

Editorial

EU Budgetary Reform and Tax Harmonization: Becoming Brothers in Arms

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The ongoing COVID-19 crisis is bringing EU-wide harmonization of national tax systems and a reform of the EU budgetary system, in particular its financing through so-called 'own resources', closer together. The political compromise reached by the European Council in July 2020 was followed by a Council Decision and an Interinstitutional Agreement in December 2020, paving the way for the creation of new own resources. In 2021, the Commission has tabled several proposals both for new own resources and for the harmonization of direct taxes, with a first link between the two. Expectations are high that 2022 will become a decisive year for the future of the fiscal landscape within the EU.

1 INTRODUCTION

On 15 July 2020 the European Commission had published a 'Tax Package for fair and simple taxation supporting the recovery strategy' (i.e., the strategy proposed by the Commission for the EU and its Member States to recover from the fallout of the COVID-19 crisis¹) comprising, next to a Communication on 'Tax good governance' and a proposal to extend the obligations for automatic exchange of information under the Directive on Administrative Cooperation (DAC)² to operators of digital platforms, a comprehensive 'Action Plan for fair and simple taxation supporting the recovery strategy'.³ In the latter, the Commission had announced certain 'flagship initiatives', such as the increased use of 'environmental taxes' (including the introduction of a Carbon Border Adjustment Mechanism, or CBAM) and the publication, before the end of 2020, of an 'Action Plan for Business Taxation for the 21st century' following the

OECD/G20 discussions regarding a minimum level of effective taxation for the digitalized economy.

Only a few days later the heads of State or government of the EU Member States, during an extraordinary summit in Brussels, had reached a political compromise not only with respect to the Multiannual Financial Framework (MFF) for 2021–2027 (representing an overall EU budget of slightly more than one trillion euros for these seven years) and a special recovery instrument 'NextGenerationEU' (representing an additional amount of 750 billion euros in grants and loans), but also concerning the reform of the EU 'own resources' system.⁴ The European Council announced that this reform would include the creation of new own resources in the form of a levy on non-recycled plastic waste (to be introduced as of 1 January 2021) and of contributions to the EU budget on the basis of a CBAM and a 'digital levy' (both to be introduced at the latest by 1 January 2023), for which Commission proposals were to be delivered until mid 2021; likewise, the Commission was invited to propose revised, and possibly extended, rules on an EU Emission Trading System (ETS) for greenhouse gas emission allowances.⁵

After further and lengthy negotiations, this political compromise was followed by a Council Decision of 14 December 2020 on the system of own resources⁶ which provided for a 'uniform call rate' of EUR 0.80/kilogram (or EUR 800 per tonne) to the weight of unrecycled plastic packaging waste generated annually in each Member State (Recital 7 and Article 2(1)(c)) and stated that the Commission would 'put forward in the first semester of 2021 proposals on a carbon border adjustment mechanism and on a digital levy with a view to their introduction at the latest by 1 January 2023'

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¹ See in this respect, inter alia, Communication COM(2020) 456 of 27 May 2020, 'Europe's moment: Repair and Prepare for the Next Generation'.

² Council Directive 2011/16/EU of 15 Feb. 2011 on administrative cooperation in the field of taxation, OJ 2011 L 64/1.

³ Communication COM(2020) 312 of 15 July 2020, 'An Action Plan for fair and simple taxation supporting the recovery strategy'.

⁴ Conclusions of the European Council of 21 July 2020, EUCO 10/20.

⁵ The current system is still based on Directive 2003/87/EC of the European Parliament and of the Council of 13 Oct. 2003 establishing a system for greenhouse gas emission allowance trading within the Union and amending Council Directive 96/61/EC, OJ 2003 L 275/32, which has been amended several times.

⁶ Council Decision (EU, Euratom) 2020/2053 of 14 Dec. 2020 on the system of own resources of the European Union and repealing Decision 2014/335/EU, Euratom, OJ 2020 L 424/1.

(Recital 8). Another two days later an Interinstitutional Agreement was concluded between the European Parliament, the Council of the EU and the Commission with respect to various budgetary matters, including a 'roadmap towards the introduction of new own resources' which, firstly, confirmed the introduction of a new own resource in the form of 'a share of revenues from national contributions calculated on the weight of non-recycled plastic packaging waste' as of 1 January 2021 and, secondly, provided that the Commission would put forward proposals on a CBAM, on a 'digital levy' and on the introduction of new own resources on that basis by June 2021.⁷

2 BUDGETARY REFORM TAKING THE LEAD: PLASTIC WASTE-RELATED NATIONAL CONTRIBUTIONS AS NEW OWN RESOURCE OF THE EU

It is true that, taking into account the rather ambitious timelines envisaged by the EU institutions, it was almost unavoidable that not everything would run as smoothly as planned. Delays in negotiations at the level of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), which had been established in June 2016 with a view to, inter alia, preparing a potentially global implementation of Action 1 of the October 2015 final BEPS report,⁸ led the Commission to postpone the publication of its vision of 'Business Taxation for the 21st century'. Moreover, national ratification of the Own Resources Decision by all Member States, required under Article 311(3) of the Treaty on the Functioning of the European Union (TFEU), encountered certain hindrances within the domestic legal orders.⁹ Yet, the latter hindrances were overcome and

ratification processes completed during the course of May 2021, so that the Own Resources Decision (and with it the whole NextGenerationEU recovery instrument) could finally enter into force on 1 June 2021 with retroactive effect as of 1 January 2021, the same day on which also a Council Regulation of 30 April 2021 on the calculation of the plastic packaging waste-related new own resource and the practicalities of its payment by Member States to the Commission retroactively entered into force.¹⁰

Even though the EU revenue to be raised through this new own resource is not exceptionally high¹¹ (and may even decrease over time if the purpose of reducing plastic waste is actually reached¹²), it is not insignificant, either, and the fact alone that this new resource has been created must be regarded as a major breakthrough in EU budgetary policy, in particular since this step is closely linked with EU environmental policy.¹³ Nevertheless, it should also be clear that this new own resource is not linked with the introduction of an 'EU plastic levy' or 'EU plastic tax',¹⁴ and neither is there any harmonization of domestic plastic levies or taxes in this respect. Rather, Member States will be obliged to pay annual contributions to the EU budget based on Eurostat data which they need to collect anyway,¹⁵ and it is up to each

see order of 8 June 2021, 2 BvE 4/21, and press release no. 48/2021 of 17 June 2021 (both available in German at <https://www.bundesverfassungsgericht.de>; accessed 13 Feb. 2022).

⁷ Interinstitutional Agreement of 16 Dec. 2020 between the European Parliament, the Council of the European Union and the European Commission on budgetary discipline, on cooperation in budgetary matters and on sound financial management, as well as on new resources, including a roadmap towards the introduction of new own resources, Annex II, Part A nos 4 and 5, OJ 2020 L 433 I/28.

⁸ See OECD/G20 Base Erosion and Profit Shifting Project, *Action 1: 2015 Final Report – Addressing the Tax Challenges of the Digital Economy* (<https://www.oecd-ilibrary.org>; accessed 13 Feb. 2022).

⁹ Problems had come up, inter alia, in Germany where Parliament (*Bundestag*) and the Federal Council (*Bundesrat*) had approved the Own Resources Decision on 25 and 26 Mar. 2021, but already on 26 Mar. 2021 the Federal Constitutional Court (*Bundesverfassungsgericht*) had ordered the preliminary suspension of the ratification process due to a constitutional complaint brought on that day by more than 2,200 individual complainants led by, among others, the founder of right-wing party *Alternative für Deutschland* (AfD); see press release no. 23/2021 of 26 Mar. 2021 (available in German at <https://www.bundesverfassungsgericht.de>; accessed 13 Feb. 2022). A few weeks later, however, the Constitutional Court repealed this decision and rejected any further preliminary injunction against the domestic ratification process; see order of 15 Apr. 2021, 2 BvR 547/21, and press release no. 29/2021 of 21 Apr. 2021 (both available in English at <https://www.bundesverfassungsgericht.de>; accessed 13 Feb. 2022). The constitutional complaint as such is still pending, though, and the same goes for an action brought by the parliamentary party of the AfD against the German ratification act, although an injunction in the latter case has meanwhile been rejected by the Constitutional Court;

¹⁰ See Art. 16 of Council Regulation (EU, Euratom) 2021/770 of 30 Apr. 2021 on the calculation of the own resource based on plastic packaging waste that is not recycled, on the methods and procedure for making available that own resource, on the measures to meet cash requirements, and on certain aspects of the own resource based on gross national income, OJ 2021 L 165/15. Further accompanying measures were Council Regulation (EU, Euratom) 2021/769 of 30 Apr. 2021 amending Regulation (EEC, Euratom) No 1553/89 on the definitive uniform arrangements for the collection of own resources accruing from value added tax, OJ 2021 L 165/9, and Council Regulation (EU, Euratom) 2021/768 of 30 Apr. 2021 laying down implementing measures for the system of own resources of the European Union and repealing Regulation (EU, Euratom) No 608/2014, OJ 2021 L 165/1.

¹¹ Pursuant to the Commission's initial proposal COM(2018) 325 of 2 May 2018 for a 'Council Decision on the system of Own Resources of the European Union', para. 3.3, and based on data available at that time, the amount was estimated to be 'around EUR 7 billion per year', i.e., ca. 4% of the annual EU budget (*ibid.*, para. 3.4).

¹² See European Court of Auditors, Opinion No 5/2018 on the Commission's proposals COM(2018) 325, 326 and 328, para. 43, OJ 2018 C 431/1.

¹³ See generally in this respect Commission Communication COM (2019) 640 of 11 Dec. 2019 on 'The European Green Deal', paras 2.1.3 and 2.2.1. See more specifically with regard to plastic waste also Commission Communication COM(2018) 18 of 18 Jan. 2018 on 'A European Strategy for Plastics in a Circular Economy'.

¹⁴ The idea of a separate 'EU plastic tax' had in fact been hinted at in Jan. 2018 by (then) Commissioner of Budget Oettinger, but was dropped afterwards. See also Commission proposal COM(2018) 325, *supra* n. 11, para. 3.3.

¹⁵ Data collection is required under European Parliament and Council Directive 94/62/EC of 20 Dec. 1994 on packaging and packaging waste, OJ 1994 L 365/10 (with subsequent amendments), and Commission Implementing Decision (EU) 2019/665 of 17 Apr. 2019 amending Decision 2005/270/EC establishing the formats relating to the database system pursuant to European Parliament

Member State to decide whether to reserve a part of its own general budget for this payment obligation or to introduce a domestic tax or levy for refinancing purposes.

3 BUT TAX HARMONIZATION IS CATCHING UP

While EU budgetary reform thus took the lead, it can be expected that EU tax harmonization will follow up quickly, given the enormous efforts the Commission is making to push matters ahead. And what is more, the links between both areas are growing stronger.

3.1 The Commission's Communication on 'Business Taxation for the 21st Century'

To begin with, the long-awaited Communication on 'Business Taxation for the 21st Century', which was finally adopted by the Commission on 18 May 2021,¹⁶ truly marks a milestone in EU tax policy. On the one hand, it places the EU's future approach to business taxation in the wider context of global social and economic changes and of EU policies addressing these changes, such as the New Industrial Strategy¹⁷ and the Capital Markets Union,¹⁸ but also the digital agenda¹⁹ and, in particular, the 'Green Deal'.²⁰ On the other hand, the Communication pays considerable heed to the changing international tax landscape and the work of the OECD/G20 Inclusive Framework, but ultimately strives to go (much) further than the latter. Under the heading of an 'EU tax mix on the road to 2050' the Commission basically invites Member States to completely rethink their current tax systems to render them 'future-proof'. However, against the background of globalization and digitalization of economic transactions, which the Commission itself takes as the starting point of its contemplations, it remains to be seen whether the proclamation of 'fairness, efficiency and simplicity' as guiding principles for a future EU tax system²¹ will prove to be more than just wishful thinking.

At least as far as simplicity is concerned, one does not gain the impression that the measures the Commission has in mind for the near future will make life for tax-payers and tax administrations any easier. Sticking closely to the 'roadmap' of the Interinstitutional Agreement of December 2020 (*supra* at 1), the Commission announced proposals for new own resources supposed to contribute to the repayment of the 'NextGenerationEU' recovery instrument: It promised a first set of proposals, including 'proposals for a CBAM, a digital levy and a revision of the EU ETS', for July 2021, but at the same time made clear that further proposals for additional new own resources would follow and 'could include a Financial Transaction Tax and an own resource linked to the corporate sector'.²² And beyond these proposals with a direct link to the EU budget as new own resources, the Commission even announced 'further measures in the area of business taxation in both the short and longer term', comprising actions 'over the next two years' and a plan 'for the decades to come'.²³

As the first measure on its agenda the Commission identified an immediate reaction to the OECD/G20 Inclusive Framework's work on the reform of the existing international corporate tax landscape. Still expecting that a 'global and consensus-based solution' was within reach by mid-2021, the Commission announced that it would act quickly once a global agreement was on the table. As regards 'Pillar 1', i.e., an agreement on the (partial) reallocation of the taxing rights concerning profits of multinational enterprises (MNEs), the Commission considered a Directive necessary to ensure consistent implementation in all EU Member States. And with respect to 'Pillar 2', i.e., an agreement on an effective minimum level of taxation for MNEs, the Commission likewise expressed its clear preference for a Directive as the 'principal method' for implementing the new OECD model rules in the EU, albeit with certain adjustments in order to guarantee compatibility with primary EU law.²⁴

In addition, the Commission already outlined the next steps of its tax harmonization plans that will be 'Going beyond the OECD agreement'. The first steps will consist of 'targeted solutions' whose core elements will be a new proposal for the 'annual publication of the effective corporate tax rate of certain large companies with operations in the EU' ('Action 1'; by 2022)²⁵ and

and Council Directive 94/62/EC on packaging and packaging waste, OJ 2019 L 112/26.

¹⁶ Communication COM(2021) 251 of 18 May 2021 on 'Business Taxation for the 21st Century'.

¹⁷ See Commission Communications COM(2020) 102 of 10 Mar. 2020 on 'A New Industrial Strategy for Europe', and COM(2021) 350 of 5 May 2021, 'Updating the 2020 New Industrial Strategy: Building a stronger Single Market for Europe's recovery'.

¹⁸ See Commission Communications COM(2015) 468 of 30 Sept. 2015 on 'Action Plan on Building a Capital Markets Union', and COM(2020) 590 of 24 Sept. 2020 on 'A Capital Markets Union for people and businesses – new action plan'.

¹⁹ See Commission Communications COM(2020) 67 of 19 Feb. 2020 on 'Shaping Europe's digital future', of 9 Mar. 2021 and, more specifically with respect to small and medium sized enterprises (SMEs), COM(2020) 120 of 10 Mar. 2020 on 'An SME Strategy for a sustainable and digital Europe'.

²⁰ See Commission Communication COM(2019) 640, *supra* n. 13.

²¹ Communication COM(2021) 251, *supra* n. 16, para. 1.2.

²² *Ibid.*

²³ *Ibid.*, para. 1.3.

²⁴ *Ibid.*, para. 2.2. On the relevance of the fundamental freedoms in this respect, see L. De Broe & M. Massant, 'Are the OECD/G20 GloBE Rules Compliant with the Fundamental Freedoms', EC Tax Rev. 86–98 (2021); J. Englisch, 'Designing a Harmonized EU-GloBE in Compliance with Fundamental Freedoms', EC Tax Rev. 136–142 (2021); *id.*, 'Non-harmonized Implementation of a GloBE Minimum Tax: How Member States Could Proceed', EC Tax Rev. 208 at 209 et seq. (2021); C. De Pietro, 'The GloBE Income Inclusion Rule and Its Global Character: Complexities underlying Its Fully Effective Application', EC Tax Rev. 220 at 228 et seq. (2021).

²⁵ Communication COM(2021) 251, *supra* n. 16, para. 3.1.

a new legislative initiative ‘to neutralise the misuse of shell entities for tax purposes’ (‘Action 2’; by fourth quarter of 2021),²⁶ and furthermore also a proposal ‘to address the debt-equity bias in corporate taxation’ through the creation of a ‘Debt-Equity Bias Reduction Allowance (DEBRA)’ (‘Action 4’; by first quarter of 2022).²⁷ The additional element of a Recommendation on the (domestic) ‘tax treatment of losses’ of, in particular, small and medium sized enterprises (SMEs) by EU Member States (‘Action 3’),²⁸ issued together with the Communication already on 18 May 2021, actually looks a bit lost in this whole context.

And last but not least, the Commission sketched its long-term goal, that is the creation of ‘An EU Business taxation environment for the 21st Century’ (‘Action 5’, by 2023)²⁹: The Commission intends to build on the progress made at the OECD/G20 level concerning (large) MNEs, but to go even further than ‘Pillar 1’ and ‘Pillar 2’ by proposing ‘a new framework for income taxation for businesses in Europe (Business in Europe: Framework for Income Taxation or BEFIT)’. This BEFIT initiative is supposed to take the form of ‘a single corporate tax rulebook for the EU, based on the features of a common tax base and the allocation of profits between Member States on a formula (formula apportionment)’, going beyond ‘Pillar 1’ in the sense that the new allocation rules would cover the whole taxable base within the Single Market, rather than merely a residual profit. BEFIT is intended to make transfer pricing rules redundant and to replace the CCCTB proposal which, despite its ‘revival’ in 2016,³⁰ never made substantial headway.

3.2 The Commission Has Already Started to ‘Deliver’

While the Commission’s July 2020 ‘Action Plan for fair and simple taxation supporting the recovery strategy’ (*supra* at 1) with its twenty-five action points³¹ (‘propose and implement until 2024’) was already quite ambitious, it is almost dwarfed by the initiatives proclaimed in the Communication on ‘Business Taxation for the 21st Century’ of May 2021. And despite the tight timelines set, on the one hand, by the European Council (*supra* at 1) and, on the other, by the Commission itself (*supra* at 3.1), the Commission has indeed started to ‘deliver’ – first in

the area of environmental levies (in a broad sense), and then in the area of direct (business) taxation.

3.2.1 Proposals of 14 July 2021: ‘Fit for 55 package’

Already on 14 July 2021 the Commission published a large package of proposals related to the aim of reaching at least 55% emissions reduction (compared to 1990) by 2030,³² accompanied by a Communication titled “‘Fit for 55’: delivering the EU’s 2030 Climate Target on the way to climate neutrality”³³ including, inter alia, a proposal for a fundamentally revised Energy Tax Directive (ETD)³⁴ and two further proposals for EU legislative measures which would be complementing each other and have a direct link with the EU’s new system of own resources (*see infra* at 3.2.2.1).³⁵

The first of the latter two proposals concerns substantial amendments to the current trading system (ETS) for greenhouse gas emission allowances (*supra* at 1) with, inter alia, an extension to the maritime sector and the introduction of a ‘separate but adjacent’ trading system for the road transport and the building sectors.³⁶ The second proposal,³⁷ aiming at a Regulation based on Article 192(1) TFEU³⁸ and to be applied as of 1

³² See in this respect also Commission Communication COM(2020) 562 of 17 Sept. 2020, ‘Stepping up Europe’s 2030 climate ambition – Investing in a climate-neutral future for the benefit of our people’.

³³ Communication COM(2021) 550 of 14 July 2021, “‘Fit for 55’: delivering the EU’s 2030 Climate Target on the way to climate neutrality”.

³⁴ Proposal COM(2021) 563 of 14 July 2021 for a ‘Council Directive restructuring the Union framework for the taxation of energy products and electricity (recast)’, aimed at replacing Council Directive 2003/96/EC of 27 Oct. 2003 restructuring the Community framework for the taxation of energy products and electricity, OJ 2003 L 283/51, as of 1 Jan. 2023. The new proposal is now also based on Art. 192(2), 1st subparagraph, TFEU.

³⁵ See on this package already H. Kogels, ‘Good Intentions and a Call for Higher Speed on the Bumpy Road to Carbon Neutrality’, EC Tax Rev. 2–5 (2022).

³⁶ Commission proposal COM(2021) 551 of 14 July 2021 for a ‘Directive of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission trading allowance within the Union, Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation (EU) 2015/57’. The proposal is based on Art. 192(1) TFEU.

³⁷ Commission proposal COM(2021) 564 of 14 July 2021 for a ‘Regulation of the European Parliament and of the Council establishing a carbon border adjustment mechanism’.

³⁸ This would imply the application of the ordinary legislative procedure (Arts 289(1), 294 TFEU) with qualified majority voting in the Council and codecision by the European Parliament. If the Regulation were to be considered as containing ‘provisions primarily of a fiscal nature’, Art. 192(2), first subparagraph, TFEU would lead to the application of the special legislative procedure (Art. 289(2) TFEU) with unanimity in the Council and mere consultation of the European Parliament. In line with the ‘Legislative financial statement’ contained in COM(2021) 564, *supra* n. 37, para. 1.4.3 (‘revenue generation is not an objective of CBAM’), one may take the view, however, that fiscal or budgetary purposes only play a subordinate role in this respect, just like under the ETS system; see with respect to the latter the discussion by R. Ismer & M. Haussner, ‘Inclusion of Consumption into the EU ETS: The Legal Basis under

²⁶ *Ibid.*

²⁷ *Ibid.*

²⁸ See *ibid.* and Commission Recommendation C(2021) 3434 of 18 May 2021 ‘on the tax treatment of losses during the COVID-19 crisis’.

²⁹ Communication COM(2021) 251, *supra* n. 16, para. 4.

³⁰ See Proposals of 25 Oct. 2016 for Council Directives ‘on a Common Corporate Tax Base (CCTB)’, COM(2016) 686, and ‘on a Common Consolidated Corporate Tax Base (CCCTB)’, COM(2016) 683.

³¹ For an overview, see A. Cordewener, ‘The COVID-19 Crisis: An Opportunity for EU Budget and Tax Reform’, EC Tax Rev. 258 at 261 (2020).

January 2023, concerns the introduction of a CBAM (*supra* at 1) which, according to the Commission, ‘involves the application on imports of a system that replicates the ETS regime applicable to domestic production’ and ‘entails – similar to the system of allowances under the ETS – the surrendering of certificates (“CBAM certificates”) by importers based on embedded emission intensity of the products they import into the Union, and purchased at a price corresponding to that of the ETS allowances at any given point in time’.³⁹

3.2.2 Proposals of 22 December 2021: (New) Own Resources and Direct (Business) Taxation

Less than half a year later, on 22 December 2021, already the next proposals have been tabled by the Commission: A first package concerning measures related to the EU’s budget, and a second one focusing on direct (business) taxation.

3.2.2.1 New Own Resources from ETS, CBAM and ‘Pillar 1’

The package on budgetary matters comprises a Communication on ‘the next generation of own resources’⁴⁰ and proposals to amend both the Own Resources Decision⁴¹ and the MFF Regulation 2021–2027.⁴² Relying on the Interinstitutional Agreement of 16 December 2020 (*supra* at 1) that new own resources to be introduced after 2021 shall be used to finance the repayment of the NextGenerationEU recovery instrument, the Commission proposes a (first) ‘basket of new own resources’:

- First of all, 25% of the revenues generated under the revised ETS (*supra* at 3.2.1), with the exception of certain allowances auctioned by the European Investment Bank, are supposed to become a new own resource. Pursuant to the Commission’s estimate, this would bring ‘around EUR 9 billion per year over the period 2023–2030’ into the EU budget.⁴³

European Union Law’, *Review of European Community & International Environmental Law (RECIEL)* 69 at 73 et seq. (2016).

³⁹ See COM(2021) 564, *supra* n. 37, para. 3.

⁴⁰ Communication COM(2021) 566 of 22 Dec. 2021, ‘The next generation of own resources for the EU Budget’.

⁴¹ Proposal COM(2021) 570 of 22 Dec. 2021 for a ‘Council Decision amending Decision (EU, Euratom) 2020/2053 on the system of own resources of the European Union’.

⁴² Proposal COM(2021) 569 of 22 Dec. 2021 for a ‘Council Regulation amending Regulation (EU, Euratom) 2020/2093 laying down the multiannual financial framework for the years 2021 to 2027’.

⁴³ COM(2021) 566, *supra* n. 40, para. 2.1. How the Commission arrives at this amount is not fully clear, and the calculations are not very coherent. In its Press Release IP/21/7025 of 22 Dec. 2021 the Commission refers to an estimate of ‘around €12 billion per year on average over 2026–2030 (€9 billion on average between 2023–2030)’, and the initial proposal COM(2018) 325, *supra* n. 11,

- Secondly, 75% of the revenues generated by the CBAM (*supra* at 3.2.1) are likewise supposed to become a new own resource. In this respect, the Commission’s estimate is that ‘around EUR 0.5 billion per year over the period 2023–2030’ could enter the EU budget, taking into consideration that no revenue is expected to be generated during a transitional period from 2023 to 2025.⁴⁴
- And thirdly, the Commission puts forward the idea of creating a new own resource ‘equivalent to 15% of the share of the residual profits of the largest and most profitable multinational enterprises’ based on the reallocation rules under a future ‘Pillar 1 Directive’ (which the Commission had expressly included in its work programme for 2022⁴⁵). According to the Commission, the contribution to the EU’s budget resulting thereof ‘could amount to roughly between €2.5 and €4 billion per year’,⁴⁶ which would be considerably less than the amount the Commission had previously intended to raise via a 3% call rate applied to the CCCTB.⁴⁷

3.2.2.2 ‘Pillar 2 Directive’ and ‘Shell Directive’

The second package presented by the Commission on 22 December 2021 consists of two proposals aimed at protecting EU Member States’ revenue in the area of direct taxation. The first proposal concerns a Directive introducing measures to ensure a minimum level of effective corporate taxation of large groups of enterprises within the Single Market⁴⁸ and is an immediate (and extremely fast) reaction to the agreement on a ‘two-pillar solution’ reached by the OECD/G20 Inclusive Framework on BEPS on 8 October 2021⁴⁹

para. 3.2 (still based on 20% auction revenue of the current ETS) had estimated that ‘annual average revenues could vary between EUR 1.2 and 3.0 billion depending on the market price for EU Emission Trading System allowances’, before assuming an average of EUR 3 billion for 2021–2017 (*ibid.*, para. 3.4). See on the latter amount also Court of Auditors, *supra* n. 12, para. 37.

⁴⁴ COM(2021) 566, *supra* n. 40, para. 2.1. Again the calculation is not very clear, though. Press Release IP/21/7025 of 22 Dec. 2021 mentions an estimate of ‘around €1 billion per year on average over 2026–2030 (€0.5 billion on average between 2023–2030)’, and the ‘Legislative financial statement’ contained in COM(2021) 564, *supra* n. 37, para. 1.4.3 states that revenue ‘for 2030 is estimated at above EUR 2.1 billion’.

⁴⁵ See Commission Communication COM(2021) 645 of 19 Oct. 2021, ‘Commission work programme 2022 – Making Europe stronger together’, at 6 and Annex I, no. 17.

⁴⁶ COM(2021) 566, *supra* n. 40, para. 2.1. There is no indication which influence the BEFIT initiative planned for 2023 (see *supra* at 3.1) might have on this amount.

⁴⁷ See COM(2018) 325, *supra* n. 11, para. 3.1, where the Commission expected ‘an annual average of approximately EUR 12 billion’ over the period 2021–2027.

⁴⁸ Proposal COM(2021) 823 of 22 Dec. 2021 for a ‘Council Directive on ensuring a global minimum level of taxation for multinational groups in the Union’.

⁴⁹ See OECD/G20 Inclusive Framework on BEPS, *Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the*

and the subsequent publication of the Global Anti-Base Erosion (GloBE) Model Rules covering ‘Pillar 2’ on 20 December 2021.⁵⁰ The proposed ‘Pillar 2 Directive’ is intended to provide for a quick and consistent transformation of the global agreement into the domestic legislation of all EU Member States, paying heed to the ‘specifics’ of EU law (in particular, the fundamental freedoms; *see supra* at 3.1) by extending the GloBE approach beyond cross-border situations of multinational groups also to large-scale domestic groups; in both cases, a threshold of a combined group turnover of at least EUR 750 million applies.

In substance the proposal comprises two interlocked core rules⁵¹ designed to ensure that large groups of enterprises pay a minimum Effective Tax Rate (ETR) of 15% on their taxable income: The Income Inclusion Rule (IIR) checks whether this minimum level is reached in each jurisdiction where the group has activities through its constituent entities and, if the local ETR is below the minimum, triggers a ‘top-up tax’ at the level of the (ultimate or at least intermediate) parent entity, with an option for Member States with low-taxed constituent entities within their tax jurisdiction to apply a ‘top-up’ tax domestically; the IIR is supposed to become operational already as soon as 1 January 2023. The Undertaxed Payments Rule (UTPR), on the other hand, functions as a backstop for situations where the 15% minimum tax burden cannot be achieved via the IIR (e.g., because the (ultimate) parent is tax resident outside the EU in a jurisdiction which either does not apply a (qualifying) IIR at all or does not apply an IIR to the parent itself if that is the low-taxed entity), and it will trigger a ‘top-up tax’ in the hands of constituent entities located in EU Member States; the UTPR is meant to be applicable as from 1 January 2024. The timeline envisaged by the Commission for the adoption and national implementation of this Directive still in 2022 is, therefore, very tight, but the current French Council Presidency seems determined to push this matter with high priority.

The second proposal on tax matters concerns a Directive aimed at preventing the ‘misuse of shell entities for tax purposes’⁵² and had been announced by the Commission as (short-term) ‘Action 2’ in its Action Plan of May 2021 (*see supra* at 3.1). This proposal

responds to a request by the European Parliament to come forward with an initiative against ‘letterbox companies’⁵³ and is a reaction to the growing number of tax-related scandals involving numerous high net individuals and their hidden fortunes and investments,⁵⁴ but also to tax-planning strategies by multinationals with BEPS effects, and beyond tax avoidance and tax evasion even to money-laundering activities. The proposed Directive, sometimes already referred to as ‘ATAD 3’⁵⁵, is intended to apply to all ‘undertakings’ (regardless of their legal form, and without any particular income or turnover threshold) which are tax resident in a Member State, and to subject them to scrutiny as to whether they have ‘minimum substance for tax purposes’. Unfortunately, due to this inherent territorial limitation to the EU the big bulk of ‘shell entities’ in offshore jurisdictions⁵⁶ will not be subject to this test.

The test consists of a stepwise filtering process that would begin with a ‘gateway’ separating high-risk cases from low-risk cases by subjecting undertakings which fulfil three cumulative indicative conditions to reporting requirements: A reporting obligation is triggered if (1) more than 75% of the undertaking’s revenues accrue from geographically mobile activities (in particular, typical passive income such as dividends, interest and royalties, rental and financial leasing income, but also income from insurance and banking services), (2) the undertaking is predominantly engaged in ‘cross-border activity’ (as it has more than 60% of the book value of its assets abroad and generates at least 60% of its income through cross-border transactions), and (3) ‘the administration of day-to-day operations and the decision-making on significant functions’ have been sourced out; certain exemption would apply to, *inter alia*, domestic holdings within the same Member State and regulated financial undertakings. Only to (high-risk) cases passing through this gate the actual core ‘substance test’ would then be applied by requiring the undertakings concerned to report in their annual tax returns (with documentary evidence) whether another set of three criteria is fulfilled,

Digitalisation of the Economy (8 Oct. 2021), <https://www.oecd.org/tax/beps/statement-on-a-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.pdf> (accessed 13 Feb. 2022).

⁵⁰ See OECD/G20 Inclusive Framework on BEPS, *Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-base Erosion Model Rules* (20 Dec. 2021), <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.pdf> (accessed 13 Feb. 2022).

⁵¹ The Commission considers the third provision comprised by the GloBE Model Rules, the Subject to Tax Rule (STTR), as a mere treaty-based solution for which no EU action will be undertaken.

⁵² Proposal COM(2021) 565 of 22 Dec. 2021 for a ‘Council Directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU’.

⁵³ See European Parliament Resolution of 26 Mar. 2019 ‘on financial crimes, tax evasion and tax avoidance’ (2018/2121(INI)), Report on financial crimes, tax evasion and tax avoidance, P8_TA(2019)0240, OJ 2021 C 108/8, para. 2.7 (in particular, cons. 133 et seq.).

⁵⁴ In the ‘Explanatory Memorandum’ the Commission refers to the ‘OpenLux investigation’ and the ‘Pandora Papers’; *see* COM(2021) 565, *supra* n. 52, para. 1 in n. 4. But several others can, of course, be added, such as the ‘Panama Papers’, ‘Paradise Papers’ and, to some degree, also the ‘Football Leaks’.

⁵⁵ This despite the fact that the proposed Directive is not intended to further amend the existing Anti-Tax Avoidance Directives ‘ATAD 1’ and ‘ATAD 2’ (Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market, OJ 2016 L 193/1, and Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries, OJ 2017 L 144/1).

⁵⁶ *See e.g.*, the latest ‘EU list of non-cooperative jurisdictions for tax purposes’ adopted by the Council on 5 Oct. 2021, 12519/21 FISC 160 ECOFIN 939.

namely: (1) Whether the undertaking has premises in the Member State of its tax residence (either self-owned or 'for its exclusive use'), (2) whether it has 'at least one own and active bank account' in the EU, and (3) whether its directors and the majority of its full-time employees are present in the Member State concerned and qualified to exercise their tasks. Non-compliance with these reporting obligations would be subject to penalties which, pursuant to the proposal, would comprise 'an administrative pecuniary sanction of at least 5% of the undertaking's turnover in the relevant tax year'.

If, according to its declaration, the undertaking does not meet all of the aforementioned 'indicators', it would be presumed to lack 'minimum substance for tax purposes' for the relevant tax year unless it can rebut the presumption by providing further supporting evidence for its business activities that generate the critical mobile income. Where no such rebuttal is possible, the proposed Directive would oblige the Member State concerned to either refuse the issuance of a tax residence certificate to the enterprise for the relevant tax year, or to state in such a certificate that the undertaking cannot benefit from double taxation conventions and the relief provisions under the EU Parent-Subsidiary and Interest and Royalties Directives⁵⁷; other Member States, too, would have to disregard such conventions and relief provisions, and the Member State of the undertaking's shareholder(s) would have to treat the relevant income as if it had directly accrued to the latter. Considering the exclusion from tax relief under the aforementioned Directives, which due to the limitation of the proposed Directive's scope to 'undertakings' in EU Member States may become one of its most important areas of application, it is striking, though, that the proposal does not contain any reference at all to recent case-law by the Court of Justice of the EU (CJEU) on national anti-avoidance measures⁵⁸ and primary EU law principles on abuse of law.⁵⁹ Neither is there any explanation as to how the new Directive would relate to the General Anti-Abuse Rule (GAAR) under the Parent-Subsidiary Directive.⁶⁰

According to the Commission's proposal, the 'Shell Directive' would have to be transposed into domestic law until 30 June 2023 and to be applied as if 1 January 2024. It is accompanied by a proposal to amend the DAC (*see supra* at 1) with rules on the automatic exchange of information between national tax authorities of EU Member States concerning the information received by 'undertakings' under their reporting obligations, including potential evidence provided to rebut the presumption of a lack of 'minimum substance for tax purposes'.

4 FINAL REMARKS

As the developments above show, EU budgetary reform has made considerable progress, but tax harmonization is about to catch up, and the Commission's quest for suitable new own resources is bound to tie both areas closer together. And as regards business tax harmonisation, there is even more to come in the very near future: The Commission has already indicated that on 11 May 2022 'Action 4' of its May 2021 Communication (*supra* at 3.1) could follow in the form of a proposal for a Directive to tackle the 'debt-equity bias' in corporate taxation through the introduction of a 'DEBRA', i.e., a type of 'notional interest deduction' on corporate equity (rather than an elimination of the deductibility of actual interest payments on debt financing). Furthermore, while it can be expected that the project of a 'digital levy' (*supra* at 1 and 3.1), which stubbornly kept popping up in different forms on various occasions over the past few years, will now be buried in light of the recent OECD/G20 Inclusive Framework on BEPS's agreement on a 'two-pillar solution',⁶¹ the Commission has already put a proposal for a 'Pillar 1 Directive' (*supra* at 3.1) on its tentative agenda for 27 July 2022.

One thing is for sure: The EU business tax landscape will soon look very different, and the current year 2022 could become one of the most important years in 'EU tax history'. It will be interesting to see whether the Commission will try to profit from this and identify additional potential sources for new own resources. Since it has already proposed to let the Union budget participate in the reallocation of profits under a 'Pillar 1 Directive' (*supra* at 3.2.2.1), would

⁵⁷ Council Directive 2011/96/EU of 30 Nov. 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (recast), OJ 2011 L 345/8, and 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, OJ 2003 L 157/49.

⁵⁸ See e.g., CJEU of 20 Dec. 2017, Joined Cases C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, ECLI:EU:C:2017:1009; of 14 June 2018, C-440/17, *GS*, ECLI:EU:C:2018:437.

⁵⁹ See CJEU of 26 Feb. 2019, Joined Cases C-116/16 and C-117/16, *T Danmark et al.*, ECLI:EU:C:2019:135, and Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16, *N Luxembourg 1 et al.*, ECLI:EU:C:2019:134.

⁶⁰ During the preparation of Council Directive (EU) 2015/121 of 27 Jan. 2015 amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, OJ 2015 L 21/1, the Commission had explained that the new GAAR in Article 1(2) would apply to 'a letterbox company with no substance'; see

Memo/13/1040 of 25 Nov. 2013, 'Questions and Answers on the Parent Subsidiary Directive', example 1.

⁶¹ In its Communication COM(2021) 251, *supra* n. 16, para. 1.2, the Commission had still stated that in the EU such a levy would 'coexist with the implementation of an OECD agreement on sharing a fraction of the taxable base of the largest multinational enterprises, once the latter is ratified and transposed in EU law'. The statement issued by the OECD/G20 Inclusive Framework on BEPS on 8 Oct. 2021, *supra* n. 49, at 3, however, clearly expects the abolition of national digital services taxes.

the idea of claiming also a share in the national amounts of 'top-up taxes' under the 'Pillar 2 Directive' (*supra* at 3.2.2.2) really be too far-fetched? After all, the Commission has justified its recent proposal of a 'basket of new own resources' with, inter alia, the (rather bold) statement that '(t)hese

initiatives require EU action, and therefore constitute an appropriate base for EU own resources'⁶² - and the refinancing of the EU's COVID-19 expenses (*supra* at 1) is a tremendous task that requires ingenious solutions.

⁶² COM(2021) 566, *supra* n. 40, para. 2.1.