EFB EUROPEAN FAMILY BUSINESSES

EFB Comments on the Proposal for the Debt Equity Bias Allowance Reduction Directive

European Family Businesses (EFB) welcomes the effort and work of the European Commission in its attempts to tackle the Debt and Equity Bias. EFB has maintained, for more than a decade, that the debt-equity bias in taxation, does not reward forward-looking, responsible businesses. Now more than ever, we must build resilience in company finances, and we must incentivise long-term growth.

In view of the challenging economic and geopolitical environment, many companies will be facing an uncertain future. It is vital that the DEBRA proposal is constructed in the most impactful way for companies. We recognise that DEBRA, ultimately, will cost the public purse, but we firmly believe that it is a cost that is vital at this moment in time. Family businesses, mid-caps, and SMEs are the backbone of our economy. They must be given the support to grow and invest responsibly for the next generation.

Therefore, we propose:

1. In relation to the provisions that would restrict t*he deductibility of interest from debt,* whilst we recognise the reasoning behind the inclusion of such provisions, EFB would caution against this approach. Debt financing is critical for all businesses to finance their operations and increasing the relative cost of debt in relation to equity, is not the right solution.

a) The different formulas or ways of financing companies are determined by a set of factors that go beyond the asymmetrical tax treatment of debt vs. equity.

b) Financing decisions are established in the long term; the absence of a transitional regime that allows the current regime to be applied for a reasonable period penalises companies.

Article 11 of the draft Directive allows for a delay in its application in certain Member States whose national legislation already offers benefits from equity deductibility (i.e. Belgium, Cyprus, Italy, Malta, Poland and Portugal). Consideration should be given to the possibility that such a transitional regime could also apply to other States.

c) Another alternative would be to reduce the 15% cap on financial charges to a rate of 10% or 5% to reduce the negative effects on businesses.

2. In addition, while we also recognise the justification given by the European Commission on not including existing equity due to the costs that may be incurred by Member States' public finances, we believe that a

larger portion of equity should be included. Under the current proposal that includes only the increases in equity, the impact on businesses will have a limited effect.

3. Article 5 of the proposed Directive includes certain **anti-abuse rules where more detail is needed**, as their application can be complex for groups of companies. By way of example, the following aspects require further clarification:

a) Increase of equity derived from the granting of loans. This rule seeks to prevent a duplicate increase in equity through the granting of a loan between associates: once in the lending entity, and a second time in the subsidiary of the borrowing entity (after contributing the funds received from the loan). In this case, it should be clarified which of the two increases in equity is the one applicable, and which one is to be corrected.

b) Increase in equity due to the transfer of shareholdings or ongoing business between associated companies. We believe that the transactions affected should be more clearly defined so as not to create future problems of fit and application of this limitation.

c) Likewise, within the limitations included, the increase in equity resulting from contributions in kind or investments in assets, when the asset is not assigned to the company's activity, cannot be taken into account. We believe that the concept of "*investments in an asset*" should be defined to avoid problems of interpretation regarding which specific operations the Directive wishes to limit.

4. From the drafting of the Directive proposal **it is not clear how the rebate is to be calculated in the case of entities forming part of a tax group.**

The proposed directive makes several references to the corporate taxpayer without specifying whether it refers to the taxpayer for each company individually or for the tax group. However, from the mechanics of calculating the base for the rebate, the calculation must be made individually for each company. This reference is relevant for the purposes of determining the concept of "net equity".

5. The proposed Directive limits the application of the reduction in the tax base to 30% of EBITDA. In a similar way to the limitation of net financial expenses, the explanatory notes allow the possibility of using the 30% of EBITDA not consumed in a given year within the following 5 years. However**, there is no mention of this possibility in the articles,** possibly due to an oversight which we hope can be corrected.

EFB would like the hard work that the European Commission has put into the DEBRA proposal to achieve its intended objectives of '…promot[ing] a robust, efficient and fair tax system' as stated in the DEBRA proposal. EFB continues to support DEBRA and offers its continued cooperation to the European Commission.

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