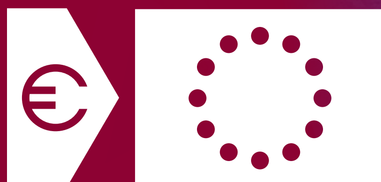

A short view

GDV positions on EU tax issues 2020

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The economic recovery from COVID-19, the transition towards a greener and more digitized economy and the necessity to remain competitive in a globalized world are the most pertinent challenges for the European Union in the coming years. A modern taxation system with secure tax revenues for the Member States is vital to respond to these challenges.

The German insurance industry appreciates that the European Parliament has set up a permanent subcommittee on taxation matters. Indeed, it is important that taxation issues are high on the agenda. Not only is it necessary to fight tax evasion and tax fraud but it is also indispensable to remove tax obstacles for EU companies in the Single Market.

With the new EU´s Tax Package (dated July 2020), the EU Commission outlines its policy and plan of how it intends to achieve both goals. The Tax Action Plan contains a set of 25 initiatives the European Commission will implement between now and 2024 to make taxation fairer, simpler and more adapted to modern technologies. Many of the Commission´s initiatives in its Tax Action Plan are most relevant for the insurance industry.

In this short paper, the German insurers give their views with eight key points regarding the EU tax policy.

GDV
DIE DEUTSCHEN VERSICHERER

1. Fair and simple taxation and tax good governance

Background:
With its tax package, the EU Commission aims to make taxation fairer and simpler. The EU Commission plans to reinforce tax transparency with a special focus on the platform economy. Furthermore, the Commission seeks to step up the fight against harmful tax practices. To this end, the Commission wants to reform the Code of Conduct and the listing of non-cooperative jurisdictions.

From an insurance perspective:
The insurance sector endorses the Commission´s objective of a fair and simple taxation. Businesses need a tax system which secures sufficient public revenues, creates a level playing field for businesses, minimizes aggressive tax planning opportunities and is accepted by the society as a whole. However, taxes should be easy to administer by tax authorities as well as businesses. Often, policy measures in the name of fair taxation come at the price of substantial compliance burden. Therefore, it is critical that the intended policy objective is thoroughly weighed against adverse consequences for taxpayers.

In particular, innovative tax measures should be introduced only with a sunset clause so that Member States are forced to review the efficacy of a given piece of legislation against the desired policy objective and any unexpected adverse effects.

An example for tax transparency legislation which is bound to cause a considerable compliance burden is the obligation to report tax planning schemes. To alleviate the burden and to avoid unintended over-reporting, the EU should draw up a white list of "low risk tax planning schemes." Furthermore, the legislation should be carefully reviewed in view of its suitability to achieve the desired objectives.

We fully support the Commission´s commitment to simplify tax rules. The plan to revise VAT rules governing financial services and the collection and refund process for withholding taxes are particularly relevant for the insurance sector.

Current VAT rules create a competitive distortion to the detriment of the insurance sector and should be reformed. The current legal situation and practice of levying withholding taxes is unsatisfactory. The refund procedure is administratively burdensome and an obstacle to cross border investments. We will articulate our position to both initiatives in more detail further below under section 5 (Withholding Taxes) and 6 (VAT).

Key points for an international tax reform

Global solution rather than unilateral measures

Minimized additional compliance burden

(e.g. applicability of European accounting standards)

Consideration of the characteristics of the insurance business model

(e.g. carve-out concept should take into account regulatory capital requirements)

Avoidance of double taxation

(e.g. clear prioritization of rule applicability, strengthened dispute resolution mechanisms)

Source: GDV

2. Digital Tax

Background:
Growing cross border business and the digitalization of the economy have revealed the necessity to modernize the international taxation rules. The EU is following a two-fold approach:

First, EU and Member States are working toward an agreement on a global solution at OECD level by the end of 2020. The global solution envisaged by the OECD consists of two pillars: a redistribution of taxation rights on company profits between countries (Pillar I) and the implementation of an effective global minimum taxation of company profits (Pillar II).

Second, if by the end of 2020 there is still no agreement, the EU is willing to act alone. In that case, the EU Council may revert to considering two draft directives proposed by the EU Commission already in 2018: one providing for new taxing rights of market states and one foreseeing an interim tax on certain revenue from digital activities.

From an insurance perspective:
The initiatives at EU level and OECD level will minimize the risk of unilateral solutions and excessive tax

competition. Issues of distribution of taxing rights between countries and a minimum taxation are issues that have to be tackled globally. Hence, any solution should be developed and agreed at the OECD rather than EU level. A reform of international taxation must not result in double taxation risks and unnecessary compliance burdens.

The reform discussed at OECD and EU level will inevitably result in additional compliance burden. Simplification options should be utilized such as whitelisting of countries with low risk of low taxation and de-minimis thresholds. Companies should not be imposed with the obligation to use IFRS accounting standards for purposes of complying with the new rules. Pre-existing rules with similar policy objectives (CFC rules, royalty or interest deduction disallowance rules, U.S. American BEAT and GILTI) should be repealed or at least turned off in instances where the minimum taxation applies.

Any carve-out scheme under Pillar I and II of the OECD project should take cognizance of the fact that the insurance business model is determined by regulation. Therefore, financial assets as required by local regulators should be recognized as giving rise to a carve-out under the minimum taxation rule. Investment and pension funds as well as investment holding entities they control should be excluded from the minimum taxation regime.

The Insurance sector should not be targeted by a redistribution of international taxing rights since current transfer pricing rules for cross border insurance business already lead to substantial taxation in market states.

Lastly, dispute resolution mechanisms should be strengthened.

3. CCCTB

Background:
With 27 Member States, it is challenging for the European economy with cross-border activities to comply with all of the different tax regimes. Therefore, the European Commission has relaunched in 2016 the Common Consolidated Corporate Tax Base (CCCTB). The CCCTB envisages a single set of rules for computing taxable income and the consolidation of tax bases across Member States.

The Commission had originally proposed the CCCTB in 2011, but that proposal proved too ambitious for Member States to agree in one go. Therefore the EU Commission pursues an incremental approach. As a first step the Common Corporate Tax Base (CCTB) is to be implemented followed by the introduction of the consolidation as the second step.

The consolidated taxable profits will be shared between the Member States in which the group is active, using an apportionment formula. Each Member State will then tax its share of the profits at its own national tax rate.

From an insurance perspective:
The insurance industry supports all measures that contribute to a fair and uniform taxation in the European market. It has to be kept in mind that without the implementation of the consolidation, the CCCTB is no real progress for the European market. For this reason the consolidation has to be implemented swiftly after the common base.

The CCCTB will help reduce tax compliance burden. For example, corporations can file one tax return for all of their EU activities. It will also increase legal certainty and curb aggressive tax planning.

The possibility to offset losses in one Member State against profits in another as foreseen in the interim prior to consolidation is an important step towards a real common market.

It is indispensable for the insurance industry that equalization provisions and other insurance business related provisions as provided by local commercial law are recognized under the CCTB. With regard to the valuation of technical provisions, it must be ensured that insurance companies can meet any liabilities arising out of insurance contracts as far as can reasonably be foreseen.

4. Financial Transaction Tax (FTT)

Background:
In spring 2020, Germany issued a revised proposal for a Council Directive regarding the introduction of a common financial transaction tax to the participating Member States in the so-called enhanced cooperation procedure (Germany, Austria, Belgium, France, Greece, Italy, Portugal, Slovakia, Slovenia and Spain). The revised proposal includes an optional exemption for pension schemes and a new system for mutualisation of the FTT revenues. Germany is pursuing to achieve an agreement to adopt an FTT by the end of this year.

Taxation of the financial sector has been under discussion at European level since 2011, when the European Commission first proposed implementing an FTT in the EU. After initial discussions, it became apparent that unanimous support amongst EU Member States for the proposal did not exist.

From an insurance perspective:
An FTT would run counter to the European Commission's stated goal of strengthening Europe as a business and investment location. None of the models for an FTT discussed so far would succeed in avoiding a negative impact on the economy and employment. The FTT is a burdensome tax impeding the trade in stock markets and impacting negatively on the real economy overall. In the insurance sector, the costs of the FTT will push up insurers' expenses and will inevitably diminish investment returns for policyholders, notably those who have signed contracts designed to provide long-term retirement income and protection against an unforeseen life event. Therefore – if an FTT cannot be avoided entirely – all pension products across Europe should be exempted from the scope of any envisaged FTT. Otherwise the FTT would have a negative effect on pension provision in Europe.

5. Withholding Taxes

Background:
The EU Commission plans to simplify the collection and refund process for withholding taxes (initiative 8).

From an insurance perspective:
The initiative 8 concerning digital solutions for withholding tax relief procedures is highly welcomed. The current legal situation and practice of collecting withholding taxes is unsatisfactory and characterized by a large number of different procedures in the Member States. This leads not only to a disproportionate administrative burden but, in some cases, the formal requirements are impossible to comply with. As a consequence, the recipient of a cross border payment is unable to obtain relief in the source state or to credit the withholding tax against its income tax in the state of residence, hence leading to unjustified double taxation.

Relief from withholding tax in accordance with a double tax treaty or an EU directive should be granted directly at source, i.e. through exemption rather than through a reclaim procedure. Ideally, no withholding tax is levied in the source state. A reclaim procedure should remain only as a back-up for cases in which the investor cannot obtain a direct relief at source. For any remaining withholding tax, the country of residence should be obliged to grant a full tax credit on the investor's income tax. Currently in some countries a full tax credit is often rejected due to a number of tax restrictions.

Regardless of the technical design features of the relief system, we consider it essential to ensure quick and efficient procedures which can be carried out by the taxpayer with acceptable administrative efforts. The future procedures should therefore be clear and simple, unified throughout Europe and in any case digital.

6. VAT

Background:
With respect to Value Added Tax (VAT) the EU Action Plan intends to make the existing VAT system more fraud-proof and easier to handle. Therefore, the Commission wants – among other measures – to modernize VAT reporting obligations (initiative 4) and to update VAT rules on financial services (initiative 18).

From an insurance perspective:
We welcome the EU Commission´s plan to modernize reporting obligations. For businesses that operate across the EU, it is important that an EU wide uniform set of reporting and invoicing requirements with standardized data models exists.

The insurance industry fully supports the modernization of the VAT rules for financial services. VAT treatment of financial services has not kept up with the necessities of the market. The VAT exemption of insurance is not a privilege. In Germany, as in other EU countries, it is effectively replaced by another indirect tax: the Insurance Premium Tax (IPT). And it comes with a price that puts the insurance industry at a competitive disadvantage: Input VAT deduction is not allowed. The non-deductible input VAT becomes a cost factor for insurance companies, which naturally impacts the pricing for the insurance products. At the end of the day the products will be more expensive for the consumer.

Furthermore, the lack of the right to deduct input VAT effectively prevents the insurance industry from outsourcing services and centralizing functions in shared service entities (such as accounting and IT services). Therefore, it is more difficult for insurance businesses to gain cost savings through outsourcing as well as from the centralization of services. They are forced to supply as many services as possible themselves, which puts them at a competitive disadvantage compared to other sectors of the economy.

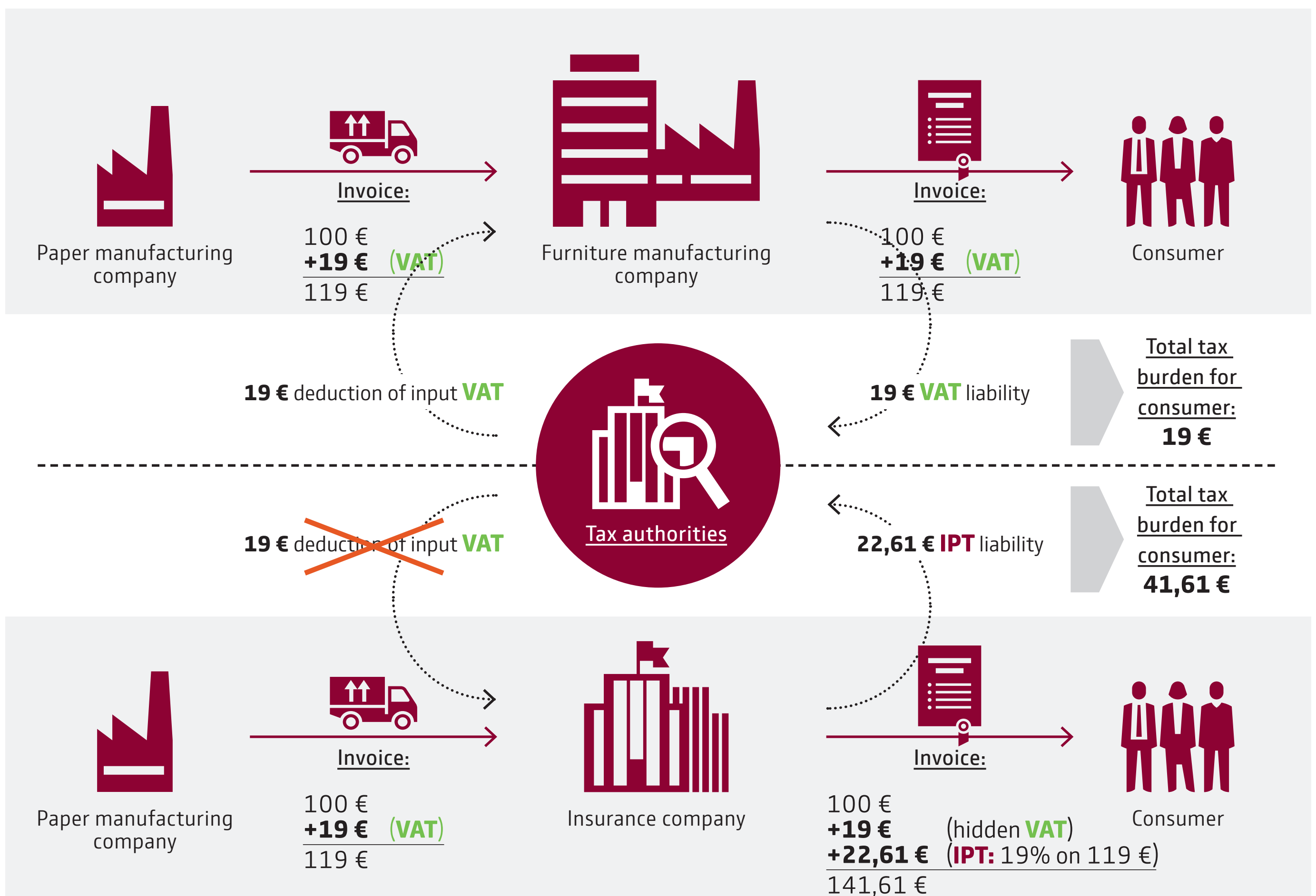
The VAT exemption for VAT groups is traditionally used in the German insurance sector to avoid input VAT costs. However, in many instances VAT grouping is

not available. Firstly, the VAT exemption does not cover transactions between unrelated parties. Secondly, the VAT group exemption requirements are often difficult or impossible to fulfil – in some cases because they run counter to regulatory requirements. Thirdly, VAT groups are limited to companies located within one EU Member State. While the rules for VAT grouping should be modernized, there are still other actions to be taken in order to create a level playing field for the insurance business in terms of VAT treatment.

One way to achieve a level playing field would be to simply allow input VAT deduction (VAT exemption with input VAT deductibility). This is the only way to create a full level playing field and should therefore be the preferred option. A less far reaching alternative would be to give insurance companies a right of option for taxation in respect of B2B transactions. An insurance company that opts for VAT taxation would then consequently be entitled to deduct input VAT on its purchases of goods and services that are used for B2B output transactions. Business customers of the insurance company would be entitled to deduct VAT charged by the insurance company. Unlike today, VAT neutrality which is the underlying principle for B2B transactions would be achieved across the transaction chain.

If such legislative change proves not feasible, the exemption for cost-sharing agreements should be made available for the insurance sector and the VAT group regime should be modernized. It is crucial that a modern, simplified EU wide VAT group regime allows for a cross border grouping in order to give groups that operate within one EU Member State and larger multinational enterprise groups equal access to the VAT grouping regime. Furthermore, a reform of the EU VAT group regime should be guided by the principles of tax certainty and easy compliance. Lastly, criteria to form a VAT group should be in line with insurance regulation.

Non-neutrality of VAT



Source: GDV

7. EU tax policy agenda for own tax resources

Background:
The EU Council agreed in its session on July 17-21, 2020 that the EU will have new own resources, based on a Carbon Border Adjustment Mechanism and on a digital levy. The Commission is still working on a new approach to business taxation.

From an insurance perspective:
Own resources for the EU either newly introduced or as a revenue share of existing taxes are a possible way to finance the EU budget. However, any new EU tax should be guided by the principles of administrative efficiency, consistency, and fairness. Fairness entails that, for example, a tax that is levied on income must take into account any expenses incurred in producing revenues (i.e. its basis must be a net amount). Fairness also means that any new EU tax together with national taxes do not lead to double taxation or an undue overall tax burden. Today, in times of global competition, it is especially important for all companies that the tax burden will not increase. Tax burden should be reduced as a response to the COVID-19 crisis.

8. Majority voting for tax proposals

Background:
Already prior to the July Tax Action Plan, the EU Commission had suggested in its communication from January 15th, 2019 that legislation in the area of taxation should be moved from unanimity to qualified majority voting.

From an insurance perspective:
The principle of unanimity in tax matters should be maintained. The gradual transition to majority decisions in the tax area bears the risk that individual Member State interests can and will be ignored. Decisions in the area of tax law concern central areas of life that particularly determine the relationship between state, citizens and the economy. Each EU Member State has adapted its tax and levy system to its specific economic and social needs. Due to the central importance of taxes to the national sovereignty an individual Member State should not be overruled by a majority.

However, there should be a response to the petrification effect of EU legislation due to unanimity for a change or repeal of legislation. This drawback of unanimous voting could be alleviated by inserting “sunset clauses” into a legislative act. Sunset clauses should especially be used in cases where the effects of innovative tax proposals are uncertain.

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