PLATAFORMA PYMES
Por un Capitalismo Inclusivo

CONPYMES
CONFEDERACIÓN NACIONAL DE PYMES

OECD PUBLIC CONSULTATION ON TAXATION TO MULTINATIONAL ENTERPRISES

On October 9, 2019 - The OECD published a proposal to ensure that multinational companies, including digital companies, pay their taxes at the locations where they provide services and obtain benefits.

Background

The Committee of Experts for the Reform of the Spanish Tax System, created by the Government of Spain, establishes four objectives for any Corporate Taxes reform (CT):

1. Recomposition of Tax Bases (TB), affected by exemptions and deductions.
2. Achieve a more balanced financing of the company's assets than is induced by the current system, by stimulating an increase in own resources and a reduction in indebtedness.
3. To prevent that profits from abroad not have a minimum taxation burden in Spain or in the country of origin.
4. Compensate previous reforms with significant reductions in nominal rates.

For their part, international economic organizations recommended four lines of action for this same reform:

1. Review of deductions, which significantly reduce effective taxation, resulting in Smes, even at a lower rate, bearing a higher effective rate than large companies.
2. Evaluation of the R&D deduction, whose efficiency does not seem to justify its tax cost.
3. Reconsideration of the existence of progressive types, which can generate disincentives for business growth.
4. Adoption of additional measures to reduce the bias introduced by the tax in favor of indebtedness. Since the interests paid to third parties are deductible from the TB, aggressive fiscal planning encourages over-indebtedness to reduce it. In this respect, in 2012, the deductibility of net financial expenses was limited, as a temporary measure, with a period of 18 years to recover the net financial expense not deducted.

The Commission of Experts for the Reform of the Spanish Tax System, following indications of international economic organizations, studied several alternatives to correct the bias to indebtedness:

a. Allowance Corporate Equity (ACE): consists of discounting, from the accounting results, the opportunity cost of own resources. The Commission points out, as a negative aspectof

the ACE, the risk of the budgetary consolidation, as it would lead to a reduction in the collection of the CT.

b. Maintenance of the current model, reducing, as Portugal did, from 18 to 5 years the term to recover the expenses not deducted. This possibility does not convince the Commission because it is inefficient to limit excessive indebtedness.

c. Elimination of the current limitation on the temporary deductibility of expenses, unableto recover the non-deducted financial expenses.

d. A formula that links the tax deductibility of net financial expenses to a balanced level of indebtedness driven solely by fiscal reasons; Spanish companies currently finance their total assets through own and third-party resources in a 35/65 proportion, according to the Commission, reaching a ratio of 50/50 (60/40 in the opinion of the IMF). This system eliminates the deduction of the net financial expenses corresponding to the external resources that exceed a maximum level which, following a pattern of gradual decrease towards the balance between sources of financing, is established each year for indebtedness with respect to total assets.

In October 2016, the European Commission presented a proposal to modify the Common Consolidated Corporate Tax Base (CCCTB), introducing the Allowance for Growth and Investment (AGI), which will allow a deduction of Corporate Tax for those companies that retain benefits or increase capital, applying a risk interest rate of 2.7% per year for 10 years on the withholding of profits or the capital increase.

In addition, there are also other fiscal guidelines set out by both the European Commission and the International Monetary Fund, which the SME Platform shares, based on:

1. Growth-friendly tax policies in the Member States (growth-friendly tax policies) and better coordination of taxes in the EU, issued on November 23, 2011 (com 2011 815 final).

2. Specific documents 119/2012 on possible reforms of real estate taxes: criteria for favorable policies, published in October 2012.

3. 2013 Objectives of the Annual Survey on Growth towards fair and competitive tax systems issued on November 28, 2012.

Positioning of Plataforma Pymes

Plataforma Pymes considers that any proposal in this field should be framed in a context that respects fiscal neutrality and meets public budgetary restrictions and its fiscal consolidation processes.

Therefore, any increase in the taxation of multinational companies is meaningless if there is no

reduction in corporate taxation of SMEs. One of the most effective ways to achieve the latter would be the reduction of taxation on the undistributed benefits of SMEs.

Plataforma Pymes recalls its positioning document on the Spanish Draft Law on Digital Services Taxes, which, among other issues, concluded:

> "… The inclusion of the taxation on certain digital services should not be an "easy" substitute for multinational anti-circumvention measures. For Plataforma Pymes these measures are necessary and must involve a reconsideration of the taxation of companies on SMEs, especiallyif this circumvention is protected in countries with low EU corporate taxation ..."

The improvement in the taxation of the undistributed benefits of SMEs would help to improve their non-bank financing from own resources. This is particularly important given the worsening financing conditions resulting from the adoption in December 2017 of the Basel III rules, which penalise SME bank financing against large companies, with external credit ratingratings.

For Plataforma Pymes, the OECD proposal should incorporate measures with respect to the CT, so that the taxable base of the tax coincides with the accounting result, thereby increasingthe total collection of the tax.

The reduction of corporate taxation to SMEs can be achieved through the introduction of Allowance Corporate Equity (ACE), following the proposed model of modification of the European Commission of the Common Consolidated Corporate Tax Base through its Allowance for Growth and Investment (AGI), which allows a deduction of CT to those companies that retain profits or increase capital.

The approach of the Committee of Experts regarding the desirability of the inclusion of the ACE, obviates the difficulties of access of small companies to bank financing. An exceptional non-bank financing action through own resources could consist of the introduction of an ACE so that the benefits not distributed and capitalized as Reserves, regardless of their use, had an effective rate on accounting result of 3.5%, comparable enjoyed by large companies in the previous Corporation Tax.

Consideration should also be given to the transposition in EU Member States of the ATA Anti-circumvention Directive, which provides for the establishment of a general anti-abuse standard, a new regime for international tax transparency, the treatment of so-called hybrid asymmetries, the limitation of the deductibility of interests and the regulation of so-called exittaxation.

In relation to this transposition, it should be remembered that the European Union has introduced the Controlled Foreign Company (CFC) rule. Through this mechanism, multinational companies that intend to divert benefits from the parent company in a country of high taxationto a subsidiary of low taxation to reduce the group's tax liabilities, may be offset by Member States through the CFC, provided that the tax is less than 40%. This will allow the incorporation of a specific anti-abuse clause in case the benefits distributed by the subsidiary are deductible expense for said branch in origin, as well as a general anti-abuse clause for schemes that only seek a tax advantage.