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

CHAPTER II

MEASURES AGAINST TAX AVOIDANCE

Article 4

Interest limitation rule

1 Exceeding borrowing costs shall be deductible in the tax period in which they are incurred only up to 30 percent of the taxpayer's earnings before interest, tax, depreciation and amortisation (EBITDA).

For the purpose of this Article, Member States may also treat as a taxpayer:

a an entity which is permitted or required to apply the rules on behalf of a group, as defined according to national tax law;

b an entity in a group, as defined according to national tax law, which does not consolidate the results of its members for tax purposes.

In such circumstances, exceeding borrowing costs and the EBITDA may be calculated at the level of the group and comprise the results of all its members.

2 The EBITDA shall be calculated by adding back to the income subject to corporate tax in the Member State of the taxpayer the tax-adjusted amounts for exceeding borrowing costs as well as the tax-adjusted amounts for depreciation and amortisation. Tax exempt income shall be excluded from the EBITDA of a taxpayer.

3 By derogation from paragraph 1, the taxpayer may be given the right:

a to deduct exceeding borrowing costs up to EUR 3 000 000;

b to fully deduct exceeding borrowing costs if the taxpayer is a standalone entity.

For the purposes of the second subparagraph of paragraph 1, the amount of EUR 3 000 000 shall be considered for the entire group.

For the purposes of point (b) of the first subparagraph, a standalone entity means a taxpayer that is not part of a consolidated group for financial accounting purposes and has no associated enterprise or permanent establishment.

4 Member States may exclude from the scope of paragraph 1 exceeding borrowing costs incurred on:

a loans which were concluded before 17 June 2016, but the exclusion shall not extend to any subsequent modification of such loans;

b loans used to fund a long-term public infrastructure project where the project operator, borrowing costs, assets and income are all in the Union.

For the purposes of point (b) of the first subparagraph, a long-term public infrastructure project means a project to provide, upgrade, operate and/or maintain a large-scale asset that is considered in the general public interest by a Member State.

Where point (b) of the first subparagraph applies, any income arising from a long-term public infrastructure project shall be excluded from the EBITDA of the taxpayer, and any excluded exceeding borrowing cost shall not be included in the exceeding borrowing costs of the group vis-à-vis third parties referred to in point (b) of paragraph 5.

5 Where the taxpayer is a member of a consolidated group for financial accounting purposes, the taxpayer may be given the right to either:

a fully deduct its exceeding borrowing costs if it can demonstrate that the ratio of its equity over its total assets is equal to or higher than the equivalent ratio of the group and subject to the following conditions:

(i) the ratio of the taxpayer's equity over its total assets is considered to be equal to the equivalent ratio of the group if the ratio of the taxpayer's equity over its total assets is lower by up to two percentage points; and

(ii) **[**[F1]all assets and liabilities are valued using the same method as in the consolidated financial statements drawn up in accordance with the International Financial Reporting Standards or the national financial reporting system of a Member State;**]**

or

b deduct exceeding borrowing costs at an amount in excess of what it would be entitled to deduct under paragraph 1. This higher limit to the deductibility of exceeding borrowing costs shall refer to the consolidated group for financial accounting purposes in which the taxpayer is a member and be calculated in two steps:

(i) first, the group ratio is determined by dividing the exceeding borrowing costs of the group vis-à-vis third-parties over the EBITDA of the group; and

(ii) second, the group ratio is multiplied by the EBITDA of the taxpayer calculated pursuant to paragraph 2.

6 The Member State of the taxpayer may provide for rules either:

a to carry forward, without time limitation, exceeding borrowing costs which cannot be deducted in the current tax period under paragraphs 1 to 5;

b to carry forward, without time limitation, and back, for a maximum of three years, exceeding borrowing costs which cannot be deducted in the current tax period under paragraphs 1 to 5; or

c to carry forward, without time limitation, exceeding borrowing costs and, for a maximum of five years, unused interest capacity, which cannot be deducted in the current tax period under paragraphs 1 to 5.

7 Member States may exclude financial undertakings from the scope of paragraphs 1 to 6, including where such financial undertakings are part of a consolidated group for financial accounting purposes.

[[F1]8 For the purposes of paragraphs 1 to 7, the taxpayer may be given the right to use consolidated financial statements prepared under accounting standards other than the International Financial Reporting Standards or the national financial reporting system of a Member State.**]**

Textual Amendments

F1 Substituted by Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.

Article 5

Exit taxation

1 A taxpayer shall be subject to tax at an amount equal to the market value of the transferred assets, at the time of exit of the assets, less their value for tax purposes, in any of the following circumstances:

a a taxpayer transfers assets from its head office to its permanent establishment in another Member State or in a third country in so far as the Member State of the head office no longer has the right to tax the transferred assets due to the transfer;

b a taxpayer transfers assets from its permanent establishment in a Member State to its head office or another permanent establishment in another Member State or in a third country in so far as the Member State of the permanent establishment no longer has the right to tax the transferred assets due to the transfer;

c a taxpayer transfers its tax residence to another Member State or to a third country, except for those assets which remain effectively connected with a permanent establishment in the first Member State;

d a taxpayer transfers the business carried on by its permanent establishment from a Member State to another Member State or to a third country in so far as the Member State of the permanent establishment no longer has the right to tax the transferred assets due to the transfer.

2 A taxpayer shall be given the right to defer the payment of an exit tax referred to in paragraph 1, by paying it in instalments over five years, in any of the following circumstances:

a a taxpayer transfers assets from its head office to its permanent establishment in another Member State or in a third country that is party to the Agreement on the European Economic Area (EEA Agreement);

b a taxpayer transfers assets from its permanent establishment in a Member State to its head office or another permanent establishment in another Member State or a third country that is party to the EEA Agreement;

c a taxpayer transfers its tax residence to another Member State or to a third country that is party to the EEA Agreement;

d a taxpayer transfers the business carried on by its permanent establishment to another Member State or a third country that is party to the EEA Agreement.

This paragraph shall apply to third countries that are party to the EEA Agreement if they have concluded an agreement with the Member State of the taxpayer or with the Union on the mutual assistance for the recovery of tax claims, equivalent to the mutual assistance provided for in Council Directive 2010/24/EU[(1)].

3 If a taxpayer defers the payment in accordance with paragraph 2, interest may be charged in accordance with the legislation of the Member State of the taxpayer or of the permanent establishment, as the case may be.

If there is a demonstrable and actual risk of non-recovery, taxpayers may also be required to provide a guarantee as a condition for deferring the payment in accordance with paragraph 2.

The second subparagraph shall not apply where the legislation in the Member State of the taxpayer or of the permanent establishment provides for the possibility of recovery of the tax debt through another taxpayer which is member of the same group and is resident for tax purposes in that Member State.

4 Where paragraph 2 applies, the deferral of payment shall be immediately discontinued and the tax debt becomes recoverable in the following cases:

a the transferred assets or the business carried on by the permanent establishment of the taxpayer are sold or otherwise disposed of;
b the transferred assets are subsequently transferred to a third country;
c the taxpayer's tax residence or the business carried on by its permanent establishment is subsequently transferred to a third country;
d the taxpayer goes bankrupt or is wound up;
e the taxpayer fails to honour its obligations in relation to the instalments and does not correct its situation over a reasonable period of time, which shall not exceed 12 months.

Points (b) and (c) shall not apply to third countries that are party to the EEA Agreement if they have concluded an agreement with the Member State of the taxpayer or with the Union on the mutual assistance for the recovery of tax claims, equivalent to the mutual assistance provided for in Directive 2010/24/EU.

5 Where the transfer of assets, tax residence or the business carried on by a permanent establishment is to another Member State, that Member State shall accept the value established by the Member State of the taxpayer or of the permanent establishment as the starting value of the assets for tax purposes, unless this does not reflect the market value.

6 For the purposes of paragraphs 1 to 5, ‘market value’ is the amount for which an asset can be exchanged or mutual obligations can be settled between willing unrelated buyers and sellers in a direct transaction.

7 Provided that the assets are set to revert to the Member State of the transferor within a period of 12 months, this Article shall not apply to asset transfers related to the financing of securities, assets posted as collateral or where the asset transfer takes place in order to meet prudential capital requirements or for the purpose of liquidity management.

Article 6

General anti-abuse rule

1 For the purposes of calculating the corporate tax liability, a Member State shall ignore an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the applicable tax law, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one step or part.

2 For the purposes of paragraph 1, an arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality.

3 Where arrangements or a series thereof are ignored in accordance with paragraph 1, the tax liability shall be calculated in accordance with national law.

Article 7

Controlled foreign company rule

1 The Member State of a taxpayer shall treat an entity, or a permanent establishment of which the profits are not subject to tax or are exempt from tax in that Member State, as a controlled foreign company where the following conditions are met:

a in the case of an entity, the taxpayer by itself, or together with its associated enterprises holds a direct or indirect participation of more than 50 percent of the voting rights, or owns directly or indirectly more than 50 percent of capital or is entitled to receive more than 50 percent of the profits of that entity; and

b the actual corporate tax paid on its profits by the entity or permanent establishment is lower than the difference between the corporate tax that would have been charged on the entity or permanent establishment under the applicable corporate tax system in the Member State of the taxpayer and the actual corporate tax paid on its profits by the entity or permanent establishment.

For the purposes of point (b) of the first subparagraph, the permanent establishment of a controlled foreign company that is not subject to tax or is exempt from tax in the jurisdiction of the controlled foreign company shall not be taken into account. Furthermore the corporate tax that would have been charged in the Member State of the taxpayer means as computed according to the rules of the Member State of the taxpayer.

2 Where an entity or permanent establishment is treated as a controlled foreign company under paragraph 1, the Member State of the taxpayer shall include in the tax base:

a the non-distributed income of the entity or the income of the permanent establishment which is derived from the following categories:

(i) interest or any other income generated by financial assets;

(ii) royalties or any other income generated from intellectual property;

(iii) dividends and income from the disposal of shares;

(iv) income from financial leasing;

(v) income from insurance, banking and other financial activities;

(vi) income from invoicing companies that earn sales and services income from goods and services purchased from and sold to associated enterprises, and add no or little economic value;

This point shall not apply where the controlled foreign company carries on a substantive economic activity supported by staff, equipment, assets and premises, as evidenced by relevant facts and circumstances.

Where the controlled foreign company is resident or situated in a third country that is not party to the EEA Agreement, Member States may decide to refrain from applying the preceding subparagraph.

or

b the non-distributed income of the entity or permanent establishment arising from non-genuine arrangements which have been put in place for the essential purpose of obtaining a tax advantage.

For the purposes of this point, an arrangement or a series thereof shall be regarded as non-genuine to the extent that the entity or permanent establishment would not own the assets or would not have undertaken the risks which generate all, or part of, its income if it were not controlled by a company where the significant people functions, which are relevant to those assets and risks, are carried out and are instrumental in generating the controlled company's income.

3 Where, under the rules of a Member State, the tax base of a taxpayer is calculated according to point (a) of paragraph 2, the Member State may opt not to treat an entity or permanent establishment as a controlled foreign company under paragraph 1 if one third or less of the income accruing to the entity or permanent establishment falls within the categories under point (a) of paragraph 2.

Where, under the rules of a Member State, the tax base of a taxpayer is calculated according to point (a) of paragraph 2, the Member State may opt not to treat financial undertakings as controlled foreign companies if one third or less of the entity's income from the categories under point (a) of paragraph 2 comes from transactions with the taxpayer or its associated enterprises.

4 Member States may exclude from the scope of point (b) of paragraph 2 an entity or permanent establishment:

a with accounting profits of no more than EUR 750 000, and non-trading income of no more than EUR 75 000; or
b of which the accounting profits amount to no more than 10 percent of its operating costs for the tax period.

For the purpose of point (b) of the first subparagraph, the operating costs may not include the cost of goods sold outside the country where the entity is resident, or the permanent establishment is situated, for tax purposes and payments to associated enterprises.

Article 8

Computation of controlled foreign company income

1 Where point (a) of Article 7(2) applies, the income to be included in the tax base of the taxpayer shall be calculated in accordance with the rules of the corporate tax law of the Member State where the taxpayer is resident for tax purposes or situated. Losses of the entity or permanent establishment shall not be included in the tax base but may be carried forward, according to national law, and taken into account in subsequent tax periods.

2 Where point (b) of Article 7(2) applies, the income to be included in the tax base of the taxpayer shall be limited to amounts generated through assets and risks which are linked to significant people functions carried out by the controlling company. The attribution of controlled foreign company income shall be calculated in accordance with the arm's length principle.

3 The income to be included in the tax base shall be calculated in proportion to the taxpayer's participation in the entity as defined in point (a) of Article 7(1).

4 The income shall be included in the tax period of the taxpayer in which the tax year of the entity ends.

5 Where the entity distributes profits to the taxpayer, and those distributed profits are included in the taxable income of the taxpayer, the amounts of income previously included in the tax base pursuant to Article 7 shall be deducted from the tax base when calculating the amount of tax due on the distributed profits, in order to ensure there is no double taxation.

6 Where the taxpayer disposes of its participation in the entity or of the business carried out by the permanent establishment, and any part of the proceeds from the disposal previously has been included in the tax base pursuant to Article 7, that amount shall be deducted from the tax base when calculating the amount of tax due on those proceeds, in order to ensure there is no double taxation.

7 The Member State of the taxpayer shall allow a deduction of the tax paid by the entity or permanent establishment from the tax liability of the taxpayer in its state of tax residence or location. The deduction shall be calculated in accordance with national law.

[F1 *Article 9*

Hybrid mismatches

1 To the extent that a hybrid mismatch results in a double deduction:

a the deduction shall be denied in the Member State that is the investor jurisdiction; and

b where the deduction is not denied in the investor jurisdiction, the deduction shall be denied in the Member State that is the payer jurisdiction.

Nevertheless, any such deduction shall be eligible to be set off against dual inclusion income whether arising in a current or subsequent tax period.

2 To the extent that a hybrid mismatch results in a deduction without inclusion:

a the deduction shall be denied in the Member State that is the payer jurisdiction; and

b where the deduction is not denied in the payer jurisdiction, the amount of the payment that would otherwise give rise to a mismatch outcome shall be included in income in the Member State that is the payee jurisdiction.

3 A Member State shall deny a deduction for any payment by a taxpayer to the extent that such payment directly or indirectly funds deductible expenditure giving rise to a hybrid mismatch through a transaction or series of transactions between associated enterprises or entered into as part of a structured arrangement except to the extent that one of the jurisdictions involved in the transaction or series of transactions has made an equivalent adjustment in respect of such hybrid mismatch.

4 A Member State may exclude from the scope of:

a point (b) of paragraph 2 of this Article hybrid mismatches as defined in points (b), (c), (d) or (f) of the first subparagraph of Article 2(9);

b points (a) and (b) of paragraph 2 of this Article hybrid mismatches resulting from a payment of interest under a financial instrument to an associated enterprise where:

(i) the financial instrument has conversion, bail-in or write down features;

(ii) the financial instrument has been issued with the sole purpose of satisfying loss absorbing capacity requirements applicable to the banking sector and the financial instrument is recognised as such in the taxpayer's loss absorbing capacity requirements;

(iii) the financial instrument has been issued

— in connection with financial instruments with conversion, bail-in or write down features at the level of a parent undertaking,
— at a level necessary to satisfy applicable loss absorbing capacity requirements,
— not as part of a structured arrangement; and

(iv) the overall net deduction for the consolidated group under the arrangement does not exceed the amount that it would have been had the taxpayer issued such financial instrument directly to the market.

Point (b) shall apply until 31 December 2022.

5 To the extent that a hybrid mismatch involves disregarded permanent establishment income which is not subject to tax in the Member State in which the taxpayer is resident for tax purposes, that Member State shall require the taxpayer to include the income that would otherwise be attributed to the disregarded permanent establishment. This applies unless the Member State is required to exempt the income under a double taxation treaty entered into by the Member State with a third country.

6 To the extent that a hybrid transfer is designed to produce a relief for tax withheld at source on a payment derived from a transferred financial instrument to more than one of the parties involved, the Member State of the taxpayer shall limit the benefit of such relief in proportion to the net taxable income regarding such payment.**]**

Textual Amendments

F1 Substituted by Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.

[F2 Article 9b

Tax residency mismatches

To the extent that a deduction for payment, expenses or losses of a taxpayer who is resident for tax purposes in two or more jurisdictions is deductible from the tax base in both jurisdictions, the Member State of the taxpayer shall deny the deduction to the extent that the other jurisdiction allows the duplicate deduction to be set off against income that is not dual-inclusion income. If both jurisdictions are Member States, the Member State where the taxpayer is not deemed to be a resident according to the double taxation treaty between the two Member States concerned shall deny the deduction.**]**

Textual Amendments

F2 Inserted by Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.

(**1**) Council Directive 2010/24/EU of 16 March 2010 concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures (OJ L 84, 31.3.2010, p. 1).