



Brussels, 11.5.2022  
COM(2022) 216 final

2022/0154 (CNS)

Proposal for a

**COUNCIL DIRECTIVE**

**on laying down rules on a debt-equity bias reduction allowance and on limiting the deductibility of interest for corporate income tax purposes**

{SEC(2022) 204 final} - {SWD(2022) 144 final} - {SWD(2022) 145 final} -  
{SWD(2022) 146 final}

## EXPLANATORY MEMORANDUM

### 1. CONTEXT OF THE PROPOSAL

#### • Reasons for and objectives of the proposal

On 18 May 2021, the European Commission adopted a Communication on Business Taxation for the 21st century<sup>1</sup> to promote a robust, efficient and fair business tax system in the EU. It sets out both a long-term and short-term vision to support Europe's recovery from the COVID-19 pandemic and to ensure adequate public revenues over the coming years. In the same vein, the EU's Capital Markets Union Action Plan (CMU)<sup>2</sup> aims at helping companies to raise the capital they need and improve their equity position, especially during a recovery period implying higher deficits and debt levels, as well a greater need for equity investment. In particular, Action 4 of the CMU<sup>3</sup> incentivises institutional investors to make more long-term investments and thus supports re-equitisation in the corporate sector, with a view to fostering the sustainable and digital transition of the EU economy. An initiative at EU level to address the debt-equity bias complements the aforementioned Action 4, with the aim to create an equitable and stable business environment, which can boost a sustainable and job-rich growth in the Union.

Tax systems in the EU allow for the deduction of interest payments on debt when calculating the tax base for corporate income tax purposes, while costs related to equity financing, such as dividends, are mostly non-tax deductible. This asymmetry in tax treatment is one of the factors favouring the use of debt over equity for financing investments. Currently, only 6 Member States address the debt-equity bias from a tax perspective and the relevant national measures differ significantly. Unless the tax-induced debt-equity bias is effectively tackled across the single market, EU business will continue to have insufficient incentives towards equity over debt financing and relevant tax planning considerations will continue distorting distribution of investment and growth.

With a view to addressing the tax-induced debt-equity bias across the single market in a coordinated way, this directive lays down rules to provide, under certain conditions, for the deductibility for tax purposes of notional interest on increases in equity and to limit the tax deductibility of exceeding borrowing costs. It applies to all taxpayers that are subject to corporate tax in one or more Member State, except for financial undertakings. Since small and medium enterprises (SMEs) usually face a higher burden to obtain financing, it is proposed to grant a higher notional interest rate to SMEs.

This proposal also replies to the European Parliament's expectation that the Commission would put forth a proposal for a debt-equity bias reduction allowance, including effective anti-avoidance provisions to avoid any allowance on equity being used as a new tool for base erosion<sup>4</sup>.

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<sup>1</sup> Communication From The Commission To The European Parliament And The Council, Business Taxation for the 21st Century, COM(2021) 251 final.

<sup>2</sup> Communication From The Commission To The European Parliament, The Council, The European Economic And Social Committee And The Committee Of The Regions, A Capital Markets Union for people and businesses-new action plan, COM/2020/590 final.

<sup>3</sup> [Action 4 - Encouraging more long-term and equity financing from institutional investors | European Commission \(europa.eu\)](https://ec.europa.eu/economy_finance/press-releases/2021/05/18-communication-business-taxation-2021-251-final)

<sup>4</sup> Report on the impact of national tax reforms on the EU economy, (2021/2074(INI)) [https://www.europarl.europa.eu/doceo/document/A-9-2021-0348\\_EN.html](https://www.europarl.europa.eu/doceo/document/A-9-2021-0348_EN.html)

- **Consistency with existing and possible future provisions in the policy area**

This Directive is part of the EU strategy on business taxation, which aims to ensure a fair and efficient tax system across the EU.

In 2016, the anti-tax avoidance directive (ATAD)<sup>5</sup> was adopted to ensure a fairer tax environment through the coordinated implementation in Member States of key measures against tax avoidance that mostly stemmed from the international Base Erosion and Profit Shifting (BEPS) project actions. While the fight against tax avoidance is not its predominant purpose, this proposal also includes an interest limitation rule. In light of the different objectives between this proposal and the ATAD rule on interest limitation, the two rules on limiting the deductibility of interest should apply in parallel.

Existing tax instruments at EU level do not contain, however, measures to address the debt-equity bias in the single market by balancing the tax treatment of debt and equity across the EU.

This Directive follows up to the Commission's Communication on Business Taxation for the 21st century for a robust, efficient and fair business tax system in the EU and reflects one of the policy initiatives envisaged in such Communication. As such, it complements a number of other policy initiatives promoted by the Commission in parallel, in the short- and long-term.

The aforementioned policy initiatives include a proposal for Business in Europe: Framework for Income Taxation (BEFIT), as a single corporate tax rulebook for the EU, based on the key features of having a common tax base and allocating profits between Member States through methods that include a formula (formulary apportionment). While the BEFIT proposal is still in an early stage of development, the two initiatives contribute to the same vision of a fair, effective and sustainable business environment in the EU.

- **Consistency with other Union policies**

This proposal contributes to the Capital Markets Union. In particular, key objectives of the CMU are to render financing more accessible to EU business and to promote the integration of national capital markets into a genuine single market. By removing the tax-induced debt-equity bias, this proposal is aimed at avoiding over-reliance on debt and encouraging the re-equitisation of businesses. As a result, companies will be in a better position to invest for the future, which will support growth and innovation and support the competitiveness of the EU economy. This will also increase their resilience to unforeseen changes in the business environment and decrease the risk of insolvency, thus contributing to enhancing financial stability.

## **2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY**

- **Legal basis**

Direct tax legislation falls within the ambit of Article 115 of the Treaty on the Functioning of the EU (TFEU). The clause stipulates that legal measures of approximation under that article shall take the legal form of a Directive.

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<sup>5</sup> 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 L 193, 19.7.2016, p. 1).

- **Subsidiarity (for non-exclusive competence)**

This proposal complies with the principle of subsidiarity. The nature of the subject requires a common initiative across the internal market.

The rules of this Directive aim to tackle the debt-equity bias in the EU corporate sector from a tax perspective and provide a common framework to be implemented into Member States' national laws in a coordinated manner. Such aims cannot be achieved in a satisfactory manner through action undertaken by each Member State while acting on its own.

Tax debt-equity bias arises from the different treatment of debt and equity financing costs for tax purposes and is a problem common to business across EU Member States. Despite this, only 6 Member States have taken tax measures to approximate the tax treatment of debt and equity. Although there is soft law guidance<sup>6</sup> for this type of tax incentives by the Code of Conduct Group (Business Taxation), the relevant national measures of the 6 Member States differ in terms of design elements and anti-tax avoidance rules, especially given the different circumstances and the different policy goals pursued in each Member State.

The complete lack of relevant tax debt bias mitigating measures in 21 Member States along with the existence of significantly different measures in another 6 Member States may create distortions to the function of the internal market and can affect the location of investment in a significant manner.

Furthermore, an EU initiative would add value, as compared to what a multitude of actions taken at national level can attain. A single rule for the EU will ensure legal certainty and allow reducing compliance costs for business as taxpayers will need to comply with a single rule for all their operations in the single market. An EU-wide rule is also expected to boost competition in the single market by ensuring that all businesses, regardless of where they are located, have similar incentives towards appropriate financing.

An EU-wide initiative in the form of a binding legislative proposal is therefore necessary to address in a coordinated and effective manner a problem that is common across the EU. An EU initiative would prevent potential loopholes between diverging national initiatives and would ensure that location of business and investment are not adversely impacted.

- **Proportionality**

The envisaged measures do not go beyond ensuring the minimum necessary level of protection for the internal market. The Directive lays down rules to provide, across the EU and for all EU taxpayers, for the deductibility of an allowance on equity financing costs complemented by a rule to limit the deductibility of interest on debt financing instruments. The Directive also ensures the sustainability of the measures for Member States' budgets by virtue of a general rule that limits the deductibility of financing costs from taxpayers' taxable base. By setting a common EU-wide framework, the Directive allows legal certainty across the single market and the reduction of compliance costs for taxpayers.

Thus, the Directive ensures only the essential degree of coordination within the Union for the purpose of materializing its aims. In this light, the proposal does not go beyond what is necessary to achieve its objectives and is therefore compliant with the principle of proportionality.

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<sup>6</sup> WK 11093/2019 REV 1

- **Choice of the instrument**

The proposal is for a Directive, which is the only available instrument under the legal base of Article 115 TFEU.

### **3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS**

- **Ex-post evaluations/fitness checks of existing legislation**

There is no EU legislation addressing the debt-equity bias. Therefore, evaluation is not relevant.

- **Stakeholder consultations**

On 1 July 2021, TAXUD launched a public consultation on a potential initiative to address the debt-equity bias. It contained a variety of questions aimed, inter alia, at delineating the problem and its drivers and identifying the appropriate form of EU action and the key features of a possible measure. The consultation closed on 7 October 2021 with a total of 67 replies.

The respondents were 37 business associations mainly representing financial organisations of all sizes (including SME), 12 companies/business organisations (mostly tax accountant and financial organisations), 3 academic and research institutions, 8 NGOs or others (mostly chamber of commerce, stock exchanges) and 7 individual citizens. Most respondents came from either Belgium (14/67), Germany (14/67) or France (12/67).

NGOs and academics are of the view that the main reason companies use debt is to decrease their tax liability and avoid dilution of their shareholders, whereas business associations and companies consider that it is the necessity of finding financing means.

A majority of respondents, among them 100% of academics, 86% of citizens, 50% of corporations and 42% of business associations, find that an EU initiative to address the tax debt-equity bias would be a useful tool to support the recovery of companies from the COVID-19 crisis and incentivise investment through equity in the transition to a greener digitalised economy without creating distortions in the single market. Companies, NGOs and academics strongly think firms should be encouraged, amongst others from a tax perspective, to use more equity and less debt.

Business associations, companies and academics clearly agree that such an initiative will reduce the room for harmful tax practices in the single market. Importantly, a majority of respondents, among them 71% of corporations, 66% of academics, 43% of citizens and 28% of business associations, think that an EU initiative would be beneficial for enterprises operating across the single market.

On the different options, a majority of respondents are very negative on the option of suppressing completely interest deductibility, among them 75% of corporations, 72% of business associations, 71% of citizens and 66% of academics find it the least suitable option and a majority is quite negative about the option for an allowance on corporate financial capital that would replace the tax deduction of interest. It was considered the best option only by 16% of corporations, 14% of citizens, 5% of business associations and no academic. On the contrary, a majority of respondents are favourable to an allowance that provides for the deductibility of a notional interest on new equity (while maintaining the existing interest deductibility). It appears the best option for 66% of academics, 28% of business associations, 25% of corporations and 14% of citizens. Business associations and companies are even more

favourable to the option of having an allowance on the stock of equity, while NGOs and academics are less favourable to this option.

Finally, a majority of respondents to this point strongly agree that the initiative should come with robust rules to avoid aggressive tax planning practices, among them 71% of citizens, 66% of academics, 42% of business associations and 33% of corporations.

In designing its proposal, the Commission took into account the results of the consultation. In particular, amongst the various policy options, the Commission decided to proceed with a proposal to give an allowance only to new equity and not to consider eliminating all deductibility of debt. Furthermore, the directive provides a robust anti-abuse framework as the need has been highlighted by the respondents.

In addition, the Commission appreciates that the protection of Member States' taxable revenues is essential to ensure a sustainable economy and safeguard public finances during the ongoing recovery period after the pandemic. Consequently, the Commission proposes to mitigate the debt-equity bias through measures addressing both the equity and the debt sides, combining an allowance for new equity with a limitation to the deductibility of debt costs.

- **Collection and use of expertise**

In identifying appropriate measures to tackle the debt-equity bias, the Commission drew on the relevant expertise of Member States that have already put in place similar measures (Belgium, Portugal, Poland, Cyprus, Malta and Italy). The Commission undertook exchanges with some of the relevant tax administrations on the anti-abuse framework and to better understand the impact in terms of costs and benefits of the various measures.

The Commission met with national public authorities/agencies, business associations and civil society groups that participate in the Commission Expert Group "Platform for Tax Good Governance, Aggressive Tax Planning and Double Taxation". The Commission also had exchanges with the European Economic and Social Committee (EESC).

- **Impact assessment**

An impact assessment was carried out to prepare this initiative.

On 17 March 2022 the Regulatory Scrutiny Board (RSB) issued a positive opinion with reservations on the submitted impact assessment regarding this proposal, including several suggestions for improvement.<sup>7</sup> The Impact Assessment report (IA) was further revised along these lines, as explained below. The IA examines five policy options in addition to the baseline scenario, i.e. no action.

Option 1 would introduce an allowance on the stock of corporate equity indefinitely, whereas Option 2 would also introduce an allowance but only for new equity and for ten years.

Option 3 would envisage an allowance on corporate capital (i.e. equity and debt) while disallowing current deductibility of interest payments and Option 4 would completely disallow the deductibility of interest expenses. Option 5 would combine an allowance for notional interest on new corporate equity (same as proposed under Option 2) for ten years with a partial limitation of tax deductibility for all companies.

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<sup>7</sup> [Please insert the links to the summary sheet and the positive opinion of the RSB after their publication.]

A rate top-up for SMEs<sup>8</sup> would be applied in all cases outlined under policy options 1, 2, 3 and 5..

The various Options have been compared against the following criteria: a) Making the tax system neutral for financing decisions, b) Enhancing the fairness of the tax system, c) Reducing distortions in the single market and d) Stimulating growth and investment in the EU. The comparison revealed that Options 1, 2, 3 and 4 can be expected to be to some degree effective in meeting some of the objectives of this initiative. However, Option 5 is the preferred option, because it successfully addresses the debt-equity bias, while balancing the budgetary impacts and addressing the fairness aspects of the tax system. It is expected to have a positive impact on investment and GDP, and moderate impacts on employment.

#### *Economic impacts*

For the assessment of the economic impacts the modelling was done by the European Commission's Joint Research Centre based on the CORTAX model.

#### *Benefits*

The preferred option (Option 5) is expected to have a positive economic impact. As main direct benefit, it will favour higher equity ratios and so reduce insolvency risks. By increasing equity investments across the EU, this option is expected to indirectly promote the development of innovative technology. Equity is particularly important for fast-growing innovative companies in their early stages and scale-ups willing to compete globally. The green and digital transition requires new and innovative investments that will benefit from the measure. By benefiting from a higher notional interest rate, SMEs will have an increased access to the equity market. Positive effects on competitiveness, innovation, growth and employment in the EU are expected. It will also tackle fragmentation of the single market by eliminating different treatment under different national allowance for equity measures and providing same administrative rules in all EU Member States. Finally, it will provide uniform and effective measures against aggressive tax planning in the EU.

#### *Costs*

The costs related to the selected option are essentially an increase in compliance costs for businesses and tax administrations. Tax compliance costs for business are expected to increase in a limited manner. Overall, costs should be relatively limited because the additional data to be reported to benefit from the allowance should be relatively simple to provide. For tax administrations, costs are also expected to increase modestly. This proposal does not significantly increase compliance burden for firms or for tax administrations.

#### *Main changes implemented*

The RSB issued a positive opinion with reservations on the IA. In particular, it was noted that IA should better highlight how the preferred option best achieves the objectives. Furthermore, the RSB noted that the IA should be enhanced as regards the possibility to use non regulatory measures and should better reflect the different stakeholder views throughout the main analysis and annexes. Annex I to the Impact Assessment explains how the RSB reservations

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<sup>8</sup> SMEs would be defined as per Article 3 of the Accounting Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013. In addition it would be required that for a company to be considered a SME, it must not be part of a group of businesses which, at consolidated level, exceeds at least two of the three limits of Article 3 under the Accounting Directive (Average number of employees in the fiscal year 250; net turnover of EUR 40 million; balance sheet total of EUR 20 million).

were addressed. Several parts of the IA were revised. First, the IA has been revised in order to clarify that a non-regulatory option could not be effective. Second, the IA has been expanded in order to reflect in detail the scale of anticipated effects on equity investment and the impact of the preferred option on tax revenues in absolute terms. The IA was also enhanced with further analysis of the reasons why an option acting both on the equity and debt sides has been considered as fit for purpose. Third, several sections of the main part of the IA were revised in order to include relevant stakeholder input, gathered through the open public consultation procedure.

#### **4. BUDGETARY IMPLICATIONS**

See Legislative Financial Statement.

#### **5. OTHER ELEMENTS**

- **Implementation plans and monitoring, evaluation and reporting arrangements**

This proposal, once adopted as a Directive, should be transposed into Member States' national law by 31 December 2023 and come into effect as of 1 January 2024. For the purpose of monitoring and evaluation of the implementation of the Directive, Member States will have to provide the Commission, on a yearly basis, with relevant information per tax year, including a list of statistical data. The relevant information is set out in Article 7 of the Directive.

The Commission shall submit a report on the application of this Directive to the European Parliament and to the Council every five years, which should start counting after [1 January 2024]. The results of this proposal will be included in the report to the European Parliament and to the Council that will be issued by [1 January 2029].

- **Detailed explanation of the specific provisions of the proposal**

This proposal applies to all taxpayers which are subject to corporate income tax in one or more Member States, with the exception of financial undertakings, as defined in Article 3(1).

It includes two separate measures that apply independently: 1) an allowance on equity; and 2) a limitation to interest deduction. Financial undertakings are not in the scope of the measures. Some financial undertakings are subject to regulatory equity requirements that prevent under-equitisation. In addition, many are unlikely to be affected by the countervailing interest limitation deduction applicable to exceeding borrowing costs. Therefore, should financial undertakings be included in the scope, the economic burden of the measures would be unequally distributed at the expense of non-financial undertakings.

- **Allowance on equity**

The allowance on equity is computed by multiplying the allowance base with the relevant notional interest rate.

$$\text{Allowance on equity} = \text{Allowance Base} \times \text{Notional Interest Rate (NIR)}$$

The allowance base is equal to the difference between equity at the end of the tax year and equity at the end of the previous tax year that is the year-on-year increase in equity.

If the allowance base of a taxpayer that has already benefitted from an allowance on equity under the rules of this Directive, is negative in a given tax period (equity decrease), a proportionate amount will become taxable for 10 consecutive tax periods and up to the total increase of net equity for which such allowance has been obtained, unless the taxpayer



provides evidence that this is due to losses incurred during the tax period or due to a legal obligation.

Equity is defined by reference to Directive 2013/34/EU (Accounting Directive)<sup>9</sup>, meaning the sum of Paid-up Capital, Share premium account, Revaluation reserve and Reserves<sup>10</sup> and Profits or Losses carried forward. Net equity is then defined as the difference between the equity of a taxpayer and the sum of the tax value of its participation in the capital of associated enterprises and of its own shares. This definition is meant to prevent cascading the allowance through participations.

The relevant notional interest rate is based on two components: the risk-free interest rate and a risk premium. The risk-free interest rate is the risk-free interest rate with a maturity of ten years, as laid down in the implementing acts to Article 77e(2) of Directive 2009/138/EC<sup>11</sup>, in which the allowance is claimed, for the currency of the taxpayer. The risk premium is set at 1%, to better account for the risk premium that investors actually pay and better mitigate the bias. The risk premium is set at 1.5% in the case of taxpayers qualifying as small or medium-sized enterprises, to better reflect the higher risk premium they incur to obtain financing. There should be no discretion on the part of Member States as to whether to apply this higher rate for SMEs or what rate to apply as the top-up for SMEs in order to avoid selectivity concerns as regards EU State Aids rules and to ensure a level playing field for SMEs in the EU regardless of their place of residence.

$$\text{NIR} = \text{Risk Free Rate} + \text{Risk Premium}$$

$$\text{Risk Premium} = 1\% \text{ (or } 1.5\% \text{ for SMEs)}$$

The notional interest rate is hence equal to the currency specific risk-free rate plus 1% or 1.5% (NIR = risk free rate + 1% or, for SMEs, NIR = risk free rate + 1.5%). This approach ensures that the measure has an impact while remains simple to implement and does not harm Member States' budgets. It also ensures that the specific circumstances of different businesses are taken into account. A specific currency rate better ensures the balance of tax treatment between equity and debt since it takes into account the currency risk separately for each currency and reflects the specific situation of each taxpayer.

The allowance is granted for ten years to approximate the maturity of most debt, while keeping the overall budgetary cost of the allowance on equity under control. This means that if an increase in a taxpayer's equity qualifies for an allowance on equity under this proposal, the relevant allowance, computed as above, shall be deductible in the year it was incurred (TY) and in the next successive nine years (TY+9). If, in the following year (TY+1), a new increase in a taxpayer's equity also qualifies for an allowance on equity under this proposal, the new allowance on equity will also be deductible for the tax year it was incurred and the following nine years since its incurrence (until TY+10).

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<sup>9</sup> In the sense of Annex III to Directive 2013/34/EU of the European Parliament and of the Council on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings.

<sup>10</sup> Reserves include: 1. Legal reserve, in so far as national law requires such a reserve; 2. Reserve for own shares, in so far as national law requires such a reserve, without prejudice to point (b) of Article 24(1) of Directive 2012/30/EU; 3. Reserves provided for by the articles of association; 4. Other reserves, including the fair value reserve

<sup>11</sup> Directive 2009/138/EC Of The European Parliament And Of The Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (recast) (OJ L 335/17.12.2009, p.1)

By way of example, if a company having equity of 100, decides to increase in year t its equity by 20, an allowance will be deducted from its taxable base every year for ten years (until t+9) calculated as 20 times the notional interest rate, i.e. 20 times the risk-free interest rate for the relevant currency plus 20 (20 times the risk premium defined as 1).

Year	t	t - 1
Equity of Company A	120	100

Allowance base = 120 – 100 = 20

Allowance = Allowance base X NIR = 20 X NIR

The allowance will be available for 10 consecutive years : t, t+1, t+2, ....t+9

If the company is a small or medium enterprise, the allowance will be calculated in the same way. The NIR will simply be different since the risk premium is higher (1.5 % instead of 1%).

To prevent tax abuse, the deductibility of the allowance is limited to a maximum of 30% of the taxpayer’s EBITDA (earnings before interest, tax, depreciation and amortization) for each tax year. A taxpayer will be able to carry forward, without time limitation, the part of the allowance on equity that would not be deducted in a tax year due to insufficient taxable profit. In addition, the taxpayer will be able to carry forward, for a period of maximum five years, unused allowance capacity, where the allowance on equity does not reach the aforementioned maximum amount.

Robust anti-abuse measures will ensure that the rules on the deductibility of an allowance on equity are not used for unintended purposes. These anti-abuse rules are inspired from the Guidance on notional interest deduction regimes which was adopted by the Code of Conduct Group in 2019 and address well-known existing schemes, such as cascading the allowance within a group.

A first measure would exclude from the base of the allowance equity increases that originate from (i) intra-group loans, (ii) intra-group transfers of participations or existing business activities and (iii) cash contributions under certain conditions. Thus, for example, as regards intra-group loans, the measure should prevent that an equity injection granted to company A located in Member State A is used to grant a loan to a related company B located in Member State B. This is because in such case, company B would also use this money to inject equity in another related company C, located in Member State C. This would lead to multiplying the allowance on equity with only one genuine equity increase at group level.

Another measure sets out specific conditions for taking into account equity increases originating from contributions in kind or investments in assets. It aims to prevent the overvaluation of assets or purchase of luxury goods for the purpose of increasing the base of the allowance. Thus, for example, the value of an asset and the related costs should not exceed reasonable professional needs and any part of the value of the asset contributed or recorded in the taxpayer’s accounting books over its market value should be deducted from the base of the allowance.

A third measure targets the re-categorisation of old capital as new capital, which would qualify as an equity increase for the purpose of the allowance. Such re-categorisation could be achieved through a liquidation and the creation of start-ups. For example, if an existing company, with retained earnings, is liquidated, there will be an increase in the equity of the parent company due to the incorporation of the retained earnings. If a new subsidiary is subsequently created and is no longer held by the parent, the previously increased base of allowance of the parent would not be reduced by the value of the participation in the subsidiary.

- **Limitation to interest deduction**

On the debt side, the allowance for notional interest on equity is accompanied by a limitation to the tax deductibility of debt-related interest payments. In particular, a proportional restriction will limit the deductibility of interest to 85% of exceeding borrowing costs (i.e. interest paid minus interest received). Such an approach allows addressing the debt-equity bias simultaneously from both the equity and the debt side, which is most efficient and preserves the sustainability of Member States' public finances.

Given that interest limitation rules already apply in the EU under Article 4 of the ATAD, the taxpayer will apply the rule of Article 6 of this proposal as a first step and then, calculate the limitation applicable in accordance with article 4 of ATAD. If the result of applying the ATAD rule is a lower deductible amount, the taxpayer will be entitled to carry forward or back the difference in accordance with Article 4 of ATAD.

By way of example, if company A has exceeding borrowing costs of 100, it should:

- (1) First, apply Article 6 of this directive proposal that limits the deductibility to 85% of 100 = 85 and thus renders a non-deductible amount of 15.
- (2) Second, compute the amount that would be deductible under Article 4 of the ATAD. If the deductible amount is lower, e.g. 80 (and subsequently the non-deductible higher, i.e. 20), the difference in the deductibility, i.e. the additional non-deductible amount (i.e.  $85 - 80 = 5$ ) would be carried forward or back in accordance with the conditions of Article 4 of ATAD, as transposed in national law.

The outcome for company A is that 15 ( $100 - 85$ ) of interest borrowing costs are non-deductible and a further 5 ( $85 - 80$ ) of interest borrowing costs are carried forward or back.

- **Monitoring and reporting**

Member States will provide specific data to the Commission on a yearly basis in order to allow monitoring the implementation and effects of the new rules. The Commission will rely on these data, amongst others, in order to evaluate the implementation of the Directive and report accordingly.

- **Delegation**

The Commission will have the power to modify the risk premium rate by adopting delegated acts. The Commission may exercise such power only under specific circumstances, i.e. where inflation and/or economic growth trends require an increase or decrease of the risk premium and provided that relevant data, reports and statistics, including those provided by Member States, conclude that the EU average of the financing conditions of debt of the companies in scope of the directive have doubled or halved since the last determination of the risk premium. In such cases it is in fact essential to be able to change applicable rates to reflect real market conditions quickly and smoothly, without recourse to a full legislative procedure. The power of the Commission is however duly restricted and revocable.

- **Transposition**

Member States that have rules in place providing for an allowance on equity increases may defer the application of the provisions of this directive for the duration of rights already established under domestic rules (grandfathering) Taxpayers that, on [1 January 2024] benefit from an allowance on equity, under domestic law (in Belgium, Cyprus, Italy, Malta, Poland and Portugal) will be able to continue to benefit from such allowance under national law for a period of up to 10 years and in no case for a period longer than the duration of the benefit

under national law. Conversely the rules of this directive will apply from their date of application to all other taxpayers in all Member States.

Proposal for a

## COUNCIL DIRECTIVE

### **on laying down rules on a debt-equity bias reduction allowance and on limiting the deductibility of interest for corporate income tax purposes**

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 115 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Parliament<sup>12</sup>,

Having regard to the opinion of the European Economic and Social Committee<sup>13</sup>,

Acting in accordance with a special legislative procedure,

Whereas:

- (1) Promoting a fair and sustainable business environment, including through targeted tax measures that incentivise investment and growth, is a high political priority of the Union. To support sustainable and long-term corporate financing, the tax system should minimise unintended distortions of business decisions, for example towards debt rather than equity financing. While the Commission's Capital Markets Union 2020 Action Plan<sup>14</sup> includes important actions to support such financing, for example Action 4 - Encouraging more long-term and equity financing from institutional investors, targeted tax measures should be adopted in order to enhance such actions. Such measures should take into account fiscal sustainability considerations.
- (2) Member States' tax systems allow the taxpayers to deduct interest payments on debt financing, and thereby reduce the corporate income tax liability, while costs related to equity financing are non-tax deductible in most Member States. The asymmetric tax treatment of debt and equity financing across the Union induces a bias towards debt in investment decisions. Moreover, where Member States provide for a tax allowance on equity financing in their domestic law, such national measures differ significantly in terms of policy design.
- (3) In order to remove possible tax related distortions among Member States, it is necessary to lay down a common framework of rules to address the tax related debt-equity bias across the Union in a coordinated manner. Such rules should ensure that

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<sup>12</sup> OJ C , , p. .Not yet published in the Official Journal.

<sup>13</sup> OJ C , , p. .Not yet published in the Official Journal.

<sup>14</sup> Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions 'A Capital Markets Union for people and businesses-new action plan', COM(2020) 590 final ([https://eur-lex.europa.eu/resource.html?uri=cellar:61042990-fe46-11ea-b44f-01aa75ed71a1.0001.02/DOC\\_1&format=PDF](https://eur-lex.europa.eu/resource.html?uri=cellar:61042990-fe46-11ea-b44f-01aa75ed71a1.0001.02/DOC_1&format=PDF))

equity and debt financing are treated in a similar way for tax purposes across the single market. At the same time, a common Union legislative framework should be sustainable also in the short term for Member States' budgets. Such framework should therefore include rules, on the one hand, for the tax deductibility of equity financing costs and, on the other, for limiting the tax deductibility of debt financing costs.

- (4) To ensure a simple and comprehensive legislative framework, the common framework of rules should apply to all undertakings in the Union that are subject to corporate income tax in a Member State. Financial undertakings have special features and require a specific treatment. If the rules to address the tax related debt-equity bias were to apply to them, the economic burden of the measures would be unequally distributed at the expense of non-financial undertakings. Financial undertakings should therefore be excluded from the scope of this Directive.
- (5) To neutralise the bias against equity financing, an allowance should be envisaged so that increases in a taxpayer's equity from one tax period to the next are deductible from its taxable base, subject to certain conditions. The allowance should be calculated by multiplying the increase in equity with a notional interest rate based on risk-free interest rate as laid down in the implementing acts adopted pursuant to Article 77e(2) of Directive 2009/138/EC. Such risk-free interest rates are already part of EU law and have been practically and effectively applied as such. Any part of the allowance that cannot be deducted in a tax period due to insufficient taxable profits may be carried forward. Taking into account the specific challenges that small- and medium-sized enterprises (SMEs) face in accessing capital markets, an increased allowance on equity should be envisaged for taxpayers that are SMEs. In order for the deduction of an allowance on equity to be sustainable for public finances in the short term, it should be limited in time. To safeguard the system from abuses, it is necessary to exclude the tax value of a taxpayer's own shares as well as that of its participation in associated enterprises from the calculation of changes in equity. In the same vein, it is necessary to provide for the taxation of a decrease in a taxpayer's equity from one tax period to the following one, to prevent an equity increase from being effected in an abusive manner. Such a rule would also encourage the retention of a level of equity. It would apply so that where there is a decrease in equity of a taxpayer that has benefitted from an allowance on equity increase, an amount calculated in the same way as the allowance would become taxable for 10 tax periods; unless the taxpayer provides evidence that this decrease is exclusively due to losses incurred during the tax period or due to a legal obligation.
- (6) In order to avoid a misuse of the deduction of the allowance on equity, it is necessary to lay down specific anti-tax avoidance rules. Such rules should target, in particular, schemes put in place to circumvent the conditions on which an equity increase qualifies for an allowance under this Directive, for instance, through the intra-group transfer of participations in associated enterprises. Such rules should also target schemes put in place to claim an allowance in the absence of any equity increase at group level. For example, intra-group debt financing or contributions in cash could be used for these purposes. Specific anti-tax avoidance rules should also prevent schemes from being put in place to claim that an increase in equity, and the corresponding allowance, is higher than it actually is, for example, through an increase in loan financing receivables or overvaluation of assets. Moreover, the general anti-tax abuse

rule in Article 6 of Council Directive (EU) 2016/1164<sup>15</sup> applies against abusive acts which are not covered by the specific anti-tax avoidance framework of this Directive.

- (7) To effectively address the tax-related debt-equity bias in a manner sustainable for the Union's public finances, an allowance for equity financing should be accompanied by a limitation on the deductibility of debt financing costs. An interest limitation rule should therefore limit the deductibility of exceeding borrowing costs and apply independently from the allowance. Given the different objectives between such a rule and the existing anti-tax avoidance rule on interest limitation of Article 4 of Directive (EU) 2016/1164, both rules should be maintained. Taxpayers should first calculate the deductibility of exceeding borrowing costs under this Directive and then under ATAD. In the event that the latter results in a lower amount of deductible exceeding borrowing costs, the taxpayer should deduct this lower amount and carry forward or back any difference between the two amounts in accordance with Article 4 of ATAD.
- (8) As the implementation and enforcement of the Union rules in each Member State are critical for safeguarding Member States' tax bases and, where necessary, for properly reviewing the Union rules, such implementation and enforcement should be monitored by the Commission. Member States should therefore communicate to the Commission, on a regular basis, specific information on the implementation and enforcement in their territory of national measures transposing this Directive.
- (9) In order to evaluate the effectiveness of this Directive, the Commission should prepare and publish an evaluation report on the basis of the information provided by Member States and of other available data.
- (10) In order to enable the smooth and prompt amendment of certain non-essential elements of this Directive taking into account ongoing developments, the power to adopt acts in accordance with Article 290 of the Treaty on the Functioning of the European Union should be delegated to the Commission, so that the latter can amend this Directive, to modify the level of the risk premium rate as an element for the calculation of the allowance on equity. It is of particular importance that the Commission carry out appropriate consultations during its preparatory work, including at expert level, and that those consultations be conducted in accordance with the principles laid down in the Interinstitutional Agreement of 13 April 2016 on Better Law-Making<sup>16</sup>. In particular, to ensure equal participation in the preparation of delegated acts, the Council should receive all documents at the same time as Member States' experts, and its experts should systematically be given access to meetings of Commission expert groups dealing with the preparation of delegated acts.
- (11) Since the objective of this Directive cannot sufficiently be achieved by the Member States but can rather, by reason of the need to provide balanced incentives for business location and entrepreneurship in the single market, be better achieved at Union level, the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality as set out in that Article, this Directive should not go beyond what is necessary in order to achieve that objective,

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<sup>15</sup> 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 L 193, 19.7.2016, p. 1).

<sup>16</sup> OJ L 123, 12.5.2016, p. 1.

HAS ADOPTED THIS DIRECTIVE:

## **CHAPTER I GENERAL PROVISIONS**

### *Article 1*

#### ***Subject matter***

This Directive lays down rules on the deduction, for corporate income tax purposes, of an allowance on increases in equity and on the limitation of the tax deductibility of exceeding borrowing costs.

### *Article 2*

#### ***Scope***

This Directive applies to taxpayers that are subject to corporate income tax in one or more Member States, including permanent establishments in one or more Member State of entities resident for tax purposes in a third country.

However, this Directive does not apply to the following financial undertakings:

- (a) ‘credit institution’ as defined in Article 4(1), point (1), of Regulation (EU) No 575/2013 of the European Parliament and of the Council<sup>17</sup>;
- (b) ‘investment firm’ as defined in Article 4(1), point (1), of Directive 2014/65/EU of the European Parliament and of the Council<sup>18</sup>;
- (c) ‘alternative investment fund manager’ as defined in Article 4(1), point (b), of Directive 2011/61/EU of the European Parliament and of the Council<sup>19</sup>, including a manager of European venture capital funds under Regulation (EU) No 345/2013 of the European Parliament and of the Council<sup>20</sup>, a manager of European social entrepreneurship funds under Regulation (EU) No 346/2013 of the European Parliament and of the Council<sup>21</sup> and a manager of European long-term investment funds under Regulation (EU) 2015/760 of the European Parliament and of the Council<sup>22</sup>;

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<sup>17</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

<sup>18</sup> Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).

<sup>19</sup> Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (OJ L 174, 1.7.2011, p. 1).

<sup>20</sup> Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 on European venture capital funds (OJ L 115, 25.4.2013, p. 1).

<sup>21</sup> Regulation (EU) No 346/2013 of the European Parliament and of the Council of 17 April 2013 on European social entrepreneurship funds (OJ L 115, 25.4.2013, p. 18).

<sup>22</sup> Regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 on European long-term investment funds (OJ L 123, 19.5.2015, p. 98).



- (d) ‘undertaking for collective investment in transferable securities’ management company’ as defined Article 2(1), point (b), of Directive 2009/65/EC of the European Parliament and of the Council<sup>23</sup>;
- (e) ‘insurance undertaking’ as defined in Article 13, point (1), of Directive 2009/138/EC of the European Parliament and of the Council<sup>24</sup>;
- (f) ‘reinsurance undertaking’ as defined in Article 13, point (4), of Directive 2009/138/EC;
- (g) ‘institution for occupational retirement provision’ as defined in Article 6, point (1), of Directive (EU) 2016/2341 of the European Parliament and of the Council<sup>25</sup>;
- (h) pension institutions operating pension schemes which are covered by Regulation (EC) No 883/2004 of the European Parliament and of the Council<sup>26</sup> as well as any legal entity set up for the purpose of investment in such schemes;
- (i) ‘alternative investment fund’ as defined in Article 4(1), point (a), of Directive 2011/61/EU, managed by an alternative investment fund manager, as defined in Article 4(1), point (b), of Directive 2011/61/EU or an alternative investment fund as defined in Article 4(1), point (a), of Directive 2011/61/EU supervised under the applicable national law;
- (j) undertakings for collective investment in transferable securities within the meaning of Article 1(2) of Directive 2009/65/EC;
- (k) ‘central counterparty’ as defined in Article 2, point (1), of Regulation (EU) No 648/2012 of the European Parliament and of the Council<sup>27</sup>;
- (l) ‘central securities depository’ as defined in Article 2(1), point (1), of Regulation (EU) No 909/2014 of the European Parliament and of the Council<sup>28</sup>;
- (m) a special purpose vehicle authorised in accordance with Article 211 of Directive 2009/138/EC;
- (n) ‘securitisation special purpose entity’ as defined in Article 2, point (2), of Regulation (EU) No 2017/2402 of the European Parliament and of the Council<sup>29</sup>;

<sup>23</sup> Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 302, 17.11.2009, p. 32).

<sup>24</sup> Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (OJ L 335, 17.12.2009, p. 1).

<sup>25</sup> Directive (EU) 2016/2341 of the European Parliament and of the Council of 14 December 2016 on the activities and supervision of institutions for occupational retirement provision (IORPs) (OJ L 354, 23.12.2016, p. 37).

<sup>26</sup> Regulation (EC) No 883/2004 of the European Parliament and of the Council of 29 April 2004 on the coordination of social security systems (OJ L 166, 30.4.2004, p. 1).

<sup>27</sup> Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (OJ L 201, 27.7.2012, p. 1).

<sup>28</sup> Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (OJ L 257, 28.8.2014, p. 1).

<sup>29</sup> Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU

- (o) ‘insurance holding company’ as defined in Article 212(1), point (f), of Directive 2009/138/EC or ‘mixed financial holding company’ as defined in Article 212(1), point (h), of Directive 2009/138/EC, which is part of an insurance group that is subject to supervision at the level of the group pursuant to Article 213 of that Directive and which is not excluded from group supervision pursuant to Article 214(2) of Directive 2009/138/EC;
- (p) ‘payment institution’ as defined in Article 4, point (4), of Directive (EU) 2015/2366 of the European Parliament and of the Council<sup>30</sup>;
- (q) ‘electronic money institution’ as defined in Article 2, point (1), of Directive 2009/110/EC of the European Parliament and of the Council<sup>31</sup>;
- (r) ‘crowdfunding service provider’ as defined in Article 2(1), point (e), of Regulation (EU) 2020/1503 of the European Parliament and of the Council<sup>32</sup>;
- (s) ‘crypto-asset service provider’ as defined in Article 3(1), point (8), of Regulation .../... of the European Parliament and of the Council<sup>33</sup>

### *Article 3* **Definitions**

For the purposes of this Directive, the following definitions shall apply:

- (1) ‘associated enterprise’ means a person who is related to another person in any of the following ways:
  - (a) the person participates in the management of the other person by being in a position to exercise a significant influence over the other person;
  - (b) the person participates in the control of the other person through a holding that exceeds 25 % of the voting rights;
  - (c) the person participates in the capital of the other person through a right of ownership that, directly or indirectly, exceeds 25 % of the subscribed capital;
  - (d) the person is entitled to 25 % or more of the profits of the other person.

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and Regulations (EC) No 1060/2009 and (EU) No 648/2012 (OJ L 347, 28.12.2017, p. 35).

<sup>30</sup> Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC (OJ L 337, 23.12.2015, p. 35).

<sup>31</sup> Directive 2009/110/EC of the European Parliament and of the Council of 16 September 2009 on the taking up, pursuit and prudential supervision of the business of electronic money institutions amending Directives 2005/60/EC and 2006/48/EC and repealing Directive 2000/46/EC (OJ L 267, 10.10.2009, p. 7).

<sup>32</sup> Regulation (EU) 2020/1503 of the European Parliament and of the Council of 7 October 2020 on European crowdfunding service providers for business, and amending Regulation (EU) 2017/1129 and Directive (EU) 2019/1937 (OJ L 347, 20.10.2020, p. 1).

<sup>33</sup> Regulation of the European Parliament and of the Council on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 (OJ L...) (OJ: Please insert in the text the number of the Regulation contained in document 2020/0265/COD and insert the number, date, and OJ reference of that Directive in the footnote.)

If more than one person participates in the management, control, capital or profits of the same person, as referred to in paragraph 1, all persons concerned shall be regarded as associated enterprises.

If the same persons participate in the management, control, capital or profits of more than one person, as referred to in paragraph 1 all persons concerned shall be regarded as associated enterprises.

For the purposes of this definition , ‘person’ means both legal and natural persons. A person who acts together with another person in respect of the voting rights or capital ownership of an entity shall be treated as holding a participation in all of the voting rights or capital ownership of that entity that are held by the other person.

In indirect participations, the fulfilment of the criteria set out in point (c) of paragraph 1 shall be determined by multiplying the rates of holding through the successive tiers. A person holding more than 50 % of the voting rights shall be deemed to hold 100 %.

The spouse, and lineal descendants of an individual, together with the individual, shall be treated as a single person.

An associated enterprise in accordance with this paragraph shall also include any operation as a result of which a person becomes an associated enterprise;

- (2) 'tax period' means a calendar year or any other appropriate period for tax purposes;
- (3) 'group' means a group as defined in Article 2, point (11), Directive 2013/34/EU of the European Parliament and of the Council<sup>34</sup>.
- (4) 'participation' means participating interest as defined in Article 2, point (2), of Directive 2013/34/EU;
- (5) 'SME' means all undertakings which do not exceed the threshold for medium-sized undertakings, as laid down in Article 3(3) of Directive 2013/34/EU;
- (6) 'equity' means, in a given tax period, the sum of the taxpayer's paid-up capital, share premium accounts, revaluation reserve and other reserves and profit or loss brought forward;
- (7) 'net equity' means the difference between the equity of a taxpayer and the sum of the tax value of the taxpayer's participation in the capital of associated enterprises and the taxpayer's own shares;
- (8) 'reserves' means any of the following:
  - (1) legal reserve, in so far as national law requires such a reserve;
  - (2) reserve for own shares, in so far as national law requires such a reserve, without prejudice to Article 24(1), point (b), of Directive 2012/30/EU;
  - (3) reserves provided for by the articles of association;
  - (4) other reserves, including the fair value reserve.

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<sup>34</sup> Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013, p. 19).

## CHAPTER II

# ALLOWANCE ON EQUITY AND INTEREST DEDUCTIONS

### *Article 4* *Allowance on Equity*

1. An allowance on equity shall be deductible, for 10 consecutive tax periods, from the taxable base of a taxpayer for corporate income tax purposes up to 30% of the taxpayer's earnings before interest, tax, depreciation and amortisation (“EBITDA ”).

If the deductible allowance on equity, in accordance with the first subparagraph, is higher than the taxpayer's net taxable income in a tax period, Member States shall ensure that the taxpayer may carry forward, without time limitation, the excess of allowance on equity to the following periods.

Member States shall ensure that the taxpayers may carry forward, for a maximum of 5 tax periods, the part of the allowance on equity which exceeds 30% of EBITDA in a tax period.

2. Subject to Article 5, the base of the allowance on equity shall be calculated as the difference between the level of net equity at the end of the tax period and the level of net equity at the end of the previous tax period.

The allowance on equity shall be equal to the base of the allowance multiplied by the 10-year risk-free interest rate for the relevant currency and increased by a risk premium of 1% or, where the taxpayer is an SME, a risk premium of 1.5%.

For the purposes of the second subparagraph of this paragraph, the 10-year risk-free interest rate for the relevant currency shall be the risk-free interest rate with a maturity of 10 years for the relevant currency, as laid down in the implementing acts adopted pursuant to Article 77e(2) of Directive 2009/138/EC for the reference date of 31 December of the year preceding the relevant tax period.

3. If, after having obtained an allowance on equity, the base of the allowance on equity is negative in a tax period, an amount equal to the negative allowance on equity shall become taxable for 10 consecutive tax periods, up to the overall increase of net equity for which such allowance has been obtained under this Directive, unless the taxpayer provides sufficient evidence that this is due to accounting losses incurred during the tax period or due to a legal obligation to reduce capital.

4. The Commission shall be empowered to adopt delegated acts in accordance with Article 9 amending paragraph 2 of this Article by modifying the rate of the risk premium, where any of the following two conditions is met:

- (a) the 10-year risk-free interest rate as referred to in paragraph 2 of this Article varies by more than two percentage points with regard to at least three Union currencies compared to the tax period in which the most recent delegated act modifying the risk premium, or, where there is no such delegated act, this Directive started to apply; or
- (b) zero or negative growth of the gross domestic product of the EU area in at least two successive quarters;

and

- (c) the relevant data, reports and statistics, including those provided by Member States, conclude that the EU average of the financing conditions of debt for taxpayers in scope of this directive has more than doubled or halved since the last determination of the risk premium established in paragraph 2.

The percentage of increase or decrease of the risk premium shall take into account the changes in the financing conditions mentioned under point (c) of the first subparagraph other than changes in the risk-free interest rate for the EU as laid down in the implementing acts adopted pursuant to Article 77e(2) of Directive 2009/138/EC, and in any case shall not be greater than the percentage of increase or decrease of the financing conditions mentioned under point (c) of the first subparagraph.

#### *Article 5* ***Anti-Abuse Rules***

1. Member States shall take appropriate measures to ensure that the base of the allowance on equity does not include the amount of any increase which is the result of:
  - (a) granting loans between associated enterprises;
  - (b) a transfer between associated enterprises of participations or of a business activity as a going concern;
  - (c) a contribution in cash from a person resident for tax purposes in a jurisdiction that does not exchange information with the Member State in which the taxpayer seeks to deduct the allowance on equity.

This paragraph shall not apply if the taxpayer provides sufficient evidence that the relevant transaction has been carried out for valid commercial reasons and does not lead to a double deduction of the defined allowance on equity.

2. Where an increase in equity is the result of a contribution in kind or investment in an asset, Member States shall take the appropriate measures to ensure that the value of the asset is taken into account for the calculation of the base of the allowance only where the asset is necessary for the performance of the taxpayer's income-generating activity.

If the asset consists of shares, it shall be taken into account at its book value.

If the asset is other than shares, it shall be taken into account at its market value, unless a different value has been given by a certified external auditor.

3. Where an increase in equity is the result of a reorganisation of a group, such increase shall only be taken into account for the calculation of the base of the allowance on equity for the taxpayer in accordance with Article 4 to the extent that it does not result in converting into new equity the equity (or part thereof) that already existed in the group before the re-organisation.

#### *Article 6* ***Limitation to Interest Deduction***

1. Member States shall ensure that a taxpayer is able to deduct from its taxable base for corporate income tax purposes exceeding borrowing costs as defined in Article 1,

point (2), of Council Directive (EU) 2016/1164<sup>35</sup> up to an amount (a) corresponding to 85% of such costs incurred during the tax period. If such amount is higher than the amount (b) determined in accordance with Article 4 of Directive (EU) 2016/1164, Member States shall ensure that the taxpayer be entitled to deduct only the lower of the two amounts in the tax period. The difference between the two amounts (a) and (b) shall be carried forward or back in accordance with Article 4 of Directive (EU) 2016/1164.

2. Paragraph 1 shall apply to exceeding borrowing costs incurred from [*OP insert the date of entry into force of this Directive*].

## **CHAPTER III MONITORING AND REPORTING**

### *Article 7 Monitoring*

Within 3 months from the end of every tax period, each Member State shall communicate the following information to the Commission regarding the tax period:

- (a) the number of taxpayers that have benefited from the allowance on equity in the tax period, also as a percentage of the total number of taxpayers falling within the scope of this Directive;
- (b) the number of SMEs that have benefitted from the allowance in the tax period, including as a percentage of the total number of SMEs falling within the scope of this Directive and the number of SMEs that have benefitted from the allowance, which are part of large groups within the meaning of Article 3(7) of Directive 2013/34/EU;
- (c) the total amount of expenditure incurred or tax revenue lost due to the deduction of allowance on equity allocated to the allowance on equity as compared to the national gross domestic product of the Member State;
- (d) the total amount of exceeding borrowing costs;
- (e) the total amount of non-deductible exceeding borrowing costs.;
- (f) the number of taxpayers to which anti-abuse measures have been applied in the tax period pursuant to this Directive including the related tax consequences and sanctions applied;
- (g) the data on the evolution in the Member State of the debt/equity ratio, within the meaning of Annex III, parts (A) and (C) to Directive 2013/34/EU.

### *Article 8 Reports*

1. By 31 December 2027, the Commission shall present a report to the European Parliament and to the Council on the implementation of this Directive.

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<sup>35</sup> 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 L 193, 19.7.2016, p. 1).

2. When drawing up the report, the Commission shall take into account the information communicated by Member States pursuant to Article 7.
3. The Commission shall publish the report on its website.

## **CHAPTER IV FINAL PROVISIONS**

### *Article 9 Exercise of Delegation*

1. The power to adopt delegated acts is conferred on the Commission subject to the conditions laid down in this Article.
2. The power to adopt delegated acts referred to in Article 4(5) shall be conferred on the Commission for an indeterminate period of time from [*OP insert the date of entry into force of this Directive*].
3. The delegation of power referred to in Article 4(5) may be revoked at any time by the Council. A decision to revoke shall put an end to the delegation of the power specified in that decision. It shall take effect the day following the publication of the decision in the Official Journal of the European Union or at a later date specified therein. It shall not affect the validity of any delegated acts already in force.
4. Before adopting a delegated act, the Commission shall consult experts designated by each Member State in accordance with the principles laid down in the Interinstitutional Agreement of 13 April 2016 on Better Law-Making.
5. As soon as it adopts a delegated act, the Commission shall notify it to the Council.
6. A delegated act adopted pursuant to Article 4(5) shall enter into force only if no objection has been expressed by the Council within a period of 2 months of notification of that act to the Council or if, before the expiry of that period, the Council has informed the Commission that it will not object. That period shall be extended by 2 months at the initiative of the Council.

### *Article 10 Informing the European Parliament*

The European Parliament shall be informed of the adoption of delegated acts by the Commission, of any objection to them, and of the revocation of a delegation of powers by the Council.

### *Article 11 Transposition*

1. Member States shall adopt and publish, by [31 December 2023] at the latest, the laws, regulations and administrative provisions necessary to comply with this Directive. They shall forthwith communicate to the Commission the text of those provisions.

They shall apply those provisions from [1 January 2024].

When Member States adopt those provisions, they shall include a reference to this Directive or accompany those provisions with such a reference on the occasion of

their official publication. Member States shall determine how such reference is to be made.

2. Member States may defer the application of the provisions of this Directive to taxpayers that on [1 January 2024] benefit from an allowance on equity under national law for a period up to 10 years and in no case for a period longer than the duration of the benefit under national law.
3. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

*Article 12*  
***Entry into force***

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

*Article 13*  
***Addressees***

This Directive is addressed to the Member States.

Done at Brussels,

*For the Council*  
*The President*