30th March 2026

European Commission's initiative: Simplifying EU rules on direct taxation

Finnwatch is a Finnish NGO investigating human rights and climate impacts of business operations as well as tax responsibility of corporations. We appreciate the opportunity to present our views on the European Commission's initiative: Simplifying EU rules on direct taxation. In our written feedback we will mostly focus on the revision needs of ATAD identified in our own research. In addition, we discuss the need to harmonize personal income taxation in order to ensure effective taxation of HNWIs. We are also happy to provide additional information if needed (saara.hietanen@finnwatch.org / +358 44 240 8500).

1. Further harmonization of ATAD based tax rules would both simplify the EU tax rules and make them more effective

The EU Commission's calls for simplification of the tax system are reasonable, given the administrative burden of navigating 27 distinct national tax systems. However, it is important to consider carefully revisions to directives such as ATAD in order not to undermine their policy objectives. Many proposals framed as "simplifications" risk creating more space for profit shifting and aggressive tax planning. Such outcomes would directly contradict the goal of preserving ATAD's effectiveness – a priority highlighted by both the Commission[1] and the Parliament[2].

Furthermore, any erosion of the tax base would jeopardize member states' revenues at a pivotal moment. The fiscal demands of responding to Russian aggression, increasing defense expenditures, and financing the green transition all require robust and reliable tax receipts. The EU must remain vigilant against harmful tax competition driven by legislative loopholes, and ATAD plays a crucial role in this.

In our view, the best way to simplify ATAD-based rules is through further harmonization. By reducing the number of discretionary options (mostly optional carve-outs) the EU can simultaneously reduce fragmentation and strengthen the anti-avoidance measures.

Our research from Finland indicates that significant vulnerabilities remain within the current ATAD framework. These weaknesses continue to allow multinational corporations to shift profits and artificially reduce their tax liabilities, with many of these issues stemming directly from optional carve-outs. The following sections detail our findings and offer specific recommendations for strengthening the directive.

[1] EU Commission Call for evidence on Simplifying EU rules on direct taxation: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/16912-Simplifying-EU-rules-on-direct-taxation-omnibus_en

[2] European Parliament resolution of 9 October 2025 on the role of simple tax rules and tax fragmentation in European competitiveness (2024/2118(INI)): https://www.europarl.europa.eu/doceo/document/TA-10-2025-0227_EN.pdf

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1.1 Interest limitation rules

Interest limitations play a crucial role in preventing profit shifting. However, based on the research conducted by Finnwatch, the following options given to member states in ATAD have proven highly problematic:

- possibility to grant all companies the right to deduct borrowing costs up to EUR 3 million (so-called EUR threshold)
- possibility to exclude loans that were concluded before 17 June 2016
- possibility to give the taxpayers the right to fully deduct all borrowing costs if the taxpayer can demonstrate that the ratio of its equity over its total assets is equal to or higher than the equivalent ratio of the group (so-called equity escape rule).

Whereas the so-called EBITDA rule takes into account the size of a firm's business, the EUR threshold does not. Hence, the EUR threshold basically allows smaller companies to shift all their profits abroad. It is particularly problematic when applied to intra-group interests, since intra-group financial arrangements are one of the most commonly used means to shift profits abroad.

In Finland the EUR threshold is set to EUR 500 000 for intra-group interests and to EUR 3 million for interests paid to non-related parties. While the Finnish threshold for intra-group interests is far better than the EUR 3 million that is adopted in many other member states, our research shows it still opens up significant possibilities for profit shifting. When we investigated investment structures that foreign investors used in their Finnish forest investments, we found out that the investors were able to shift the majority of their Finnish-born profits abroad using intra-group financing arrangements[3]. The most common reason for the deductibility of all interests was that they did not exceed the EUR 500 000 threshold (while the interests were much higher than what could have been deducted under the EBITDA rule).

Another study conducted by Finnwatch shows that applying the EUR thresholds on entity level provides large groups wide possibilities to circumvent the regulation. According to our study, Finland's biggest real estate investor company had transferred the group's loans from its parent company balance sheet to its numerous subsidiaries in order to multiply the amount of interest the group can pay to its Luxembourg-based owner and deduct in Finland[4]. The company in question has 200+ subsidiaries in Finland meaning that the total amount the group entities could deduct rose extremely high, since each individual subsidiary is allowed to deduct interests up to EUR 500 000.

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[3] Finnwatch. (2023). Tapaustutkimus: kansainvälisten metsärahastojen ja -sijoitusyhtiöiden verojärjestelyt. Tutkimusartikkeli. https://finnwatch.org/images/pdf/Tutkimusartikkeli_Tapaustutkimus_kansainvalisten_metsarahastojen_ja_sijoitusyhtioiden_verojarjestelyt.pdf

[4] Finnwatch. (2020). Aggressiivista verosuunnittelua kiinteistöalalla. Tutkimusartikkeli. https://finnwatch.org/fi/tutkimukset/aggressiivista-verosuunnittelua-kiinteistoealalla

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<u>Recommendation:</u> ATAD should require all member states to apply the EUR thresholds on group-level. Alternatively, an even better option would be to abandon the EUR thresholds and stick to the EBITDA rule, which takes into account the size of the business.

The provision that exempts loans that were concluded before 17 June 2016 is also problematic, since it opens up tax planning opportunities and can lead to remarkably lower taxation in the country of operation. When Finnwatch conducted a case study on the financial arrangements of a large Finnish electricity network company in 2020, half of the company's loans fulfilled the exemption criteria[5]. The total amount of interest exempted rose up to EUR 35 million. This obviously lowered the company's tax bill remarkably. While there may have been some basis for a transitional exemption for old loans, it is very difficult to come up with good reasons for having such a generous exemption still in place several years after the adoption of ATAD.

<u>Recommendation:</u> The option to grant exemption to loans concluded before 17th June 2016 should be removed from ATAD.

Finland has also used the option to include an equity escape clause in the national legislation. The clause that allows certain companies to deduct unlimited interest expenses can provide enormous opportunities for profit shifting and tax avoidance. Many businesses have the possibility to arrange their financing in a way that the equity / asset ratio remains higher in the local entity as compared to the group financial statements prepared by the ultimate parent company. If no further conditions are set, the equity escape clause can then exempt all interests paid to the owners of the group from interest limitations.

This was the case in Finland for several years before the conditions required for applying the clause were made stricter a few years ago. Basically groups that pay more than 20 percent of their interests to group's material owners are no longer allowed to apply the equity escape clause. According to our recent study this change was effective in curbing aggressive tax planning: after the change a large electricity network company that previously applied the equity escape clause and was thus able to deduct substantive interests paid to its owners is no longer able to abuse the loophole[6]. Consequently, the taxes paid by the company in Finland have doubled.

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[5] Finnwatch. (2020). Sähkönsiirtoyhtiöt välttävät veroja korkojärjestelyillä. Tutkimusartikkeli. https://finnwatch.org/fi/tutkimukset/saehkoensiirtoyhtioet-vaelttaevaet-veroja-korkojaerjestelyillae

[6] Finnwatch. (2025). Loppu korkokikkailulle? – Verolakimuutosten vaikutukset sähkönsiirtoyhtiöiden verovälttelyyn. Tutkimusartikkeli. https://finnwatch.org/fi/tutkimukset/loppu-korkokikkailulle-verolakimuutosten-vaikutukset-saehkoensiirtoyhtioeiden-verovaelttelyyn. Media coverage in English: https://www.helsinkitimes.fi/finland/finland-news/domestic/26158-tax-reform-stops-caruna-s-profit-shifting-adds-millions-to-state-revenue.html

While restrictions like the one Finland adopted some years ago can help to curb tax avoidance schemes exploiting the equity escape clause, it is worth considering whether the option to provide such exemption should be removed from ATAD altogether. At least member states should be required to ensure the legislation contains sufficient provisions to prevent the abuse of the clause.

Recommendation: The option to include an equity escape clause in the national legislation should be removed from ATAD.

It is also important to ensure that the ATAD-based regulation applies to all types of entities and structures. In Finland certain joint structures (*yhteisetuudet* in Finnish) are excluded from the interest limitations and according to our study, this has been abused by foreign investors. In a study conducted in 2023 we found out that a large French financial institution is using such an exempted structure in its forest investments in Finland[7]. Since the interest limitations do not apply to this structure, the company is able to shift all profits abroad in the form of intra-group interests.

Recommendation: It should be made compulsory for member states to apply ATAD-based regulation to all types of entities and structures.

1.2 CFC rules

CFC rules are designed to prevent the abuse of foreign low-taxed entities in tax avoidance. If the conditions listed in ATAD are met, the CFC rules allow a member state to tax a resident entity (or other type of taxpayer) for the income received by a controlled foreign company. A foreign company can be regarded as 'a controlled foreign company' if the resident taxpayer holds at least 50 percent participation in the foreign company and foreign company's profits are subject to CIT that is less than half of what would be paid in the member state where the taxpayer is resident. These thresholds can be seen as somewhat loose, since in some cases the tax benefits arising from the use of foreign companies can be remarkable even if the difference between the CIT rates is smaller. While the member states are allowed to implement stricter thresholds than those introduced in the directive, most member states find it hard to go any further than the peers. Thus, the minimum standards introduced in ATAD play a crucial role and basically define the EU-wide standard level.

Recommendation: Setting the low-tax threshold higher would make the CFC rules more effective. Lowering the participation requirement would have the same effect.

[7] Finnwatch. (2023). Tapaustutkimus: kansainvälisten metsärahastojen ja -sijoitusyhtiöiden verojärjestelyt. Tutkimusartikkeli. https://finnwatch.org/images/pdf/Tutkimusartikkeli_Tapaustutkimus_kansainvalisten_metsarahastojen_ja_sijoitusyhtioiden_verojarjestelyt.pdf

ATAD provides two options for defining what income earned by the foreign controlled company will be attributed to the parent company tax base and taxed in its resident country. Basically member states can choose to tax only income arising from non-genuine arrangements that have been put in place in order to obtain a tax advantage (transactional approach). Alternatively, member states can choose to tax certain types of passive income (non-transactional approach). Here again, limiting the options would reduce fragmentation between member states. Tax Justice Network, for instance, has recommended phasing out transactional regimes, which the organization reckons less effective in curbing tax avoidance as compared to the non-transactional approach[8].

However, severe weaknesses are not limited to the transactional approach. The biggest problem in current CFC rules is that the rules can very seldom be applied to controlled foreign companies located in other member states. The reason for this is the substantive economic activity carve-out (substance carve out), which exempts entities located in EEA countries if they carry out substantive economic activities in their country of residence[9]. Basically an entity can be regarded as carrying out 'substantive economic activities' if the company employs a single employee and rents a small office space in its country of residence. The costs of doing so are in many cases remarkably lower than the tax advantage received by shifting profits to the low-taxed entity. Thus, some companies can circumvent the CFC rules by setting up a small office in another EEA country. The fact that CFC rules very rarely apply to EEA-located entities is particularly problematic taking into account that in the EU majority of profit shifting takes place from one member state to another[10].

Unfortunately the problem cannot be solved by simply removing the carve-out from ATAD, since the carve-out was added to the directive to align the rules with ECJ case Cadbury Schweppes (C-196/04) and the freedom of establishment. The EU should, however, find ways to tackle the problem, since currently the CFC rules are not effective in preventing profit shifting from one member state to another. One option could be to investigate if the Danish CFC rules are working more effectively than those in other EU countries, since Denmark has adopted a slightly different approach in its CFC legislation. The possibility to extend the carve-out to entities located in non-EEA countries should also be removed from ATAD as a wider scope for carve-out makes the CFC rules even weaker. This could be easily done as the Cadbury Schweppes case only affects rules related to EEA countries.

[8] Tax Justice Network. (2024). ATAD Public Consultation – Submission by the Tax Justice Network. https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/14287-Anti-tax-Avoidance-Directive-ATAD-evaluation/F3495217_en

[9] The problems related to the carve-out are widely discussed in Tokola, A. (2023). Changes to the Finnish CFC Regime: What Were the Effects?. Nordic Tax Journal Volume 2023 (2023): Issue 1 (December 2023). https://doi.org/10.2478/ntaxj-2022-0010

[10] See f.ex. Tørsløv, T., Wier, L. & Zucman, G. (2022). The Missing Profits of Nations. https://gabriel-zucman.eu/files/TWZ2022Restud.pdf

<u>Recommendation:</u> Investigate Danish CFC rules as a possible model for revised EU-wide CFC rules. Remove the option to extend the substance carve-out to non-EEA countries.

Recently, there has also been debate about whether the CFC rules are still needed now that we have the Pillar 2 minimum tax rules in place. In regard to this, it is crucial to keep in mind that the scope of the rules is completely different: while the current CFC rules apply to companies of all sizes, the minimum tax rules only apply to the largest multinationals. There are also major differences in the tax base and due to the recent side-by-side changes, the minimum tax rules can no longer be applied to corporations that have their ultimate parent entity in the US. This means that also the geographical scope of minimum tax rules is more limited. So far we also have very little knowledge on the real effectiveness of the minimum tax rules. Following this, there is absolutely no reason to limit the scope of the CFC rules or to make any other changes that could make the CFC rules less effective at the moment.

<u>Recommendation:</u> EU should refrain from any changes that could make the CFC rules less effective (incl. limiting the scope of the rules).

1.3 Exit taxation

The exit tax rules in ATAD aim to prevent companies from transferring assets from a high-tax country to a low-tax country in order to avoid paying taxes for the gains, which have accrued while the company was resident in the high-tax country. The exit tax rules grant the member state a right to tax the accrued value of the assets, calculated as the difference between the market value of the transferred assets at the time of the exit and the acquisition value of the assets decreased with depreciation or amortization made in taxation.

Finnwatch has not conducted research on the exit tax rules for companies, but our research indicates there is an urgent need to establish similar exit tax rules for individuals. While some member states have introduced such rules domestically, there are still a number of member states that are lacking such legislation. This opens up opportunities for tax avoidance, since individuals can currently avoid paying capital gains taxes by moving to a country, which does not levy taxes on capital gains. Minimum level exit tax rules for individuals, added to ATAD or introduced by a separate “ATAD for individuals”, would tackle this type of tax avoidance and help to unify the (currently heterogeneous) existing exit tax rules across the EU.

Finland is one of the member states that have not adopted any exit tax rules applicable for individuals. A Finnwatch study published in 2023 indicates that this is abused by wealthy individuals. According to our study, the wealthy individuals move to “low-tax countries” remarkably more often than the less wealthy[11]. In this case, by “low-tax countries” we mean countries that either have low or no capital gains taxation or countries that offer preferential tax treatment to HNWIs that choose to relocate themselves. While the number of HNWIs moving abroad for tax reasons is not likely to be big, it still has effects on the tax revenue collected as well as the fairness of the tax system. The problem should be solved by introducing an exit tax. While it could also be introduced nationally, an EU-level exit tax would bring greater benefits by protecting the member states from base erosion, curbing the rising tax competition on wealthy individuals and ensuring that exit taxes are unified in all member states.

Recommendation: Create minimum level exit tax rules for individuals, by adding them to ATAD or introducing a separate “ATAD for individuals”.

2. Actions to tackle fragmentation are also needed in PIT

While the Commission's focus has been in simplifying corporate income taxation, similar efforts are also needed in personal taxation. The lack of common minimum standards, particularly in the field of taxing capital and capital income, is creating arbitrage opportunities for HNWIs and causing member states tax income losses. The rise of preferential tax schemes offered to HNWIs has exacerbated the problem. Common minimum standards are also needed to tackle the rising wealth inequality and wealth concentration.

The wealth of the very richest is increasing at an unprecedented pace. In 2024, Oxfam reported that the world's five richest men had doubled their wealth since 2020, while during the same period five billion people had become even poorer[12]. In 2024, the pace only accelerated: according to Oxfam, billionaires' wealth grew three times faster in 2024 than in the previous year[13].

In countries like the US the concentration of wealth is already becoming a serious threat to democracy. However, the problem is very much present in the EU too[14], and the EU should urgently take actions to tackle the problem.

[11] Finnwatch. (2023). Maastamuuttajan omaisuustulojen ja kohdemaan verotuksen välinen yhteys. Seurantaraportti. https://finnwatch.org/fi/julkaisut/maastamuuttajan-omaisuustulojen-ja-kohdemaan-verotuksen-vaelinen-yhteys

[12] Oxfam. (2024) Inequality Inc. How corporate power divides our world and the need for a new era of public action. Report. Available at: https://www.oxfam.org/en/research/inequality-inc

[13] Oxfam. (2025). Takers not Makers: The unjust poverty and unearned wealth of colonialism. Report. Available at: https://www.oxfam.org/en/research/takers-not-makers-unjust-poverty-and-unearned-wealth-colonialism

[14] Oxfam. (20.1.2025). Billionaire wealth in the EU surges by nearly €400 million per day in 2024, with a new billionaire nearly every week. Press release. https://www.oxfam.org/en/press-releases/billionaire-wealth-eu-surges-nearly-eu400-million-day-2024-new-billionaire-nearly

It is not a coincidence that wealth keeps on accumulating to the very richest. It is to a large extent a consequence of chosen tax policy. In most countries capital income is taxed at a lower rate as compared to personal income taxes levied at wages. Further, the current tax systems focusing on 'realized income only' make it easy for a person living on capital income to avoid taxes altogether. Both of these features benefit mainly the very wealthy HNWIs, since they typically earn most of their income as capital income, whereas for the majority of people salary is the main source of income.

The fact that we are currently not taxing unrealized capital gains means that the wealth of the very rich can increase untaxed. Income accrued in a personal holding company is not taxed in personal income taxation unless the company pays dividends to its owners. Rich individuals can easily choose not to. Similarly, the increase in the value of stocks held by a person are only taxed at the moment the person sells the shares.[15] These features mean that the wealth of the HNWIs can grow remarkably in a year, and the person's taxable income still be zero. And often it is not just a question of postponing the taxation. Instead, the rise in the wealth may never be taxed as one's income if it is, for example, not sold but passed forward as inheritance. According to Oxfam, 69 percent of all millionaire wealth in the EU is inherited, not earned[16].

What makes the situation even worse, is that the fragmented capital gains taxation across the EU makes it possible for the HNWIs to escape the taxation of realized capital income too. We have countries that do not tax capital gains, and schemes offering preferential tax treatment to HNWIs are on the rise. According to the EU Tax Observatory, the number of preferential tax regimes targeting foreigners had already risen to 28 in 2021[17]. These regimes inflict revenue losses on other countries and make it more difficult to impose taxes on the HNWIs.

Changes are needed to fix the problem. Options include a global minimum tax for HNWIs, preferably agreed in the UN tax negotiations. However, the UN member states already chose not to include taxing HNWIs as a topic of an early protocol, which would have ensured that the negotiations about the solutions start immediately. This creates uncertainty whether UN-led solutions can be achieved in an adequate time frame and thus, the EU should also move forward and start planning its own minimum tax for the wealthiest. Other actions that could be taken on EU level include (but are not limited to) a minimum tax for capital income,

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[15] See f.ex. EU Tax Observatory. (2024). A blueprint for a coordinated minimum effective taxation standard for ultra-high-net-worth individuals. https://www.taxobservatory.eu/publication/a-blueprint-for-a-coordinated-minimum-effective-taxation-standard-for-ultra-high-net-worth-individuals/

[16] Oxfam. (20.1.2025). Billionaire wealth in the EU surges by nearly €400 million per day in 2024, with a new billionaire nearly every week. Press release. https://www.oxfam.org/en/press-releases/billionaire-wealth-eu-surges-nearly-eu400-million-day-2024-new-billionaire-nearly

[17] EU Tax Observatory. (2021). New Forms of Tax Competition: An Empirical Investigation. Report No 3, p. 3. https://www.taxobservatory.eu/www-site/uploads/2021/11/EU-Tax-Observatory-Report-3-Tax-Competition-November-2021-3.pdf

common minimum standards for inheritance and wealth taxes as well as strict rules for offering preferential tax treatment.

Recommendation: EU should create its own minimum tax for the high net wealth individuals. In addition, EU should consider adopting common minimum standards for capital income, inheritance and wealth taxes as well as strict rules for offering preferential tax treatment.

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