preceding the tested Fiscal Year*.”

consider various corporate income tax systems that will co-exist. In addition, the application of this threshold raises various practical questions. Article 6, §2 of the BEFIT Proposal stipulates that a company becomes a BEFIT group member on the day that the threshold is reached but does not specifically consider the amount of financial net income or loss to be taken into account (pursuant to Article 7 BEFIT Proposal) and on the application of the adjustments (pursuant to a.o. section 2 of the BEFIT Proposal) in such case. [42] Moreover, it is unclear why a nine-month requirement is introduced and how this should be interpreted. Assume, for example, that the UPE of a group, which is in scope of BEFIT and accounts per calendar year, acquires 75% of the ownership of company Z in December of FY X. Should company Z be considered a BEFIT group member for FY X even though the 75% participation is not yet held for more than nine months in year X? If so, what happens if the UPE sells the shares in June X+1, i.e. within nine months but after the tax return filing deadline of Article 57, §2 BEFIT Proposal has passed? A group might be faced with an increased administrative burden if it would be required to file a revised BEFIT information return while the purpose of the nine-month requirement is not obvious.

### *2.2 Administration and procedures*

#### 2.2.1 *BEFIT information return*

According to Article 57 BEFIT Proposal, the filing entity shall file the BEFIT information return which must comprise the listed items and which must be filed within four months. For comments on this timing, reference is made to section 1.4.

If errors occur in the BEFIT information return, the filing entity must notify the filing authority within two months of the timely submission of the BEFIT information return pursuant to Article 58 of the BEFIT Proposal. The filing authority shall then transmit a revised BEFIT information return to the competent authorities of all Member States of other BEFIT group members. We would like to understand why this possibility is limited to two months only[43] and what happens if the filing entity identifies an error after this two-month period. Assume, for example, that a BEFIT group member A that accounts per calendar year acquires the shares of a subsidiary in September of FY X and receives a dividend from this subsidiary in December FY X. The shares are not yet held for more than one year at the time the dividend is distributed. In the assumption that the Denkavit doctrine of the CJEU can be applied[44], BEFIT group member A may possibly already exclude the dividend in accordance with Article 8 of the BEFIT Proposal for the relevant year. However, if the shares are ultimately not held for one year, the filing entity will voluntarily need to amend the BEFIT information

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[42] Section 5 BEFIT Proposal contains some specific rules for entering the BEFIT group and Article 55, § 2 and 3 BEFIT Proposal contains specific rules with respect to the allocation mechanism when companies join a group. Article 6, §2 and 3 BEFIT Proposal on the one hand and section 5 and Article 55, § 2 and 3 BEFIT Proposal on the other hand do not entirely seem consistent though since the former article refers to days whereas the later refers to months in certain instances.
[43] Especially since the individual tax returns only need to be filed within three months after the notification from the filing authority pursuant to Article 61 BEFIT Proposal which implies that the individual tax returns will only need to be submitted within 11 or 12 months after the end of the financial year.
[44] CJEU 17 October 1996, C-283/94, Denkavit. See *supra* Section. 1.2.

return even if the two-month period has expired.[45] The filing entity does, however, not seem to have such a possibility without incurring penalties. An appeal against the content of the BEFIT information return does not appear possible either as this possibility is currently limited to the situation that no BEFIT information return was filed.[46]

### 2.2.2 *BEFIT team*

A BEFIT team will be established consisting of one or more representatives of each relevant tax administration. This team will need to examine the completeness and accuracy of the information mentioned in the BEFIT information return. The BEFIT team will endeavour to reach consensus within four months on (a) the identification of the filing entity and BEFIT group members, (b) the information on the group structure, (c) the relevant fiscal year and (d) information regarding the baseline allocation percentage. If consensus is reached, these aspects cannot be subject to any future challenge.

A consensus can definitively contribute to the commendable goal to increase tax certainty and to reduce tax disputes. However, the question remains whether consensus implies that an administrative appeal or juridical appeal on these aspects is not possible anymore and whether such impossibility is only directed to the tax authorities or also to the BEFIT group members. If taxpayers are not permitted to question the accuracy of these aspects at a later stage, this may go against the taxpayers' fundamental right to defense and to an effective remedy before the tribunal.

If a consensus by unanimity is not reached, a consensus is deemed achieved if BEFIT team members give their consent by simple majority. To reach simple majority, the voting rights shall be allocated to each competent authority in the BEFIT team in proportion to the revenues earned in the relevant fiscal year by the BEFIT group members in their territory. The quorum requires the presence of at least two third of the BEFIT team members. If the quorum is not reached the initially filed BEFIT information return shall form the basis for the individual tax returns. This rule seems overly complex and raises various questions: what should be understood by 'revenues', how should this rule be applied in case an error is discovered or revenues change upon a later tax audit, and will the BEFIT information return also form the basis if the quorum is reached but not the simple majority? Moreover, it is not clear what procedure to follow if the BEFIT team intends to agree on an amendment to be made to the BEFIT information return. In such case, it would be appropriate to give the BEFIT group the possibility to express its point of view.

Although consensus has certainly the potential to reduce disputes and increase tax certainty for taxpayers, it remains at present uncertain whether this goal will effectively be achieved if the BEFIT team is not obliged to reach consensus. Considering that the accuracy of the elements to decide upon is not extremely difficult to verify and to effectively achieve the goal of increasing tax certainty and reducing tax dispute, we suggest (a) removing the simple majority rule, (b) defining consensus in a simpler manner and (c) to foresee that consensus on the BEFIT information return is deemed

[45] If the filing entity would not yet be allowed to exclude the dividend and the one year holding period will ultimately be met, the filing entity will need to have the possibility to amend the BEFIT information return as well.
[46] See Article 59, 66 and 68 BEFIT Proposal.

achieved if the BEFIT team is unable to reach consensus within five months on the BEFIT information return as filed or on amendments thereto.

### 2.2.3 *Individual information return*

The BEFIT Proposal incorporates a hybrid one-stop-shop approach, which implies that a BEFIT information return must be filed by the filing entity and that an individual tax return must be filed by each BEFIT group member with its local tax authority. According to the BEFIT Proposal, the competent authorities of the Member States shall issue an individual tax assessment in accordance with the individual tax return. Where required, an amended tax assessment will be issued and if the BEFIT tax base is affected, a revised BEFIT information return shall be issued by the filing authority within one month. In such case, all relevant Member States need to issue amended tax assessments (unless the difference of the tax base does not exceed €10.000 or 1% of the BEFIT tax base). A similar procedure applies if an error in an individual tax return is notified by a BEFIT group member within two months of submission of such return.

As also mentioned in section 1.1, this approach may increase complexity and administrative burdens for in-scope groups and tax authorities considering the many tax returns to be filed, the many rules to consider due to the wide sovereignty of Member States to further adjust the allocable tax base and the potential many re-assessments to be made in case of adjustments to the individual tax return that affect the BEFIT tax base. To lower the administrative burden and to protect legal certainty, we would therefore recommend specifying the limited adjustments that Member States are allowed to make to the allocated taxable basis, to limit the events of re-assessments by raising the threshold and to clarify the consequences if a Member State would not agree with the amended tax assessment issued in another Member State and the revised BEFIT information return.

### 2.2.4 *Audits*

According to Article 65 of the BEFIT Proposal, the competent authorities of the Member State where an audit has taken place must inform the BEFIT team of the results of the audit if it affects the outcome of the allocation of the BEFIT tax base. The other members of the BEFIT team shall express their views within three months. Following the audit, the filing authority shall issue a revised BEFIT information return within a month. It is not clear how the possibility for members of the BEFIT team to express their views within three months relates to the issuance of the revised BEFIT information return within one month. For purposes of legal certainty, it should be clarified what the consequences and procedure would be if a member of the BEFIT team would not agree with the outcome of the tax audit.

### 2.2.5 *Appeals*

Although the BEFIT Proposal foresees rules to make an administrative or judicial appeal and thus considers the right to defense, such procedures are often costly and can be very time-consuming. In addition, contradictory outcomes cannot be ruled out if different procedures are running simultaneously in multiple Member States. For legal certainty and simplicity, we recommend adding a dispute resolution mechanism to the BEFIT proposal.

## 3 TRANSFER PRICING

The BEFIT Proposal stipulates that in the first seven fiscal years post-implementation (transition phase), transactions between entities that are subject to the BEFIT rules (i.e. intra-BEFIT group transactions) are considered to be priced at arm's length if they are considered to be in "a low-risk zone". The "low-risk zone" would cover the expense incurred / income earned by a BEFIT group member from an intra-BEFIT group transaction that increases by less than 10% compared to the average amount of the income or expense in the previous three fiscal years. If this threshold is exceeded, the transaction is presumed not to be consistent with the arm's length principle, unless the BEFIT group member can provide evidence that the relevant intra-BEFIT group transaction was priced in accordance with the arm's length principle. These aspects raise some concerns.

*10%-threshold*

The 10%-threshold seems to be aimed at combatting undesirable tax planning arrangements, which is as such a legitimate objective. We note, however, that multiple situations exist whereby the amount of intercompany expenses or income would already soon exceed the above described 10% threshold and where there is clearly no undesirable tax planning arrangement (i.e., an increase of expenses due to organic growth or economic downturn, inflation or realization of efficiencies). We believe that for purposes of realizing the objective of the BEFIT Proposal, the 10%-threshold is too strict and should in our view be reconsidered (see also our remarks in relation to the burden of proof).

*Burden of proof*

Many countries have adopted a legal transfer pricing related framework, whereby taxpayers are obliged to prepare (contemporaneous) transfer pricing documentation and whereby non-compliance leads to a reversal of the burden of proof and/or penalties. This in our view provides a solid division between the position of the taxpayer (who is in a position to provide factual evidence/explanation in relation to the arm's length character of its intra-group transactions) and (ii) the tax administration who should be in a position to assess the arm's length character of the prices for the intra-group transaction. If the taxpayer meets the documentation requirements, it is in our view appropriate that it is initially up to a tax administration to 'proof' that the pricing of the transactions cannot be considered arm's length to avoid situations whereby taxpayers (continuously) have to "proof" that a price for a transaction can be considered arm's length. In this respect, it should also be noted that the OECD Transfer Pricing Guidelines acknowledge that it can be difficult to determine this (see e.g. paragraphs 2. - 4. and 11. of the preface of the OECD Transfer Pricing Guidelines).

Within most of the Member States, the above-mentioned legal framework was further harmonized after the implementation of Action 13 of the BEPS project and exists already for multiple years. It should also be mentioned that the aim of the proposed TP Directive[47] is to further harmonize the interpretation of the ‘arm’s length principle” and to further develop common approaches. Shifting the burden of proof to the taxpayer is in breach of the commonly implemented legal framework. In our view, there is no solid substantiation for this reversal and we would recommend to align the risk assessment framework with common approaches.

## 4 INTERACTION PILLAR TWO DIRECTIVE AND BEFIT PROPOSAL

Pillar Two rules aim to end the so-called race-to-the bottom by ensuring that in-scope MNEs pay a minimum tax of 15% in each jurisdiction they operate in. If the effective tax rate (**ETR**) is lower than 15% in a certain jurisdiction, a Top Up Tax in principle becomes due. To calculate the ETR per jurisdiction, the adjusted covered taxes of all constituent entities in a jurisdiction on the one hand and the GloBE income or loss of all constituent entities in a jurisdiction on the other hand are aggregated.

The BEFIT Proposal blends the net income or loss of all Member States and, after several adjustments, divides the BEFIT tax base – if any – among the BEFIT group members through a formula that is based on the average taxable result of the BEFIT group member in the three previous years compared to the average taxable result of the BEFIT group.

The interaction between these different sets of rules can create situations of over taxation as illustrated by the following two examples. This is due to the fact that the Top Up Tax under Pillar Two is calculated on the basis of the (adjusted) financial net income or loss realized in a jurisdiction which differs from the BEFIT tax base that is allocated to a jurisdiction under the BEFIT Proposal.

Example 1: A Co is the UPE of the Group and tax resident in Member State A. The Group has a consolidated revenue exceeding €750m each year and is in scope of both the Pillar Two rules as well as the BEFIT Proposal. In the EU the Group has three other entities that are tax resident in Member State X, Y and Z respectively. The corporate income tax rates and taxable income or loss[48] are as follows[49]:

| **Rate** | **A Co** | **X Co** | **Y Co** | **Z Co** |
|---|---|---|---|---|
| CIT Rate | 20% | 15% | 20% | 25% |
| **Financial Year** | **A Co** | **X Co** | **Y Co** | **Z Co** |
| X – 3 | 150 | 300 | 150 | 10 |

[47] Proposal for a Council Directive on Transfer Pricing, COM(2023) 529 (12 Sept. 2023).
[48] For purposes of this example, the financial income is assumed to be equal to the taxable income which is on its turn assumed to be equal under local CIT, Pillar Two and BEFIT.
[49] In this example, unit rounding is used. This may result in minor rounding differences.

| | | | | |
|---|---|---|---|---|
| X – 2 | 250 | 100 | 200 | 20 |
| X – 1 | 150 | 350 | 150 | 40 |
| X | 200 | 500 | 100 | 100 |
| **Pillar Two without BEFIT in FY X** | **A Co** | **X Co** | **Y Co** | **Z Co** |
| CIT | 40 | 75 | 20 | 25 |
| ETR Pillar Two | 20% | 15% | 20% | 25% |
| Top Up Tax | 0 | 0 | 0 | 0 |
| **Pillar Two with BEFIT in FY X** | **A Co** | **X Co** | **Y Co** | **Z Co** |
| Allocation key | 29%[50] | 40%[51] | 27%[52] | 4%[53] |
| Allocated BEFIT tax base | 261[54] | 360[55] | 243[56] | 36[57] |
| CIT | 52 | 54 | 49 | 9 |
| ETR Pillar Two | 26%[58] | 11%[59] | 49%[60] | 9%[61] |
| Top Up Tax | 0 | 20[62] | 0 | 6[63] |

The example shows that mismatches arise between the Pillar Two rules and BEFIT due to the BEFIT allocation key resulting in a higher ETR for the Group under BEFIT (i.e. approx. 21%) than under the current rules without BEFIT (i.e. approx. 18%).

[50] The average of the taxable results in 3 previous years of A Co equals 183 (i.e. (550/3). The average of the taxable results of all BEFIT group members equals 623.
[51] The average of the taxable results in 3 previous years of X Co equals 250 (i.e. (750/3). The average of the taxable results of all BEFIT group members equals 623.
[52] The average of the taxable results in 3 previous years of Y Co equals 167 (i.e. (500/3). The average of the taxable results of all BEFIT group members equals 623.
[53] The average of the taxable results in 3 previous years of Z Co equals 23 (i.e. (70/3). The average of the taxable results of all BEFIT group members equals 623.
[54] 29% x 900 BEFIT taxable basis in FY X (i.e. 200 + 500 + 100 + 100).
[55] 40% x 900 BEFIT taxable basis in FY X.
[56] 27% x 900 BEFIT taxable basis in FY X.
[57] 4% x 900 BEFIT taxable basis in FY X.
[58] 52 taxes / 200 GloBE income in FY X.
[59] 54 taxes / 500 GloBE income in FY X
[60] 49 taxes / 100 GloBE income in FY X
[61] 9 taxes / 100 GloBE income in FY X
[62] 4% (15%-11%) x 500 GloBE income.
[63] 6% (15% - 9%) x 100 GloBE income.

Example 2: the facts are the same as for example 1, with the sole exception that Y Co and Z Co are loss-making in financial year X.[64]

| Rate | A Co | X Co | Y Co | Z Co |
|---|---|---|---|---|
| CIT Rate | 20% | 15% | 20% | 25% |
| **Financial Year** | **A Co** | **X Co** | **Y Co** | **Z Co** |
| X – 3 | 150 | 300 | 150 | 10 |
| X – 2 | 250 | 100 | 200 | -20 |
| X – 1 | 150 | 350 | -150 | - 40 |
| X | 200 | 500 | -100 | -150 |
| **Pillar Two without BEFIT in FY X** | **A Co** | **X Co** | **Y Co** | **Z Co** |
| CIT | 40 | 75 | 0 | 0 |
| ETR Pillar Two | 20% | 15% | - | - |
| Top Up Tax | 0 | 0 | 0 | 0 |
| **Pillar Two with BEFIT in FY X** | **A Co** | **X Co** | **Y Co** | **Z Co** |
| Allocation key | 37%[65] | 50%[66] | 13%[67] | 0%[68] |

[64] In this example, unit rounding is used. This may result in minor rounding differences.

[65] The average of the taxable results in 3 previous years of A Co equals 183 (i.e. (550/3). As mentioned above in section 1.5, it is not entirely clear how to apply the allocation key if group members reported losses in the past three years. In particular, it is not clear whether the negative average result of Z Co (amounting to 17) must be considered to calculate the average of the taxable results of all BEFIT group members or whether this negative average result must also be set at zero following Article 45, §2 a. To avoid illogical results, we have assumed for the purpose of this example that it must be set at zero, although the BEFIT Proposal does not explicitly foresee this. The average of the taxable results of all BEFIT group members equals 500 in that case.

[66] The average of the taxable results in 3 previous years of X Co equals 250 (i.e. (750/3). The average of the taxable results of all BEFIT group members equals 500.

[67] The average of the taxable results in 3 previous years of Y Co equals 67 (i.e. (200/3). The average of the taxable results of all BEFIT group members equals 500.

[68] According to Article 45, §2 a BEFIT group member with a negative taxable result shall have an allocation percentage of zero.

| | | | | |
|---|---|---|---|---|
| Allocated BEFIT tax base | 167[69] | 225[70] | 59[71] | 0 |
| CIT | 33 | 34 | 12 | 0 |
| ETR Pillar Two | 17% | 7% | - | - |
| Top Up Tax | 0 | 40[72] | 0 | 0 |

This example equally shows that a Top Up Tax is levied when applying the BEFIT Proposal whereas no Top Up Tax would be levied under the current rules. This is due to the loss relief among BEFIT group members and the BEFIT allocation key. This approach does not match with the principles of Pillar Two that verifies the ETR in a jurisdiction based on the income or loss realized in a jurisdiction. Although the ETR in both situations is more or less similar for the Group in this example (approx. 26%), Y Co and Z Co do not have tax losses carried forward under BEFIT, resulting in more taxes to be paid in the following years when these entities become profitable. Under the current rules, both Y Co and Z Co would have tax losses carried forward resulting in a deferred tax asset that the group is permitted to take into account for Pillar Two purposes at the minimum rate of 15%. From an overall perspective, the Group therefore is more highly taxed under BEFIT compared to the current rules. The Group would also be more highly taxed under BEFIT compared to the situation where the Group sets up the same operations in one Member State. The BEFIT Proposal therefore appears to stimulate what it intends to tackle, i.e. over taxation and a distortion of investment decisions. In discussing the interaction of the BEFIT Proposal with the Pillar Two rules, the Impact Assessment is in our view not correct when stating that "*the sequencing between BEFIT and Pilar 2 is quite straightforward*" and that "*the design of a new system like BEFIT will be able to align with features of Pillar 2*".[73]

In these circumstances, it is questionable whether the BEFIT Proposal brings significant benefits to businesses.[74] We therefore encourage the European Commission to properly consider all facts and circumstances and to first discuss these issues with both the OECD as well as all third states that have implemented the Pillar Two rules as these states may be required to amend their national legislation. Until these issues are addressed globally, we would recommend limiting the BEFIT Proposal to the harmonization of the rules that determine the taxable basis.

[69] 37% x 450 BEFIT taxable basis.
[70] 50% x 450 BEFIT taxable basis.
[71] 13% x 450 BEFIT taxable basis.
[72] 8% (15%-7%) x 500 GloBE income.
[73] Impact Assessment p 120-121.
[74] The calculations do not seem to properly consider the interaction with Pillar Two: Impact Assessment p. 43.

**ANNEX: EXAMPLE DEMERGER**

***Comparison of the wording regarding a demerger in the Pillar Two rules and the BEFIT Proposal***

| **Pillar Two rules** | **BEFIT Proposal** |
|---|---|
| (c) Where a single MNE Group within the scope of the GloBE Rules demerges into two or more Groups (each a demerged Group), the consolidated revenue threshold is deemed to be met by a demerged Group:<br>i. with respect to the first tested Fiscal Year ending after the demerger, if the demerged Group has annual revenues of EUR 750 million or more in that year;<br>ii. with respect to the second to fourth tested Fiscal Years ending after the demerger, if the demerged Group has annual revenues of EUR 750 million or more in at least two of the Fiscal Years following the year of the demerger. | 5. Where there is a demerger of a group into two or more groups (the 'demerged groups'), the threshold of EUR 750 000 000 referred to in paragraph 1 shall be deemed to be met by each of the demerged groups where:<br>(a) in the first fiscal year ending after the demerger, each of the demerged groups has annual combined revenues of EUR 750 000 000 or more in that fiscal year;<br>(b) in the second to fourth fiscal years ending after the demerger, each of the demerged groups has annual combined revenues of EUR 750 000 000 or more in at least two of those fiscal years |
| **OECD Commentary Pillar Two rules** | |
| • First year following the demerger<br><br>34. Under subparagraph (i), the consolidated revenue threshold set out in Article 1.1 is deemed to be met by a demerged Group if the demerged Group has annual revenues of EUR 750 million or more in the first tested fiscal year after the demerger. This means that instead of applying a test that considers previous fiscal years, this rule is triggered for each demerged Group that has annual revenues of EUR 750 million or more in the Fiscal Year that is being tested. Note that this paragraph only applies to demerged Groups. The sale of a controlling interest in a single Entity will therefore not fall within the scope of paragraph (c).<br>35. Sub-paragraph (i) applies to a Group in the Fiscal Year "ending after the demerger". For example, Assume Group A has a Fiscal Year that is the same as the calendar year. The UPE of Group A distributed all of the shares of subgroup B to its shareholders in 30 June of Year 1. This distribution will be considered a demerger under Article 6.1.3 and result in the creation of Group B. The Fiscal Year of Group A ends on the 31 of December of Year 1. In this | |

| | |
|---|---|
| case, paragraph (i) tests Group A's consolidated revenue for Year 1 because it is the first tested Fiscal Year that ends after the demerger. Paragraph (i) also tests Group B's consolidated revenue for its first tested Fiscal Year that ends after the demerger. Thus, if Group B adopts or retains the calendar year as its Fiscal Year, paragraph (i) will apply to its Fiscal Year ending 31 December of Year 1 because that is Group B's first tested year that ends after the demerger. However, because Group B's first tested Fiscal Year is composed of a period other than 12 months, then the EUR 750 million threshold has to be adjusted proportionally consistent with Article 1.1.2.<br><br>• Second and subsequent years following demerger<br><br>36. Paragraph (ii) provides the rule for the second to fourth tested Fiscal Years after a demerger. It states that the consolidated revenue threshold set out in Article 1.1 is deemed to be met by a demerged Group if it has annual revenues of EUR 750 million or more in at least two Fiscal Years following the demerger. As for paragraph (i), this rule takes into account the annual revenue of the Fiscal Year that is being tested. For example, a demerged Group meets the test in the second Fiscal Year (i.e. the tested Fiscal Year), if it has consolidated revenues of EUR 750 million or more in Fiscal Years 1 and 2 following the demerger. | |

***Example of a demerger under the BEFIT Proposal***

Z Co is the UPE of the Group Z. On 1 July of Year X, Group Z demerges creating the Group W. Z Co remains the UPE of Group Z. W Co is the UPE of Group W. The consolidated revenue of Group Z and group W are as follows:

| Year | Group Z | Group W |
|---|---|---|
| X – 5 | 730M | |
| X – 4 | 760M | |
| X – 3 | 720M | |
| X – 2 | 730M | |

| | | |
|---|---|---|
| X – 1 | 750M | |
| X | 400M | 390M |
| X + 1 | 750M | 200M |
| X + 2 | 650M | 170M |
| X + 3 | 770M | 220M |

- First year following the demerger

The year that ends after the demerger could be interpreted in two ways: on the one hand it could be interpreted as referring to the year in which the demerger took place from a legal point of view. On the other hand, it could be interpreted as the year that ends after the year of the demerger. According to the OECD Commentary on Pillar Two, year X is the first year that ends after the merger. The year that ends after the demerger is in other words the year of the demerger.

The consolidated revenue of Group Z is not equal to at least €750M in Year X. The fact that the "two out of four year" threshold is met for Group Z seems irrelevant.[75] Therefore, the Pillar Two rules will in principle not apply to Group Z in Year X.

Group W's financial year in that case runs from 1 July until 31 December. The revenue of Group W has to be recalculated (since it only covers 6 months). A €375M threshold applies (€750M / 2) and therefore Group W would be subject to the Pillar Two rules in Year X.

The BEFIT Proposal does not provide further guidance on how to apply the rules. We assume it is intended to have a similar outcome. However, the reference to 'combined' revenues raises uncertainties as it could be interpreted in such a way that the annual revenues of the separate groups should be combined. It is recommended that the wording is aligned with Pillar Two and the same guidance is added.

- Second and subsequent years following demerger

Under the Pillar Two rules uncertainty arises in these years, especially in the year following the year that the demerger took place. Reading the text in a strict manner, two interpretations are possible: (i) in Year X +1, Group Z could never be subject to the Pillar Two rules (since it considers two of the Fiscal Years following the year of the demerger) or (ii) the rules could apply retrospectively (i.e., only determined after Year X + 2 has lapsed). The first interpretation seems to be mostly in line with the text itself. Both interpretations seem nonetheless undesirable.

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[75] See the paragraph 34 to the Commentary to Article 6.1.1.(c) of the Pillar Two rules: "*This means that instead of applying a test that considers previous fiscal years, this rule is triggered for each demerged Group that has annual revenues of EUR 750M or more in the Fiscal Year that is being tested.*"

The OECD Commentary seems to take another interpretation which appears more logical but which is contrary to the wording of the Pillar Two rules as it also considers the year of the demerger: "*a demerged Group meets the test in the second Fiscal Year (i.e. the tested Fiscal Year), if it has consolidated revenues of EUR 750 million or more in Fiscal Years 1 and 2 following the demerger*." Note that Fiscal year 1 is the year of the demerger in the example given in the Commentary. In this interpretation, the Pillar Two rules would also not apply in this specific example in the first year after the demerger since the threshold is not met in year X. In year X + 2 the Pillar Two rules do not apply for both group Z and W since the threshold is not met in at least two years following the demerger. In year X + 3 the Pillar Two rules do not apply for group W but do apply for group Z since Group Z meets the €750M threshold in at least two years following the demerger. Group Z likely only knows it is in scope of the Pillar Two rules in Year X + 3 after the year has lapsed.

As mentioned above, the BEFIT Proposal does not provide further guidance and the reference to 'combined' revenues raises uncertainties. Moreover, due to the uncertainty under the Pillar Two rules, it would be recommended to clarify the text of the BEFIT proposal. Moreover, the example shows that a group might only know it is in scope after the year has elapsed, which also shows the above-mentioned timing difficulties if a BEFIT tax return must be filed within 4 months.

In addition, it should also be clarified how these rules interact with the provision that the BEFIT group is governed by the Directive for a period of five years.[76]

[76] Article 54, § 1 BEFIT Proposal.