Common Consolidated Corporate Tax Base (CCCTB)

Proposal for a Council Directive and initial comments

Loyens & Loeff CCCTB-team

June 2011
CCCTB

Introduction

On March 16, 2011, the European Commission released a proposal for a council directive on a Common Consolidated Corporate Tax Base (“CCCTB”; the “Proposal”), accompanied by an impact assessment. The CCCTB purports to reduce existing inefficiencies and distortions resulting from the co-existence of twenty-seven different regimes by offering a single set of rules which taxpayers operating within the EU can use to calculate their taxable profits. Under the proposal, the application of the CCCTB is optional for taxpayers. However, once opted into the system, the consolidation with group entities is mandatory.

Taxpayers that opt for the CCCTB regime and form a group will have to file a single tax return with the tax authorities of one Member State for their activities in the entire EU (one-stop-shop system). A single consolidated tax return will be used to establish the corporate tax base and all Member States in which the company or CCCTB group is active will be entitled to tax a certain portion of that base, according to a specific formula based on three equally-weighted factors (assets, labour and sales). This formulary apportionment is one of the more sensitive aspects of the Proposal, not only for the taxpayers concerned, but also for the Member States involved. Despite various impact assessments, it remains to be seen what the consequences will be for the tax revenues of the Member States. Given the current budget constraints in various EU Member States, this aspect will certainly be addressed in the discussions that will take place with respect to the Proposal.

The June 2011 special edition of Highlights & Insights on European Taxation includes the Proposal, a summary of the official impact assessment and comments by Loyens & Loeff tax experts. A copy of this special edition of Highlights & Insights on European Taxation is enclosed.
On June 10 and 11, 2011, the Amsterdam Centre for Tax Law organised a seminar on the Proposal. During the Seminar various representatives from the DG Taxation of the European Commission, the business community and tax consultancy firms, presented their views on the Proposal. The Head of the Unit Analyses and Coordination of Tax Policies of the DG Taxation – Mr. Neale – and several of his staff members, who drafted the Proposal, attended the Seminar.

Recent developments

Pursuant to the EU Treaty, Member States have the right to assess whether legislative proposals by the European Commission comply with the general principles of EU law, including the “principle of subsidiarity”. This principle entails that in areas which do not fall within its exclusive competence, as is the case with direct taxation, the European Union shall act only if and insofar as the objectives of the proposed action cannot be sufficiently achieved by the Member States themselves, but can by reason of the scale or effects of the proposed action better be achieved at the level of the European Union. Proposed legislative acts should also be justified by the European Commission with regard to the principle of subsidiarity. The Proposal therefore contains a paragraph in which the European Commission gives reason for the Proposal in view of the principle of subsidiarity.

Any national Parliament or any chamber of a national Parliament may, within eight weeks from the date of transmission of a proposed legislative act, issue to the Presidents of the European Parliament, the Council and the European Commission a “yellow card” in the form of a reasoned opinion stating why it considers that the proposal in question does not comply with the principle of subsidiarity. Each national Parliament has two votes and if a Member State applies a bicameral system, as is the case in for instance the Netherlands, each chamber has one vote. If the number of yellow cards issued represent at least 1/3 of the total votes (i.e. 18 votes with 27 Member States (1/3 of 54) the so-called “yellow card procedure” has to be applied. Pursuant to this procedure the proposed legislative act must be re-considered by the European Commission. Subsequently, the European Commission may decide to maintain, amend or withdraw the proposal.
Various (chambers of) national Parliaments, including the Netherlands Lower House (*Tweede Kamer*) have issued yellow cards on the Proposal. In addition, other (chambers of) national Parliaments provided comments with respect to subsidiarity and/or proportionality of the Proposal in the form of reasoned opinions without issuing yellow cards. The total number of yellow cards issued against the Proposal amounts to 13. Although this number is not sufficient for a formal yellow card procedure, during the seminar the representative of DG Taxation indicated that DG Taxation will carefully address all comments made by the Member States on short notice.

**CCCTB-seminar June 10 and 11, 2011**

During the seminar there was a lively discussion about various aspects of the Proposal.

There was, for instance, a discussion relating to Article 7 of the Proposal. This article stipulates that a company that opts for the CCCTB-system shall cease to be subject to the national corporate tax arrangements in respect of all matters regulated by the Directive unless stated otherwise. The view of the European Commission seems to be that the Directive will provide an integral EU corporate taxation system that, together with certain other EU laws, will fully replace the national corporate tax law systems of the individual Member States. This would mean that the national corporate tax laws will no longer apply to taxpayers opting for the CCCTB-system, but for certain specific exceptions included in the Directive.

There was also a discussion about the various anti-abuse provisions in the Proposal. The Proposal contains a general anti-abuse rule (article 80) and various specific anti-abuse rules. One of these specific anti-abuse rules is aimed at non-EU low-taxed controlled foreign companies (“CFCs”). The proposed CCCTB tax base includes the non-distributed income of such non-EU CFCs. It seems that under the CCCTB CFC-rules no tax credit for tax paid by the CFC will be allowed. This point, which was confirmed by Mr. Neale, may need some further consideration.
Another point that was addressed was the anti-abuse provision of article 75 of the Proposal. Article 75 stipulates that under certain circumstances an exempt share disposal is treated as a taxable transfer of assets. The provision is aimed at so-called repackaged asset transfers whereby, instead of transferring the assets directly to a third-party buyer, the assets are first transferred to a subsidiary that forms part of the CCCTB group and, subsequently, the shares of such subsidiary are transferred to the third-party buyer. Such a share transfer is taxed as if the assets have been sold directly. Article 75 refers to asset transfers “within the current or previous tax years”. This raised the question whether all previous years should be taken into account or only the previous year (as could be concluded from the German language version of the Proposal and the initial text proposals in the working papers from Commission Services). Mr. Neale indicated that the term “previous tax years” in the first sentence of article 75 of the Proposal mistakenly mentions “years”, while it only intends to address the previous year.

Many other questions and uncertainties of this new system were discussed. The representatives of DG Taxation gave transparent and useful explanations and comments on the CCCTB regime and the political background that should be taken into consideration. Most probably all contributions made during the seminar will be combined in a booklet which will be released later this year.

**Future outlook**

The European Commission aims for the CCCTB to be approved unanimously by the Council in 2013, after consultation with the European Parliament. Following such approval, Member States should implement the CCCTB into national law within two or three years.

DG Taxation indicated during the seminar that the political and economical climate should also be taken into account when choosing the proper moment to send the CCCTB-proposal to the European Parliament and the Council. The calendar of the EU presidencies is also of the essence. In this respect it is interesting to note that also Member States of which (chambers of) parliaments issued yellow cards, will chair the presidency within the next years.
Poland will have the presidency in the second half of 2011, Denmark and Cyprus in 2012, Ireland and Lithuania in 2013 and Greece in the first half of 2014. It is clear that CCCTB is a “long-term”-project and it will take at least several years before it will be adopted, even if only by 9 Member States, which is the minimum number of Member States (1/3rd of 27) that is required to introduce the CCCTB-proposal based on Enhanced Cooperation. This will also leave sufficient time to revise the draft of the Proposal if the European Commission would consider this necessary based on the comments made by the national Parliaments and the comments (to be) made in literature.

Depending on the further developments, the European Commission could also consider to introduce CCCTB in 2 stages, first the introduction of the common base and thereafter the introduction of the consolidation regime. Most of the technical complexities and the concerns from Member States lay in this consolidation. On the other hand, in our view taxpayers can only realize the real benefits of CCCTB if group consolidation within the EU is available.

Loyens & Loeff will follow the CCCTB-developments and will periodically update its CCCTB website which can be found on www.ccctb.nl.

For questions or comments with respect to CCCTB, please feel free to contact one of the members of the Loyens & Loeff CCCTB-team, or your regular contact within Loyens & Loeff NV.

Loyens & Loeff CCCTB-team
This month in H&I

Special edition:
Proposal for a Common Consolidated Corporate Tax Base (CCCTB)

Introduction by Dennis Weber


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INTRODUCTION

For ten years, work has been in progress for a proposal for a council directive on a Common Consolidated Corporate Tax Base (CCCTB). For various (political) reasons, publication of the proposal has been delayed time and again. Finally, on 16 March 2011, the Proposal for the CCCTB saw the light of day.

The CCCTB Proposal could be called unique. Creating an entirely new tax system is no sinecure, certainly now when here, the system encompasses between 9 (if a small core group) and 27 (if the whole of the EU opts in) Member States. In the planning of such a system, many economic, political and budgetary decisions have to be made. In addition, such a system will have fiscal consequences which, given that there has been little or no international experience to fall back on, are difficult to predict.

It is thus not surprising that much is being debated on this proposal and that much debate will follow.

In this special edition of Highlights & Insights on European Taxation, comments are provided on each Chapter of the Proposal for a Council Directive on a CCCTB. In this way, the Editorial Board trusts to contribute to the further debate on the content and desirability of a CCCTB within the EU.

Dennis Weber
( general editor)

DIRECT TAXATION, LEGISLATION

1 Proposal for a Council Directive on a Common Consolidated Corporate Tax Base ('CCCTB'). Comments by Peter Adriaansen, Hans Bakker, Imme Kam, Thies Sanders, Paul Simonis, Matthijs Vogel, Jochem van der Wal and Dennis Weber

On 16 March 2011, the Commission released a proposal for a Council Directive on a Common Consolidated Corporate Tax Base ('CCCTB'), accompanied by an impact assessment. The CCCTB purports to reduce existing inefficiencies and distortions resulting from the co-existence of twenty-seven different regimes by offering a single set of rules which taxpayers operating within the EU can use to calculate their taxable profits. Under the proposal, the application of the CCCTB is optional for taxpayers. Taxpayers that opt for the CCCTB regime will only have to file a single tax return with the tax authorities of one Member State for their activities in the entire EU (one-stop-shop system). A single consolidated tax return will be used to establish the corporate tax base, after which all Member States in which the company or CCCTB group is active would be entitled to tax a certain portion of that base, according to a specific formula based on three equally weighted factors (assets, labour and sales).

The Commission aims for the current proposal to be approved unanimously by the Council in 2013, after consultation with the European Parliament. Member States must have transposed the proposal into national law two or three years after it has been adopted.

It should be recalled that in the long process leading to the proposal, a number of Member States have made reservations. If unanimous approval is not obtained, a smaller group of Member States may voluntarily continue with the CCCTB project by means of enhanced cooperation. The main elements of the proposal are summarized below.

Common corporate tax base

The proposed defines a common corporate tax base, including detailed rules on when taxable profits are deemed to be realized for tax purposes, the tax depreciation of assets, principles of group affiliation and the treatment of income from third countries.

The CCCTB system uses the ‘all in or all out’ principle. If a taxpayer opts for CCCTB, each EU affiliated company that meets the conditions must be included. Once a taxpayer has opted in, the CCCTB is to be applied for a minimum of five years.
Consolidation

The proposal includes a European cross-border corporate tax consolidation. As a consequence, (i) transfer pricing rules do not apply with respect to transactions within a CCCTB group; (ii) internal restructurings are possible without immediate adverse tax consequences; and (iii) tax losses can be utilized and set off across borders.

Eligibility for consolidation (group membership) is determined in accordance with a two-part test based on (i) control (more than 50% of voting rights); and (ii) ownership (more than 75% of equity) or rights to profits (more than 75% of rights giving entitlement to profit).

In calculating the consolidated tax base, profits and losses arising from transactions directly carried out between members of a group are ignored.

Sharing mechanism

The CCCTB does not intend to harmonize the corporate tax rates of the various Member States. The CCCTB is attributed to the different Member States where the companies participating in the CCCTB group are resident, which would subsequently levy corporate tax on the tax base so attributed in accordance with their domestic provisions, including domestic corporate tax rates. The CCCTB is attributed to the various taxpayers by means of a sharing mechanism, which takes the form of the following formula:

Anti-abuse provisions

In addition to a more general anti-abuse provision stating that artificial transactions will be ignored, the proposal also includes more detailed anti-abuse provisions (e.g. CFC, switch over clause).

Administrative framework

Groups will be able to deal with a single tax administration (‘principal tax authority’, namely of the Member State in which the parent company of the group (‘principal taxpayer’) is resident for tax purposes. The proposal also includes an advance ruling mechanism.

European Commission, 16 March 2011, no. COM 2011/121

EUROPEAN COMMISSION
Brussels, COM(2011) 121/4
2011/0058 (CNS)

Proposal for a COUNCIL DIRECTIVE on a Common Consolidated Corporate Tax Base (CCCTB) [SEC(2011) 315] [SEC(2011) 316]

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Explanatory memorandum

1  Context of the proposal
The Common Consolidated Corporate Tax Base (CCCTB) aims to tackle some major fiscal impediments to growth in the Single Market. In the absence of common corporate tax rules, the interaction of national tax systems often leads to over-taxation and double taxation, businesses are facing heavy administrative burdens and high tax compliance costs. This situation creates disincentives for investment in the EU and, as a result, runs counter to the priorities set in Europe 2020 – A strategy for smart, sustainable and inclusive growth. The CCCTB is an important initiative on the path towards removing obstacles to the completion of the Single Market and was identified in the Annual Growth Survey as a growth-enhancing initiative to be frontloaded to stimulate growth and job creation.

The common approach proposed would ensure consistency in the national tax systems but would not harmonise tax rates. Fair competition on tax rates is to be encouraged. Differences in rates allows a certain degree of tax competition to be maintained in the internal market and fair tax competition based on rates offers more transparency and allows Member States to consider both their market competitiveness and budgetary needs in fixing their tax rates.

The CCCTB is compatible with the rethinking of tax systems and the shift to more growth-friendly and green taxation advocated in the Europe 2020 strategy. In designing the common base supporting research and development has been a key aim of the proposal. Under the CCCTB all costs relating to research and development are deductible. This approach will act as an incentive for companies opting in to the system to continue to invest in research and development. To the extent that there are economic losses to be offset on a cross-border basis, consolidation under the CCCTB tends to shrink the common base. However, in general, the common base would lead to an average EU base that is broader than the current one, mostly due to the option retained for the depreciation of assets.

A key obstacle in the single market today involves the high cost of complying with transfer pricing formalities using the arm’s length approach. Further, the way that closely-integrated groups tend to organise themselves strongly indicates that transaction-by-transaction pricing based on the ‘arm’s length’ principle may no longer be the most appropriate method for profit allocation. The possibility of cross-border loss offsets is only made possible in a limited number of circumstances within the EU, which leads to over-taxation for companies engaged in cross-border activities. In addition, the network of Double Tax Conventions (DTCs) does not offer an appropriate solution for the elimination of double taxation in the single market, as it is designed to operate in a bilateral context at the international level, rather than within a closely integrated setting.

The CCCTB is a system of common rules for computing the tax base of companies which are tax resident in the EU and of EU-located branches of third-country companies. Specifically, the common fiscal framework provides for rules to compute each company's (or branch's) individual tax results, the consolidation of those results, when there are other group members, and the apportionment of the consolidated tax base to each eligible Member State.

The CCCTB will be available for all sizes of companies; MNEs would be relieved from the fact of certain tax obstacles in the single market and SMEs would incur less compliance costs when they decided to expand commercially to another Member State. The system is optional. Since not all businesses trade across the border, the CCCTB will not force companies not planning to expand beyond their national territory to bear the cost of shifting to a new tax system.

Harmonisation will only involve the computation of the tax base and will not interfere with financial accounts. Therefore, Member States will maintain their national rules on financial accounting and the CCCTB system will introduce autonomous rules for computing the tax base of companies. These rules shall not affect the preparation of annual or consolidated accounts.

There is no intention to extend harmonisation to the rates. Each Member State will be applying its own rate to its share of the tax base of taxpayers.

Under the CCCTB, groups of companies would have to apply a single set of tax rules across the Union and deal with only one tax administration (one-stop-shop). A company that opts for the CCCTB ceases to be subject to the national corporate tax arrangements in respect of all matters regulated by the common rules. A company which does not qualify or does not opt for the system provided for by the CCCTB Directive remains subject to the national corporate tax rules which may include specific tax incentive schemes in favour of Research & Development.

Business operating across national borders will benefit both from the introduction of crossborder loss compensation and from the reduction of company tax related compliance costs. Allowing the immediate consolidation of profits and losses for computing the EU-wide taxable bases is a step towards reducing over-taxation in cross-border situations and thereby towards improving the tax neutrality conditions between domestic and cross-border activities to better exploit the potential of the Internal Market. Calculations on a sample of EU multinationals shows that, on average approximately 50% of non-financial and 17% of financial multinational groups could benefit from immediate cross-border loss compensation.

A major benefit of the introduction of the CCCTB will be a reduction in compliance costs for companies. Survey evidence points to a reduction in the compliance costs for recurring tax related tasks in the range of 7% under CCCTB. The reduction in actual and perceived compliance costs is expected to exert a substantial influence on firms' ability and willingness to expand abroad in the medium and long term. The CCCTB is expected to translate into substantial savings in compliance time and outlays in the case of a parent company setting up a new subsidiary in a different Member State. On average, the tax experts participating in the study estimated that a large enterprise spends over € 140,000 (0.23% of turnover) in tax related expenditure to open a new subsidiary in another Member State. The CCCTB will reduce these costs by € 87,000 or 62%. The savings for a medium sized enterprise are even more significant, as costs are expected to drop from € 128,000 (0.55% of turnover) to € 42,000 or a decrease of 67%.

The proposal will benefit companies of all sizes but it is particularly relevant as part of the effort to support and encourage SMEs to benefit from the Single Market as set out in the review of the Small Business Act (SBA) for Europe. The CCCTB notably contributes to reduced tax obstacles and administrative burdens, making it simpler and cheaper for SMEs to expand their activities across the EU. The CCCTB will mean that SMEs operating across borders and opting into the system will only be required to calculate their corporate tax base according to one set of tax rules. The CCCTB complements the European Private Company (SPE), which is still under discussion in the Council. A common framework for computing the tax base for companies in the EU would be particularly useful for SPEs operating across Member States.

The present proposal is not intended to influence the tax revenues and the impact on the distribution of the tax bases between the EU Member States has been analysed. In fact, the impact

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Results of consultations with the interested parties and impact assessments

(a) Consultations

Following publication of the Company Tax Study in 2001, the Commission led a broad public debate and held a series of consultations.

The most important step in that process was the creation of a Working Group (CCCTB WG) consisting of experts from the tax administrations of all Member States. The CCCTB WG was set up in November 2004 and met thirteen times in plenary sessions up until April 2008. In addition, six sub-groups were established to explore specific areas in more depth and reported back to the CCCTB WG. The role of the national experts was limited to providing technical assistance and advice to the Commission services. The CCCTB WG also met in extended format three times (i.e. December 2005, 2006 and 2007) to allow all key experts and stakeholders from the business, professions and academia to express their views.

Further, the Commission consulted informally, on a bilateral basis, several business and professional associations. Some of those interest groups submitted their views officially. The results of academic research were also considered. Thus, leading scholars furnished the Commission with their insights in connection with various features of the system.

The Commission also organised two events in Brussels (April 2002) and Rome (December 2003 with the Italian Presidency). In February 2008, another conference, co-sponsored by the Commission and an academic institution, took place in Vienna and discussed in detail several items relevant to the CCCTB. Finally, on 20 October 2010, the Commission consulted experts from Member States, business, think tanks and academics on certain topics which its services had reconsidered and further developed since the last meeting of the CCCTB WG in April 2008.

(b) Impact Assessment

A very detailed Impact Assessment has been prepared. It includes the results of the following studies: (i) European Tax Analyzer (ETA); (ii) Price Waterhouse Cooper-Study (PWC); (iii) Amadeus and Orbis database; (iv) Deloitte Study and (v) CORTAX study.

The report follows the Guidelines of Secretariat General for Impact Assessments and thereby it provides: (i) a review of the consultation process; (ii) a description of the existing problems; (iii) a statement of the objectives of the policy; and (iv) a comparison of alternative policy options which could attain the stated objectives. In particular, a CCTB (common tax base without consolidation) and a CCCTB (common tax base with consolidation), both compulsory and optional, are subject to analysis and their respective economic, social and environmental impacts are compared.
Comparison of Policy Options

The impact assessment looks at different options with the aim to improve the competitive position of European companies by providing them with the possibility to compute their EU-wide profits according to one set of rules and, hence, choose a legal environment that best suits their business needs, while eliminating tax costs related to the existence of 27 separate national tax systems. The report considers 4 main policy scenarios, which are compared with the ‘no action’ or ‘status-quo’ scenario (option 1):

(i) An optional Common Corporate Tax Base (optional CCTB): EU-resident companies (and EU-situated permanent establishments) would have the option to compute their tax base pursuant to a set of common rules across the Union instead of any of the 27 national corporate tax systems. ‘separate accounting’ (i.e. transaction-by-transaction pricing according to the ‘arm’s length’ principle) would remain in place for intragroup transactions, as the system would not involve a consolidation of tax results (option 2).

(ii) A compulsory Common Corporate Tax Base (compulsory CCTB): all qualifying EU-resident companies (and EU-situated permanent establishments) would be required to compute their tax base pursuant to a single set of common rules across the Union.

The new rules would replace the current 27 national corporate tax systems. In the absence of consolidation, ‘separate accounting’ would continue to determine the allocation of profit in intragroup transactions (option 3).

(iii) An optional Common Consolidated Corporate Tax Base (optional CCCTB): a set of common rules establishing an EU-wide consolidated tax base would be an alternative to the current 27 national corporate tax systems and the use of ‘separate accounting’ in allocating revenues to associated enterprises. Thus, the tax results of each group member (i.e. EU-resident company or EU-situated permanent establishment) would be aggregated to form a consolidated tax base and re-distributed according to a preestablished sharing mechanism based on a formula. Under this scenario, EU-resident companies and/or EU-situated permanent establishments owned by companies resident outside the Union would be entitled to apply the CCCTB, provided that they fulfil the eligibility requirements for forming a group and all eligible members of the same group opt to apply the common rules (‘all-in all-out’) (option 4).

(iv) A compulsory Common Consolidated Corporate Tax Base (compulsory CCCTB): EU-resident companies and/or EU-situated permanent establishments owned by companies resident outside the Union would be required to apply the CCCTB rules insofar as they fulfilled the eligibility requirements for forming a group.

Impact Analysis

The economic results of the Impact Assessment show that the removal of the identified corporate tax obstacles would allow business to make sounder economic choices and thus improve the overall efficiency of the economy. The options for an optional and compulsory CCCTB will both result in a slightly higher welfare. The optional CCCTB is preferable for a number of reasons. The two main reasons verified in the Impact Assessment are (i) the estimated impact on employment is more favourable and (ii) the enforced change by every single company in the Union to a new method of calculating its tax base (regardless of whether it operates in more than one Member State) is avoided.

The reforms under analysis are potentially associated with important dynamic effects in the long run. The reduction in uncertainty and in the costs (actual and perceived) that companies operating in multiple jurisdictions currently incur is the main channel through which these effects are expected to materialize. Ultimately, this will translate into increased cross-border investment within the Union, stemming both from further expansion of European and foreign multinational enterprises and from de novo investment of purely domestic companies into other Member States. Notably, the elimination of additional compliance costs associated with the obligation to comply with different tax rules across the Union and deal with more than one tax administration (‘one-stop-shop’ principle) are likely to enhance companies’ capacity to expand cross-border. Such a prospect should be particularly beneficial for small and medium enterprises which are mostly affected by the high compliance costs of the current situation.

Although the Impact Assessment points out that the final impact of the introduction of a CCCTB on overall tax revenues depends on the Member States’ own policy choices, it is important that
Member States pay close attention to the revenue effects, in particular given the very difficult budgetary situation in many Member States.

In general, the new rules for the common base would lead to an average EU base that is broader than the current one. To the extent that there are economic losses to be offset on a cross-border basis, consolidation under CCCTB tends to shrink the common base.

In fact, the impact on the revenues of Member States will ultimately depend on national policy choices with regard to possible adaptations of the mix of different tax instruments or applied tax rates. In this respect, it is difficult to predict the exact impacts on each of the Member States. However, the Directive includes a clause to review the impacts after 5 years.

3 Legal elements of the proposal

(a) 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 be vested the legal form of a Directive.

(b) Subsidiarity

This proposal complies with the principle of Subsidiarity.

The system of the CCCTB aims to tackle fiscal impediments, mainly resulting from the fragmentation of the Union into 27 disparate tax systems, that businesses are faced with when they operate within the single market. Non-coordinated action, planned and implemented by each Member State individually, would replicate the current situation, as companies would still need to deal with as many tax administrations as the number of Member States in which they are liable to tax.

The rules set out in this proposal, such as the relief for cross-border losses and tax-free group restructurings, would be ineffective and likely to create distortion in the market, notably double taxation or non-taxation, if each Member State applied its own system. Neither would disparate national rules for the division of profits improve the current – already complex – process of allocating business profits amongst associated enterprises.

The nature of the subject requires a common approach.

A single set of rules for computing, consolidating and sharing the tax bases of associated enterprises across the Union is expected to attenuate market distortions caused by the current interaction of 27 national tax regimes. Further, the building blocks of the system, especially cross-border loss relief, tax-free intra-group asset transfers and the allocation of the group tax base through a formula, could only be materialised under a common regulatory umbrella. Accordingly, common rules of administrative procedure would have to be devised to allow the principle of a ‘one-stop-shop’ administration to function.

This proposal is limited to combatting tax obstacles caused by the disparities of national systems in computing the tax base between associated enterprises. The work that followed up to the Company Tax Study identified that the best results in tackling those obstacles would be achieved if a common framework regulated the computation of the corporate tax base and cross-border consolidation. Indeed, these matters may only be dealt with by laying down legislation at the level of the Union, since they are of a primarily cross-border nature. This proposal is therefore justified by reference to the principle of Subsidiarity because individual action by the Member States would fail to achieve the intended results.

(c) Proportionality

This proposal, being shaped as an optional system, represents the most proportionate answer to the identified problems. It does not force companies which do not share the intention of moving abroad to bear the unnecessary administrative cost of implementing the common rules in the absence of any real benefits.

The present initiative is expected to create more favourable conditions for investment in the single market, as tax compliance costs should be expected to decrease. Further, companies would be likely to derive considerable benefits from the elimination of transfer pricing formalities, the possibility to transfer losses across national borders within the same group as well as from tax-free intra-group reorganisations. The positive impact should outweigh possible additional financial and administrative costs which national tax authorities would have to undergo for the purpose of implementing the system at a first stage.
The measures laid down in this proposal are both suitable and necessary for achieving the desired end (i.e. proportionate). They namely deal with harmonising the corporate tax base, which is a prerequisite for curbing the identified tax obstacles and rectifying the elements that distort the single market. In this regard, it should also be clarified that this proposal does not involve any harmonisation of tax rates (or setting of a minimum tax rate). Indeed, the determination of rates is treated as a matter inherent in Member States’ tax sovereignty and is therefore left to be dealt with through national legislation.

4 Budgetary implication

This proposal for a Directive does not have any budgetary implications for the European Union.

2011/0058 (CNS)
Proposal for a
COUNCIL DIRECTIVE
on a Common Consolidated Corporate Tax Base (CCCTB)
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 Commission,
After transmission of the draft legislative act to the national Parliaments,
Having regard to the opinion of the European Parliament 1,
Having regard to the opinion of the European Economic and Social Committee 2,
Acting in accordance with a special legislative procedure,
Whereas:

(1) Companies which seek to do business across frontiers within the Union encounter serious obstacles and market distortions owing to the existence of 27 diverse corporate tax systems. These obstacles and distortions impede the proper functioning of the internal market. They create disincentives for investment in the Union and run counter to the priorities set in the Communication adopted by the Commission on 3 March 2010 entitled Europe 2020 – A strategy for smart, sustainable and inclusive growth 3. They also conflict with the requirements of a highly competitive social market economy.

(2) Tax obstacles to cross-border business are particularly severe for small and medium enterprises, which commonly lack the resources to resolve market inefficiencies.

(3) The network of double taxation conventions between Member States does not offer an appropriate solution. The existing Union legislation on corporate tax issues addresses only a small number of specific problems.

(4) A system allowing companies to treat the Union as a single market for the purpose of corporate tax would facilitate cross-border activity for companies resident in the Union and would promote the objective of making the Union a more competitive location for investment internationally. Such a system would best be achieved by enabling groups of companies with a taxable presence in more than one Member State to settle their tax affairs in the Union according to a single set of rules for calculation of the tax base and to deal with a single tax administration (‘one-stop-shop’). These rules should also be made available to entities subject to corporate tax in the Union which do not form part of a group.

(5) Since differences in rates of taxation do not give rise to the same obstacles, the system (the Common Consolidated Corporate Tax Base (CCCTB)) need not affect the discretion of Member States regarding their national rate(s) of company taxation.

(6) Consolidation is an essential element of such a system, since the major tax obstacles faced by companies in the Union can be tackled only in that way. It eliminates transfer pricing formalities and intra-group double taxation. Moreover, losses incurred by taxpayers are automatically offset against profits generated by other members of the same group.

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1 OJ C[...], [...], p.[...].
2 OJ C[...], [...], p.[...].
(7) Consolidation necessarily entails rules for apportionment of the result between the Member States in which group members are established.

(8) Since such a system is primarily designed to serve the needs of companies that operate across borders, it should be an optional scheme, accompanying the existing national corporate tax systems.


(10) All revenues should be taxable unless expressly exempted.

(11) Income consisting in dividends, the proceeds from the disposal of shares held in a company outside the group and the profits of foreign permanent establishments should be exempt. In giving relief for double taxation most Member States exempt dividends and proceeds from the disposals of shares since it avoids the need of computing the taxpayer's entitlement to a credit for the tax paid abroad, in particular where such entitlement must take account of the corporation tax paid by the company distributing dividends. The exemption of income earned abroad meets the same need for simplicity.

(12) Income consisting in interest and royalty payments should be taxable, with credit for withholding tax paid on such payments. Contrary to the case of dividends, there is no difficulty in computing such a credit.

(13) Taxable revenues should be reduced by business expenses and certain other items. Deductible business expenses should normally include all costs relating to sales and expenses linked to the production, maintenance and securing of income. Deductibility should be extended to costs of research and development and costs incurred in raising equity or debt for the purposes of the business. There should also be a list of nondeductible expenses.

(14) Fixed assets should be depreciable for tax purposes, subject to certain exceptions. Long-life tangible and intangible assets should be depreciated individually, while others should be placed in a pool. Depreciation in a pool simplifies matters for both the tax authorities and taxpayers since it avoids the need to establish and maintain a list of every single type of fixed asset and its useful life.

(15) Taxpayers should be allowed to carry losses forward indefinitely, but no loss carryback should be allowed. Since carry-forward of losses is intended to ensure that a taxpayer pays tax on its real income, there is no reason to place a time limit on carry forward. Loss carry back is relatively rare in the practice of the Member States, and leads to excessive complexity.

(16) Eligibility for consolidation (group membership) should be determined in accordance with a two-part test based on (i) control (more than 50% of voting rights) and (ii) ownership (more than 75% of equity) or rights to profits (more than 75% of rights giving entitlement to profit). Such a test ensures a high level of economic integration between group members, as indicated by a relation of control and a high level of participation. The two thresholds should be met throughout the tax year; otherwise, the company should leave the group immediately. There should also be a nine-month minimum requirement for group membership.

(17) Rules on business reorganisations should be established in order to protect the taxing rights of Member States in an equitable manner. Where a company enters the group, pre-consolidation trading losses should be carried forward to be set off against the taxpayer's apportioned share. When a company leaves the group, no losses incurred during the period of consolidation should be allocated to it. An adjustment may be made in respect of capital gains where certain assets are disposed within a short period after entry to or exit from a group. The value of self-generated intangible assets should be assessed on the basis of a suitable proxy, that is to say research and development, marketing and advertising costs over a specified period.

(18) When withholding taxes are charged on interest and royalty payments made by taxpayers, the proceeds of such taxes should be shared according to the formula of that tax year. When withholding taxes are charged on dividends distributed by taxpayers, the proceeds of such taxes

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should not be shared since, contrary to interest and royalties, dividends have not led to a previous deduction borne by all group companies.

(19) Transactions between a taxpayer and an associated enterprise which is not a member of the same group should be subject to pricing adjustments in line with the ‘arm’s length’ principle, which is a generally applied criterion.

(20) The system should include a general anti-abuse rule, supplemented by measures designed to curb specific types of abusive practices. These measures should include limitations on the deductibility of interest paid to associated enterprises resident for tax purposes in a low-tax country outside the Union which does not exchange information with the Member State of the payer based on an agreement comparable to Council Directive 2011/16/EU concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation and taxation of insurance premiums and rules on controlled foreign companies.

(21) The formula for apportioning the consolidated tax base should comprise three equally weighted factors (labour, assets and sales). The labour factor should be computed on the basis of payroll and the number of employees (each item counting for half). The asset factor should consist of all fixed tangible assets. Intangibles and financial assets should be excluded from the formula due to their mobile nature and the risks of circumventing the system. The use of these factors gives appropriate weight to the interests of the Member State of origin. Finally, sales should be taken into account in order to ensure fair participation of the Member State of destination. Those factors and weightings should ensure that profits are taxed where they are earned. As an exception to the general principle, where the outcome of the apportionment does not fairly represent the extent of business activity, a safeguard clause provides for an alternative method.

(22) Directive 95/46/EC of the European Parliament and the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data applies to the processing of personal data carried out within the framework of this Directive.

(23) Groups of companies should be able to deal with a single tax administration (‘principal tax authority’), which should be that of the Member State in which the parent company of the group (‘principal taxpayer’) is resident for tax purposes. This Directive should also lay down procedural rules for the administration of the system. It should also provide for an advance ruling mechanism. Audits should be initiated and coordinated by the principal tax authority but the authorities of any Member State in which a group member is subject to tax may request the initiation of an audit. The competent authority of the Member State in which a group member is resident or established may challenge a decision of the principal tax authority concerning the notice to opt or an amended assessment before the courts of the Member State of the principal tax authority. Disputes between taxpayers and tax authorities should be dealt with by an administrative body which is competent to hear appeals at first instance according to the law of the Member State of the principal tax authority.

(24) The Commission should be empowered to adopt delegated acts in accordance with Article 290 of the Treaty on the Functioning of the European Union in order to adapt the Annexes to take into account the changes to the laws of the Member States concerning company forms and corporate taxes and update the list of the nondeductible taxes as well as lay down rules on the definition of legal and economic ownership in relation to leased assets and the calculation of the capital and interest elements of the leasing payments and of the depreciation base of a leased asset. It is necessary that the powers are delegated to the Commission for an indeterminate time, in order to allow the rules to be adjusted, if needed.

(25) In order to ensure uniform conditions for the implementation of this Directive as regards the annual adoption of a list of third country company forms which meet the requirements set out in this Directive, laying down rules on the calculation of the labour, asset and sales factors, the allocation of employees and payroll, assets and sales to the respective factor as well as the valuation of assets for the asset factor and the adoption of a standard form of the notice to opt and of

1 OJ L 64, 11.3.2011, p. 1.
3 OJ L 281, 23.11.1995, p. 31 - 50.
rules on electronic filing, on the form of the tax return, on the form of the consolidated tax return and on the required supporting documentation, powers should be conferred on the Commission. Those powers should be exercised in accordance with Regulation (EU) No 182/2011 of the European Parliament and of the Council of 28 February 2011 laying down the rules and general principles concerning mechanisms for control by the Member States of the Commission’s exercise of implementing powers.1

(26) The objective of this Directive cannot be sufficiently achieved through individual action undertaken by the Member States because of the lack of coordination among national tax systems. Considering that the inefficiencies of the internal market primarily give rise to problems of a cross-border nature, remedial measures must be adopted at the level of the Union. Such an approach is in accordance with the principle of subsidiarity, as set out in Article 5 of the Treaty on the European Union. In accordance with the principle of proportionality, as set out in that Article, this Directive does not go beyond what is necessary to achieve that objective.

(27) The Commission should review the application of the Directive after a period of five years and that Member States should support the Commission by providing appropriate input to this exercise.

HAS ADOPTED THIS DIRECTIVE:

Chapter I Scope

Article 1 Scope
This Directive establishes a system for a common base for the taxation of certain companies and groups of companies and lays down rules relating to the calculation and use of that base.

Article 2 Eligible companies
1. This Directive shall apply to companies established under the laws of a Member State where both of the following conditions are met:
   (a) the company takes one of the forms listed in Annex I;
   (b) the company is subject to one of the corporate taxes listed in Annex II or to a similar tax subsequently introduced.

2. This Directive shall apply to companies established under the laws of a third country where both of the following conditions are met:
   (a) the company has a similar form to one of the forms listed in Annex I;
   (b) the company is subject to one of the corporate taxes listed in Annex II.

3. The Commission may adopt delegated acts in accordance with Article 127 and subject to the conditions of Articles 128, 129 and 130 in order to amend Annexes I and II to take account of changes to the laws of the Member States concerning company forms and corporate taxes.

Article 3 Eligible third country company forms
1. The Commission shall adopt annually a list of third country company forms which shall be considered to meet the requirements laid down in Article 2(2)(a). That implementing act shall be adopted in accordance with the examination procedure referred to in Article 131(2).

2. The fact that a company form is not included in the list of third country company forms referred to in paragraph 1 shall not preclude the application of this Directive to that form.

Comment
This Chapter sets out the scope of the Directive and the eligibility criteria for applying the common tax base.

Article 2 defines separate eligibility criteria, depending on the question whether the applicant is a company established under the laws of a Member State or under the laws of a third (non-EU) State. Both categories of applicants must be subject to a qualifying tax on profits. The qualifying forms of profit taxes will be confirmed in an annex to the Directive under the

procedures of article 127 and further which, unlike the procedures for an amendment of the annexes to the EC Parent Subsidiary Directive and the EC Interest Royalty Directive, does not require unanimity among Member States. The list of qualifying corporation taxes of the draft Directive is similar to the annex of the EC Parent Subsidiary Directive. It is unclear whether partial exemptions from tax or application of special regimes would invalidate the eligibility to the Directive. For instance, certain taxpayers may only be liable to profit tax in respect of certain defined sources of profits or activities, or they may only be liable to tax with the application of beneficial regimes.

The second requirement for eligibility is that applicants established under the laws of a Member State must have a qualifying legal form, which will also be confirmed in an annex to the Directive. As to this annex, the same observations apply as to the annex specifying the qualifying corporation taxes. For applicants established under the laws of a third State, it suffices that they are similar to one of the qualifying legal forms which apply to Member State applicants. Third State applicants, therefore, seem to be subject to less restrictive eligibility criteria than Member State applicants, because third State applicants are not required to have a legal form which has been confirmed in the annex. Nonetheless, the Commission will endeavour to release periodically an indicative list of qualifying third country legal forms (article 3). This differential treatment between Member State applicants vis-à-vis third State applicants begs the question of what eligibility criteria ought to be applied in the case of a migration or re-domiciliation of a third country applicant to a Member State. Should reference then be sought in the laws of establishment of the third country applicant, or the laws of the hosting Member State? In answering this question, is it relevant that such hosting Member State applies the principle of incorporation or the principle of effective management? In light of the residency principles of article 6(3), it may well be the case that an applicant has been established under the laws of a third country and, therefore, does not need to be specifically listed in the annex, whereas the applicant can nonetheless apply the common base to its worldwide income by virtue of being a resident in a Member State.

Jochem van der Wal

Chapter II Fundamental Concepts

Article 4 Definitions

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

(1) ‘taxpayer’ means a company which has opted to apply, the system provided for by this Directive;
(2) ‘single taxpayer’ means a taxpayer not fulfilling the requirements for consolidation;
(3) ‘non-taxpayer’ means a company which is ineligible to opt or has not opted to apply the system provided for by this Directive;
(4) ‘resident taxpayer’ means a taxpayer which is resident for tax purposes in a Member State according to Article 6(3) and (4);
(5) ‘non-resident taxpayer’ means a taxpayer which is not resident for tax purposes in a Member State according to Article 6(3) and (4);
(6) ‘principal taxpayer’ means:
(a) a resident taxpayer, where it forms a group with its qualifying subsidiaries, its permanent establishments located in other Member States or one or more permanent establishments of a qualifying subsidiary resident in a third country; or
(b) the resident taxpayer designated by the group where it is composed only of two or more resident taxpayers which are immediate qualifying subsidiaries of the same parent company resident in a third country; or
(c) a resident taxpayer which is the qualifying subsidiary of a parent company resident in a third country, where that resident taxpayer forms a group solely with one or more permanent establishments of its parent; or
(d) the permanent establishment designated by a non-resident taxpayer which forms a group solely in respect of its permanent establishments located in two or more Member States.
(7) ‘group member’ means any taxpayer belonging to the same group, as defined in Articles 54 and 55. Where a taxpayer maintains one or more permanent establishments in a Member State
other than that in which its central management and control is located, each permanent establishment shall be treated as a group member;

(8) 'revenues' means proceeds of sales and of any other transactions, net of value added tax and other taxes and duties collected on behalf of government agencies, whether of a monetary or non-monetary nature, including proceeds from disposal of assets and rights, interest, dividends and other profits distributions, proceeds of liquidation, royalties, subsidies and grants, gifts received, compensation and ex-gratia payments. Revenues shall also include non-monetary gifts made by a taxpayer. Revenues shall not include equity raised by the taxpayer or debt repaid to it;

(9) 'profit' means an excess of revenues over deductible expenses and other deductible items in a tax year;

(10) 'loss' means an excess of deductible expenses and other deductible items over revenues in a tax year;

(11) 'consolidated tax base' means the result of adding up the tax bases of all group members as calculated in accordance with Article 10;

(12) 'apportioned share' means the portion of the consolidated tax base of a group which is allocated to a group member by application of the formula set out in Articles 86 - 102;

(13) 'value for tax purposes' of a fixed asset or asset pool means the depreciation base less total depreciation deducted to date;

(14) 'fixed assets' means all tangible assets acquired for value or created by the taxpayer and all intangible assets acquired for value where they are capable of being valued independently and are used in the business in the production, maintenance or securing of income for more than 12 months, except where the cost of their acquisition, construction or improvement are less than EUR 1,000. Fixed assets shall also include financial assets;

(15) 'financial assets' means shares in affiliated undertakings, loans to affiliated undertakings, participating interests, loans to undertakings with which the company is linked by virtue of participating interests, investments held as fixed assets, other loans, and own shares to the extent that national law permits their being shown in the balance sheet;

(16) 'long-life fixed tangible assets' means fixed tangible assets' with a useful life of 15 years or more. Buildings, aircraft and ships shall be deemed to be long-life fixed tangible assets;

(17) 'second-hand assets' means fixed assets with a useful life that had partly been exhausted when acquired and which are suitable for further use in their current state or after repair;

(18) 'improvement costs' means any additional expenditure on a fixed asset that materially increases the capacity of the asset or materially improves its functioning or represents more than 10% of the initial depreciation base of the asset;

(19) 'stocks and work-in-progress' means assets held for sale, in the process of production for sale or in the form of materials or supplies to be consumed in the production process or in the rendering of services;

(20) 'economic owner' means the person who has substantially all the benefits and risks attached to a fixed asset, regardless of whether that person is the legal owner. A taxpayer who has the right to possess, use and dispose of a fixed asset and bears the risk of its loss or destruction shall in any event be considered the economic owner;

(21) 'competent authority' means the authority designated by each Member State to administer all matters related to the implementation of this Directive;

(22) 'principal tax authority' means the competent authority of the Member State in which the principal taxpayer is resident or, if it is a permanent establishment of a nonresident taxpayer, is situated;

(23) 'audit' means inquiries, inspections or examinations of any kind conducted by a competent authority for the purpose of verifying the compliance of a taxpayer with this Directive.

**Article 5 Permanent establishment**

1. A taxpayer shall be considered to have a ‘permanent establishment’ in a State other than the State in which its central management and control is located when it has a fixed place in that other State through which the business is wholly or partly carried on, including in particular:

(a) a place of management;

(b) a branch;

(c) an office;
23/5/2011 H:/ORDERS/krw/krwtijd/HI/HI1106 - 11-0835/HI1106_006_unicode.3d pag. 18

(d) a factory;
(e) a workshop;
(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

2. A building site or construction or installation project shall constitute a permanent establishment only if it lasts more than twelve months.

3. Notwithstanding paragraphs 1 and 2, the following shall not be deemed to give rise to a permanent establishment:
   a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the taxpayer;
   b) the maintenance of a stock of goods or merchandise belonging to the taxpayer solely for the purpose of storage, display or delivery;
   c) the maintenance of a stock of goods or merchandise belonging to the taxpayer solely for the purpose of processing by another person;
   d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the taxpayer;
   e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the taxpayer, any other activity of a preparatory or auxiliary character;
   f) the maintenance of a fixed place of business solely for any combination of activities mentioned in points (a) to (e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

4. Notwithstanding paragraph 1, where a person – other than an agent of an independent status to whom paragraph 5 applies – is acting on behalf of a taxpayer and has, and habitually exercises, in a State an authority to conclude contracts in the name of the taxpayer, that taxpayer shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the taxpayer, unless the activities of such person are limited to those mentioned in paragraph 3 which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that paragraph.

5. A taxpayer shall not be deemed to have a permanent establishment in a State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

6. The fact that a taxpayer which is a resident of a State controls or is controlled by a taxpayer which is a resident of another State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either taxpayer a permanent establishment of the other.

Comment

Chapter II provides for definitions of frequently used concepts within the Directive.

Article 4 provides for definitions of a number of terms. Confusingly, this list is not in alphabetical order, and it does not seem to be exhaustive because the Directive frequently uses terms which appear not to have been defined in this article.

Article 5 provides for a definition of the term ‘permanent establishment’ (PE). It appears that this definition matches almost entirely the definition of this term as used in the OECD Model Convention. The concept of PE is relevant for purposes of non-resident applicants, in that the Directive only applies to income which they derive from a PE in a Member State (article 6(7)). Barring a possible application of switch-over to a credit system (article 73), income derived by a Member State resident applicant from a PE in a third country is exempt (article 11, letter (e)).

It should be observed that the Directive does not specifically provide for a provision for income from a foreign immovable property comparable to clause 6 of the OECD Model Convention. It does not automatically follow from the Directive that income derived from immovable property follows the rules of income derived from a PE.

Jochem van der Wal
Chapter III Opting for the system provided for by this directive

Article 6 Opting
1. A company to which this Directive applies which is resident for tax purposes in a Member State may opt for the system provided for by this Directive under the conditions provided for therein.

2. A company to which this Directive applies which is not resident for tax purposes in a Member State may opt for the system provided for by this Directive under the conditions laid down therein in respect of a permanent establishment maintained by it in a Member State.

3. For the purposes of paragraphs 1 and 2, a company that has its registered office, place of incorporation or place of effective management in a Member State and is not, under the terms of an agreement concluded by that Member State with a third country, regarded as tax resident in that third country shall be considered resident for tax purposes in that Member State.

4. Where, under paragraph 3, a company is resident in more than one Member State, it shall be considered to be resident in the Member State in which it has its place of effective management.

5. If the place of effective management of a shipping group member or of a group member engaged in inland waterways transport is aboard a ship or boat, it shall be deemed to be situated in the Member State of the home harbour of the ship or boat, or, if there is no such home harbour, in the Member State of residence of the operator of the ship or boat.

6. A company resident in a Member State which opts for the system provided for by this Directive shall be subject to corporate tax under that system on all income derived from any source, whether inside or outside its Member State of residence.

7. A company resident in a third country which opts for the system provided for by this Directive shall be subject to corporate tax under that system on all income from an activity carried on through a permanent establishment in a Member State.

Article 7 Applicable law
Where a company qualifies and opts for the system provided for by this Directive it shall cease to be subject to the national corporate tax arrangements in respect of all matters regulated by this Directive unless otherwise stated.

Article 8 Directive overrides agreements between Member States
The provisions of this Directive shall apply notwithstanding any provision to the contrary in any agreement concluded between Member States.

Comment

Article 6(1) and (2) confirm the optional character of the Directive for both Member State resident applicants and third country resident applicants. With respect to the former, application of the Directive will apply to all income wherever arising (article 6(6)). With respect to the non-resident applicant, the Directive will only apply to income derived through a PE in a Member State (article 6(2) and (7)). Residency of an applicant is determined by the internationally acceptable principles of registered office, place of incorporation, or place of effective management. The Directive requires that the applicant is not concurrently a resident of a third country under a prevailing tax treaty between a Member State and such third country (article 6(3)). The Directive further provides for a tie-breaker on the basis of effective management in the case of dual residency between Member States.

Articles 7 and 8 make plain that when the Directive is applied, it will supersede all national corporate tax arrangements and tax arrangements between Member States. Other than the provisions of article 14(1)(d) and (j), a question which remains unanswered is the extent to which the Directive will supersede national taxes on profits, for instance, regional and municipal taxes. Working Paper CCCTB/WP/045 summarises various options on this topic which have been considered by the Commission Working Group and experts, and observations of Member States, such as allowing a deduction for (some of) such taxes under the common tax base or permitting Member States to allow for a deduction against the apportioned share of the common tax base. It remains unclear which of the options have been chosen under the proposed Directive.
Chapter IV Calculation of the tax base

Article 9 General principles

1. In computing the tax base, profits and losses shall be recognised only when realised.
2. Transactions and taxable events shall be measured individually.
3. The calculation of the tax base shall be carried out in a consistent manner unless exceptional circumstances justify a change.
4. The tax base shall be determined for each tax year unless otherwise provided. A tax year shall be any twelve-month period, unless otherwise provided.

Article 10 Elements of the tax base

The tax base shall be calculated as revenues less exempt revenues, deductible expenses and other deductible items.

Article 11 Exempt revenues

The following shall be exempt from corporate tax:
(a) subsidies directly linked to the acquisition, construction or improvement of fixed assets, subject to depreciation in accordance with Articles 32 to 42;
(b) proceeds from the disposal of pooled assets referred to in Article 39(2), including the market value of non-monetary gifts;
(c) received profit distributions;
(d) proceeds from a disposal of shares;
(e) income of a permanent establishment in a third country.

Article 12 Deductible expenses

Deductible expenses shall include all costs of sales and expenses net of deductible value added tax incurred by the taxpayer with a view to obtaining or securing income, including costs of research and development and costs incurred in raising equity or debt for the purposes of the business.

Deductible expenses shall also include gifts to charitable bodies as defined in Article 16 which are established in a Member State or in a third country which applies an agreement on the exchange of information on request comparable to the provisions of Directive 2011/16/EU. The maximum deductible expense for monetary gifts or donations to charitable bodies shall be 0.5% of revenues in the tax year.

Article 13 Other deductible items

A proportional deduction may be made in respect of the depreciation of fixed assets in accordance with Articles 32 to 42.

Article 14 Non-deductible expenses

1. The following expenses shall be treated as non-deductible:
(a) profit distributions and repayments of equity or debt;
(b) 50% of entertainment costs;
(c) the transfer of retained earnings to a reserve which forms part of the equity of the company;
(d) corporate tax;
(e) bribes;
(f) fines and penalties payable to a public authority for breach of any legislation;
(g) costs incurred by a company for the purpose of deriving income which is exempt pursuant to Article 11; such costs shall be fixed at a flat rate of 5% of that income unless the taxpayer is able to demonstrate that it has incurred a lower cost;
(h) monetary gifts and donations other than those made to charitable bodies as defined in Article 16;
(i) save as provided for in Articles 13 and 20, costs relating to the acquisition, construction or improvement of fixed assets except those relating to research and development;
(j) taxes listed in Annex III, with the exception of excise duties imposed on energy products, alcohol and alcoholic beverages, and manufactured tobacco.

2. Notwithstanding point (j) of paragraph 1 a Member State may provide for deduction of one or more of the taxes listed in Annex III. In the case of a group, any such deduction shall be applied to the apportioned share of the group members resident or situated in that Member State.

3. The Commission may adopt delegated acts in accordance with Article 127 and subject to the conditions of Articles 128, 129 and 130 to amend Annex III as is necessary in order to include all similar taxes which raise more than 20% of the total amount of corporate tax in the Member State in which they are levied.

Amendments to Annex III shall first apply to taxpayers in their tax year starting after the amendment.

**Article 15 Expenditure incurred for the benefit of shareholders**

Benefits granted to a shareholder who is an individual, his spouse, lineal ascendant or descendant or associated enterprises, holding a direct or indirect participation in the control, capital or management of the taxpayer, as referred to in Article 78, shall not be treated as deductible expenses to the extent that such benefits would not be granted to an independent third party.

**Article 16 Charitable bodies**

A body shall qualify as charitable where the following conditions are met:

(a) it has legal personality and is a recognised charity under the law of the State in which it is established;

(b) its sole or main purpose and activity is one of public benefit; an educational, social, medical, cultural, scientific, philanthropic, religious, environmental or sportive purpose shall be considered to be of public benefit provided that it is of general interest;

(c) its assets are irrevocably dedicated to the furtherance of its purpose;

(d) it is subject to requirements for the disclosure of information regarding its accounts and its activities;

(e) it is not a political party as defined by the Member State in which it is established.

**Comment**

*Article 9* lays down a few general principles, such as the realisation principle and the consistency requirement, which will sound familiar to most of us. Still, the CCCTB draughtsmen have also made a number of interesting choices here. Recognition of profits and especially losses only upon realisation is one of them. Most existing systems probably have some ways to recognise losses before they are realised. A decline in value or usefulness of an asset can be expressed by (partially) writing off its book value, or accelerating depreciation before the asset is actually disposed. The general principle of article 9 appears to be overly restrictive in this respect and may lead to artificial realisations.

*Article 10* sets out the basic concept of the CCCTB tax base. It is revenue based, rather than balance sheet based, i.e. it starts from the profit and loss account, rather than comparing the value of the company at the beginning and the end of the year. Although the outcome should be the same eventually, it may take some adjustment of perspective by those, such as the Dutch, who are used to calculating taxable income starting from the increase in net equity during the tax year.

*Article 11* is amazing because it is so short. The participation exemption in paragraphs (c) and (d) for instance, consists of only nine words. If the existing legislation in Member States is any indication at all, this number will be multiplied by something between a hundred and a thousand before we have a viable operational regime. Paragraph (e) contains a full exemption for income from permanent establishments in third countries, which seems a logical choice. Presumably the standard OECD methodology will apply for calculating the income attributable to a permanent establishment on the basis of the treaties with those third countries. The Directive does not mention this, but it would seem appropriate for the income of the permanent establishment to be calculated in the local currency, in order to avoid that translation
results arise which are exempt or non-deductible for the CCCTB group but invisible in the permanent establishment.

Article 12 states deductible expenses includes costs and expenses incurred with a view to obtaining or securing income. It is not quite clear whether this is intended as an independent restriction on deductibility next to articles 14 and 15. In other words, will there be expenses – apart from the non-deductible items specifically listed in article 14 and the benefits granted to shareholders of article 15 – which are not deductible because they have no bearing on the obtaining or securing of income? And if so, who is to be the judge of that? Gifts to charitable bodies are deductible with a maximum of 0.5% of revenues. But there are gifts to charitable bodies which are made with a view to securing or obtaining revenue. Directors of companies will tell their shareholders that the gifts they make serve no other purpose than that and if the shareholders would not believe them, they would of course demand that the money be distributed to them as dividend, so that they could choose their own charities. Another question raised by this provision is why the gifts regime applies only to monetary gifts. The wording the provision suggests that gifts in kind are deductible without the 0.5% limitation.

Article 13 seems to be no more than a link to the depreciation provisions in articles 32 – 42.

Article 14 contains a list of non-deductible items. I will not go into every single one of them, but merely highlight those of which the meaning is not immediately obvious.

- The specific disallowance of profit distributions and repayments of equity and debt under (a) has its mirror image in article 4(8) where revenue is stated not to include equity raised by the taxpayer of debt repaid to him. Both provisions seem to be stating the obvious, but it has to be kept in mind that the concept of tax base in the directive does not contain any reference to any commonly accepted principles of accounting of profit determination, apparently not even economic common sense. The draftsmen must, therefore, have considered it necessary to specifically rule out these items, even if it is obvious that no sensible accountant would ever seek to deduct them.

- Why a transfer from retained earnings to equity (c) – say a stock dividend – should be mentioned here escapes me. Such book entries represent neither cash outflows, nor, to my knowledge, deductible items under any normal system of profit determination, so it seems unnecessary to exclude them expressly from deduction.

- The term corporate tax in letter (d) is not defined in the Directive. In all events it would presumably include the taxes listed in annex II, but it is not quite clear how this affects profit taxes levied by local authorities, such as the German Gewerbesteuer. See also under article 7 about the question whether such taxes can still be levied at all once a company has opted into the common base.

- Costs incurred in connection with exempt income are disallowed. These costs are fixed at 5% of the exempt income in any given year, unless the taxpayer demonstrates that his actual costs – presumably his actual costs connected with exempt income – are lower. For some of the categories of exempt income, such as dividends received and capital gains on shares this will work out as a 95% exemption rather than a full exemption in most cases. Income from permanent establishments is by its nature, already a net concept. Any costs connected with the permanent establishment would normally be taken into account when calculating the exempt result, so this provision should not apply to permanent establishment income.

- The exclusion of monetary gifts and donations under (h) raises the same questions as discussed above under article 12.

- Letter (i) provides that the cost of acquisition, construction or improvement of fixed assets is as such, not deductible. Eventually though, such costs will generally reduce the tax base through the depreciation mechanism, or via the calculation of a taxable gain or loss upon disposal of the asset.

- Annex III lists a number of Member State taxes which paragraph (j) excludes from deduction. The list contains a wide variety of taxes and, frankly, seems a little haphazard. The German Versicherungssteuer, for instance, is on the list, but its Dutch equivalent, the Assurantiebelasting is not. The reasoning behind excluding these taxes from deduction is not immediately obvious. Some of these taxes, such as property transfer taxes, may eventually be taken into account because they form part of the cost price or depreciation base of a fixed asset, but that would not apply to some of the other taxes listed, such as periodic property taxes or motor
vehicle registration taxes. Paragraph (j) makes an exception for excise duties on energy products, alcohol and tobacco, but as excise duties do not seem to be listed in Annex III, it is not clear what the exception refers to.

**Article 15** This provision rules out the deduction of costs incurred for the benefit of shareholders, certain members of their families and associated enterprises. Essentially, this is a codification of the arm’s length principle, as such expenses are disallowed to the extent that they would not be granted to an independent third party. The logical mirror image of this is an exemption for non arm’s length benefits granted by affiliated entities. The draft, however, does not contain such an exemption, so payments which are disallowed under article 15 may still be taxed in the hands of the recipient.

**Article 16** gives a definition of the term charitable bodies. In order to qualify as such, charities have to be recognised by the laws of the State in which they are established, but they also have to meet a number of criteria imposed by the Directive itself.

Thies Sanders

**Chapter V Timing and quantification**

**Article 17 General principles**

Revenues, expenses and all other deductible items shall be recognised in the tax year in which they accrue or are incurred, unless otherwise provided for in this Directive.

**Article 18 Accrual of revenues**

Revenues accrue when the right to receive them arises and they can be quantified with reasonable accuracy, regardless of whether the actual payment is deferred.

**Article 19 Incurrence of deductible expenses**

A deductible expense is incurred at the moment that the following conditions are met:

(a) the obligation to make the payment has arisen;
(b) the amount of the obligation can be quantified with reasonable accuracy;
(c) in the case of trade in goods, the significant risks and rewards of ownership over the goods have been transferred to the taxpayer and, in the case of supplies of services, the latter have been received by the taxpayer.

**Article 20 Costs related to non-depreciable assets**

The costs relating to the acquisition, construction or improvement of fixed assets not subject to depreciation according to Article 40 shall be deductible in the tax year in which the fixed assets are disposed of, provided that the disposal proceeds are included in the tax base.

**Article 21 Stocks and work-in-progress**

The total amount of deductible expenses for a tax year shall be increased by the value of stocks and work-in-progress at the beginning of the tax year and reduced by the value of stocks and work-in-progress at the end of the same tax year. No adjustment shall be made in respect of stocks and work-in-progress relating to long-term contracts.

**Article 22 Valuation**

1. For the purposes of calculating the tax base, transactions shall be measured at:

(a) the monetary consideration for the transaction, such as the price of goods or services;
(b) the market value where the consideration for the transaction is wholly or partly non-monet-
yary;
(c) the market value in the case of a non-monetary gift received by a taxpayer;
(d) the market value in the case of non-monetary gifts made by a taxpayer other than gifts to charitable bodies;
(e) the fair value of financial assets and liabilities held for trading;
(f) the value for tax purposes in the case of non-monetary gifts to charitable bodies.

2. The tax base, income and expenses shall be measured in EUR during the tax year or translated into EUR on the last day of the tax year at the annual average exchange rate for the calendar year.
issued by the European Central Bank or, if the tax year does not coincide with the calendar year, at the average of daily observations issued by the European Central Bank through the tax year. This shall not apply to a single taxpayer located in a Member State which has not adopted the EUR. Nor shall it apply to a group if all group members are located in the same Member State and that state has not adopted the EUR.

**Article 23 Financial assets and liabilities held for trading (trading book)**

1. A financial asset or liability shall be classified as held for trading if it is one of the following:
   (a) acquired or incurred principally for the purpose of selling or repurchasing in the near term;
   (b) part of a portfolio of identified financial instruments, including derivatives, that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking.

2. Notwithstanding Articles 18 and 19, any differences between the fair value at the end of the tax year and the fair value at the beginning of the same tax year, or at the date of purchase if later, of financial assets or liabilities held for trading shall be included in the tax base.

3. When a financial asset or liability held for trading is disposed of, the proceeds shall be added to the tax base. The fair value at the beginning of the tax year, or the market value at the date of purchase if later, shall be deducted.

**Article 24 Long-term contracts**

1. A long-term contract is one which complies with the following conditions:
   (a) it is concluded for the purpose of manufacturing, installation or construction or the performance of services;
   (b) its term exceeds, or is expected to exceed, 12 months.

2. Notwithstanding Article 18, revenues relating to a long-term contract shall be recognised, for tax purposes, at the amount corresponding to the part of the contract completed in the respective tax year. The percentage of completion shall be determined either by reference to the ratio of costs of that year to the overall estimated costs or by reference to an expert evaluation of the stage of completion at the end of the tax year.

3. Costs relating to long-term contracts shall be taken account of in the tax year in which they are incurred.

**Article 25 Provisions**

1. Notwithstanding Article 19, where at the end of a tax year it is established that the taxpayer has a legal obligation, or a probable future legal obligation, arising from activities or transactions carried out in that, or previous tax years, any amount arising from that obligation which can be reliably estimated shall be deductible, provided that the eventual settlement of the amount is expected to result in a deductible expense.

   Where the obligation relates to an activity or transaction which will continue over future tax years, the deduction shall be spread proportionately over the estimated duration of the activity or transaction, having regard to the revenue derived therefrom.

   Amounts deducted under this Article shall be reviewed and adjusted at the end of every tax year. In calculating the tax base in future years account shall be taken of amounts already deducted.

2. A reliable estimate shall be the expected expenditure required to settle the present obligation at the end of the tax year, provided that the estimate is based on all relevant factors, including past experience of the company, group or industry. In measuring a provision the following shall apply:
   (a) account shall be taken of all risks and uncertainties. However, uncertainty shall not justify the creation of excessive provisions;
   (b) if the term of the provision is 12 months or longer and there is no agreed discount rate, the provision shall be discounted at the yearly average of the Euro Interbank Offered Rate (Euribor) for obligations with a maturity of 12 months, as published by the European Central Bank, in the calendar year in the course of which the tax year ends;
   (c) future events shall be taken into account where they can reasonably be expected to occur;
   (d) future benefits directly linked to the event giving rise to the provision shall be taken into account.
**Article 26 Pensions**

In case of pension provisions actuarial techniques shall be used in order to make a reliable estimate of the amount of benefits that employees have earned in return for their service in the current and prior period.

The pension provision shall be discounted by reference to Euribor for obligations with a maturity of 12 months, as published by the European Central Bank. The calculations shall be based on the yearly average of that rate in the calendar year in the course of which the tax year ends.

**Article 27 Bad debt deductions**

1. A deduction shall be allowed for a bad debt receivable where the following conditions are met:
   (a) at the end of the tax year, the taxpayer has taken all reasonable steps to pursue payment and reasonably believes that the debt will not be satisfied wholly or partially; or the taxpayer has a large number of homogeneous receivables and is able to reliably estimate the amount of the bad debt receivable on a percentage basis, through making reference to all relevant factors, including past experience where applicable;
   (b) the debtor is not a member of the same group as the taxpayer;
   (c) no deduction has been claimed under Article 41 in relation to the bad debt;
   (d) where the bad debt relates to a trade receivable, an amount corresponding to the debt shall have been included as revenue in the tax base.

2. In determining whether all reasonable steps to pursue payment have been made, the following shall be taken into account:
   (a) whether the costs of collection are disproportionate to the debt;
   (b) whether there is any prospect of successful collection;
   (c) whether it is reasonable, in the circumstances, to expect the company to pursue collection.

3. Where a claim previously deducted as a bad debt is settled, the amount recovered shall be added to the tax base in the year of settlement.

**Article 28 Hedging**

Gains and losses on a hedging instrument shall be treated in the same manner as the corresponding gains and losses on the hedged item. In the case of taxpayers which are members of a group, the hedging instrument and hedged item may be held by different group members. There is a hedging relationship where both the following conditions are met:

(a) the hedging relationship is formally designated and documented in advance;
(b) the hedge is expected to be highly effective and the effectiveness can reliably be measured.

**Article 29 Stocks and work-in-progress**

1. The cost of stock items and work-in-progress that are not ordinarily interchangeable and goods or services produced and segregated for specific projects shall be measured individually. The costs of other stock items and work-in-progress shall be measured by using the first-in first-out (FIFO) or weighted-average cost method.

2. A taxpayer shall consistently use the same method for the valuation of all stocks and work-in-progress having a similar nature and use. The cost of stocks and work-in-progress shall comprise all costs of purchase, direct costs of conversion and other direct costs incurred in bringing them to their present location and condition. Costs shall be net of deductible Value Added Tax. A taxpayer who has included indirect costs in valuing stocks and work-in-progress before opting for the system provided for by this Directive may continue to apply the indirect cost approach.

3. The valuation of stocks and work-in-progress shall be done in a consistent way.

4. Stocks and work-in-progress shall be valued on the last day of the tax year at the lower of cost and net realisable value. The net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.
Article 30 Insurance undertakings

Insurance undertakings that have been authorised to operate in the Member States, in accordance with Council Directive 73/239/EEC\(^1\) for non-life insurance, Directive 2002/83/EC of the European Parliament and of the Council\(^2\) for life insurance, and Directive 2005/68/EC of the European Parliament and of the Council\(^3\) for reinsurance, shall be subject to the following additional rules:

(a) the tax base shall include the difference in the market value, as measured at the end and the beginning of the same tax year, or upon completion of the purchase if later, of assets in which investment is made for the benefit of life insurance policyholders bearing the investment risk;

(b) the tax base shall include the difference in the market value, as measured at the time of disposal and the beginning of the tax year, or upon completion of the purchase if later, of assets in which investment is made for the benefit of life insurance policyholders bearing the investment risk;

(c) the technical provisions of insurance undertakings established in compliance with Directive 91/674/EEC\(^4\) shall be deductible, with the exception of equalisation provisions. A Member State may provide for the deduction of equalisation provisions. In the case of a group, any such deduction of equalisation provisions shall be applied to the apportioned share of the group members resident or situated in that Member State. Amounts deducted shall be reviewed and adjusted at the end of every tax year. In calculating the tax base in future years account shall be taken of amounts already deducted.

Article 31 Transfers of assets towards a third country

1. The transfer of a fixed asset by a resident taxpayer to its permanent establishment in a third country shall be deemed to be a disposal of the asset for the purpose of calculating the tax base of a resident taxpayer in relation to the tax year of the transfer. The transfer of a fixed asset by a non-resident taxpayer from its permanent establishment in a Member State to a third country shall also be deemed to be a disposal of the asset.

2. Paragraph 1 shall not apply where the third country is party to the European Economic Area Agreement and there is an agreement on the exchange of information between that third country and the Member State of the resident taxpayer or of the permanent establishment, comparable to Directive 2011/16/EU.

Comment

Article 17 chooses the accrual principle as the leading principle for the timing of recognition of revenue and expenses.

Articles 18 and 19 contain further definitions of the terms ‘accrue’ and ‘incurred’. The decisive moment is that when the right to receive a payment or the obligation to make a payment arises.

Article 20 provides that the cost price of a non-depreciable fixed asset may be deducted in the year in which the asset is disposed and the proceeds of the disposal are included in the tax base as revenue. The wording of article 20 is too restrictive, as it allows no deduction for assets which are lost or destroyed. Otherwise, article 20 effectively taxes the capital gain, or deducts the capital loss on disposal of the asset much in the same way existing tax systems do.

Article 21 takes mutations in stocks and work in progress into account, except for work in progress on long-term contracts, as defined in article 24.

Article 22 contains a number of valuation rules. It makes a distinction between market value (for non-monetary transactions and gifts) and fair value (for financial assets held on trading account). The purpose of that terminology is not quite clear, as it seems to me that in practice, the two terms are more or less synonymous. Donations in kind to charities are to be valued at tax book value, which may be higher or lower than market value. This is presumably just a practical measure to avoid valuation disputes, but the effect is that the 0.5% limit on deduction

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of gifts to charities can be circumvented by giving an asset with a lower book value. The deduction of the book value stays within the 0.5% limit, but the higher market value is effectively deducted against the capital gain which would have been realised if the asset had been sold on the open market. The charity is, of course, free to realise that higher value at a later moment anyway.

Article 23 provides that financial assets held for trading are to be valued on a mark to market basis and both realised and unrealised profits and losses in respect of them are to be reported every year.

Article 24 defines long-term contracts as contracts regarding manufacturing, installation construction and the performance of services, the term of which is expected to exceed 12 months. Revenues from these contracts are reported not on an accrual basis (i.e. when the legal entitlement to a remuneration arises), but by reference to the percentage of the contract which is completed by the end of a tax year. That percentage of completion can be determined either from the percentage of estimated total cost incurred, or by an expert evaluation. Obviously the long-term contract regime must be limited to those contracts which provide for a fixed total output, because otherwise no percentage of completion can be determined. Thus for example, a typical toll manufacturing contract will not qualify, even though it is a manufacturing contract and most are expected to run for much longer than 12 months, because the contract will merely state that A will manufacture goods from raw materials provided and owned by B, without stating a fixed total number of units that A undertakes to produce. Without a fixed total, it is impossible to say what percentage of completion A has reached at any given time, so for such contracts, the normal accrual system of profit realisation must apply.

Article 25 sets out the requirements for provisions. (i) There must be a legal obligation or probable future legal obligation, which (ii) arises from activities or transactions carried out in or before the tax year and (iii) which can be reliably estimated. This definition is perhaps slightly restrictive in that it allows no provision for payments which a taxpayer expects to make voluntarily, or out of common decency, even though he is not legally obliged to do so. Paragraph 2 states that a reliable estimate is the amount for which the obligation could be settled as at the end of the tax year, taking into account all risks and uncertainties. I assume that means that if it is uncertain whether a payment will have to be made, the provision has to be calculated on the basis of a probability percentage, rather than providing the (net present value of) the maximum amount that could reasonably be due. Paragraph 2 (c) expressly states that future developments have to be taken into account, provided they can reasonably be expected to occur. This means, for instance, that future inflation has to be taken into account when valuing pension obligations which are linked to a cost of living index. Provisions for defined benefit pensions have to reflect that an employee’s salary may be expected to rise during the remainder of his career, such that his pension entitlements will be higher than calculated on his current salary.

Article 26 contains supplementary rules with respect to pension provisions, basically prescribing the use of actuarial techniques to determine the amount of a pension provision. Surprisingly, the second paragraph requires that taxpayers use 12 month Euribor as the discount percentage, rather than a long-term discount rate in line with the long term character of pension obligations.

Article 27 provides that bad debt losses on an individual receivable may only be deducted once the creditor has taken all reasonable steps to pursue payment. What steps are considered to be reasonable depends on the expected cost of collecting the debt and the chances of success. In many cases of course – especially with respect to related party debt – no steps will be taken at all and the deduction will be based solely on the argument that the chances of successfully collecting the amount owed are too slim in relation to the cost. It is not fully clear what the relation is between article 27 and the exceptional depreciation rule in article 41, which seems to offer the same possibility for a deduction, but without the reasonable steps test.

There is a specific provision for large portfolios of homogeneous receivables, which may be written off on a percentage basis if a reliable estimate can be made of the amount which will eventually turn out to be uncollectable. If the debt is a trade receivable, the loss may only be deducted if a corresponding amount has been included in the tax base as revenue.

Article 28 sets out rules for hedging. The first requirement is, of course, that the hedge
instrument is suitable and effective. If that is the case, hedge treatment is applied provided the hedge instrument is ‘formally designated and documented’ as such in advance by the taxpayer. Precisely what formalities have to be met is not clarified, but this provision seems to leave a lot of space for manoeuvre, as it is essentially the taxpayer who decides whether or not to fulfil the formalities. If there is a hedging relationship, the hedge instrument is treated in the same way as the hedged item. This means that if the hedge concerns a risk on an exempt item, such as a portfolio of shares, the gain or loss on the hedge instrument will be exempt as well. Also in terms of timing, the hedge will follow the underlying risk, so the hedge result will be taken into account at the same time as the underlying gain or loss is realised.

Article 29 deals with the valuation of stocks and work in progress. It is noted that there is a separate set of rules for work in progress on long-term contracts (article 24). Stocks of interchangeable goods are to be valued at direct cost or lower net realisable value, on a LIFO basis. If a taxpayer had included indirect costs in his stocks valuation prior to opting into the common base system, he may continue to do so.

Thies Sanders

Chapter VI Depreciation of fixed assets

Article 32 Fixed asset register
Acquisition, construction or improvement costs, together with the relevant date, shall be recorded in a fixed asset register for each fixed asset separately.

Article 33 Depreciation base
1. The depreciation base shall comprise any cost directly connected with the acquisition, construction or improvement of a fixed asset.
   Costs shall not include deductible value added tax.
   In the case of fixed assets produced by the taxpayer, the indirect costs incurred in production of the asset shall also be added to the depreciation base in so far as they are not otherwise deductible.
2. The depreciation base of an asset received as a gift shall be its market value as included in revenues.
3. The depreciation base of a fixed asset subject to depreciation shall be reduced by any subsidy directly linked to the acquisition, construction or improvement of the asset as referred to in Article 11(a).

Article 34 Entitlement to depreciate
1. Subject to paragraph 3, depreciation shall be deducted by the economic owner.
2. In the case of leasing contracts in which economic and legal ownership does not coincide, the economic owner shall be entitled to deduct the interest element of the lease payments from its tax base. The interest element of the lease payments shall be included in the tax base of the legal owner.
3. A fixed asset may be depreciated by no more than one taxpayer at the same time. If the economic owner of an asset cannot be identified, the legal owner shall be entitled to deduct depreciation. In that case the interest element of the lease payments shall not be included in the tax base of the legal owner.
4. A taxpayer may not disclaim depreciation.
5. The Commission may adopt delegated acts in accordance with Article 127 and subject to the conditions of Articles 128, 129 and 130 in order to lay down more detailed rules concerning:
   (a) the definition of legal and economic ownership, in relation in particular to leased assets;
   (b) the calculation of the capital and interest elements of the lease payments;
   (c) the calculation of the depreciation base of a leased asset.

Article 35 Depreciation of improvement costs
Improvement costs shall be depreciated in accordance with the rules applicable to the fixed asset which has been improved as if they related to a newly acquired fixed asset.
**Article 36 Individually depreciable assets**

1. Without prejudice to paragraph 2 and Articles 39 and 40, fixed assets shall be depreciated individually over their useful lives on a straight-line basis. The useful life of a fixed asset shall be determined as follows:
   
   (a) buildings: 40 years;
   
   (b) long-life tangible assets other than buildings: 15 years;
   
   (c) intangible assets: the period for which the asset enjoys legal protection or for which the right is granted or, if that period cannot be determined, 15 years.

2. Second-hand buildings, second-hand long-life tangible assets and second-hand intangible assets shall be depreciated in accordance with the following rules:
   
   (a) a second-hand building shall be depreciated over 40 years unless the taxpayer demonstrates that the estimated remaining useful life of the building is shorter than 40 years, in which case it shall be depreciated over that shorter period;
   
   (b) a second-hand long-life tangible asset shall be depreciated over 15 years, unless the taxpayer demonstrates that the estimated remaining useful life of the asset is shorter than 15 years, in which case it shall be depreciated over that shorter period;
   
   (c) a second-hand intangible asset shall be depreciated over 15 years, unless the remaining period for which the asset enjoys legal protection or for which the right is granted can be determined, in which case it shall be depreciated over that period.

**Article 37 Timing**

1. A full year's depreciation shall be deducted in the year of acquisition or entry into use, whichever comes later. No depreciation shall be deducted in the year of disposal.

2. Where an asset is disposed of, voluntarily or involuntarily, during a tax year, its value for tax purposes and the value for tax purposes of any improvement costs incurred in relation to the asset shall be deducted from the tax base in that year. Where a fixed asset has given rise to an exceptional deduction under Article 41, the deduction under Article 20 shall be reduced to take into account the exceptional deduction already received.

**Article 38 Rollover relief for replacement assets**

1. Where the proceeds from the disposal of an individually depreciable asset are to be re-invested before the end of the second tax year after the tax year in which the disposal took place in an asset used for the same or a similar purpose, the amount by which those proceeds exceed the value for tax purposes of the asset shall be deducted in the year of disposal. The depreciation base of the replacement asset shall be reduced by the same amount.

   An asset which is disposed of voluntarily must have been owned for a minimum period of three years prior to the disposal.

2. The replacement asset may be purchased in the tax year prior to the disposal.

   If a replacement asset is not purchased before the end of the second tax year after the year in which the disposal of the asset took place, the amount deducted in the year of disposal, increased by 10%, shall be added to the tax base in the second tax year after the disposal took place.

3. If the taxpayer leaves the group of which it is a member or ceases to apply the system provided for by this Directive within the first year, without having purchased a replacement asset, the amount deducted in the year of disposal shall be added to the tax base. If the taxpayer leaves the group or ceases to apply the system in the second year, that amount shall be increased by 10%.

**Article 39 Asset pool**

1. Fixed assets other than those referred to in Articles 36 and 40 shall be depreciated together in one asset pool at an annual rate of 25% of the depreciation base.

2. The depreciation base of the asset pool at the end of the tax year shall be its value for tax purposes at the end of the previous year, adjusted for assets entering and leaving the pool during the current year. Adjustments shall be made in respect of acquisition, construction or improvement costs of assets (which shall be added) and the proceeds of disposal of assets and any compensation received for the loss or destruction of an asset (which shall be deducted).

3. If the depreciation base as calculated in accordance with paragraph 2 is a negative amount, an
amount shall be added, so that the depreciation base is zero. The same amount shall be added to the tax base.

Article 40 Assets not subject to depreciation
The following assets shall not be subject to depreciation:
(a) fixed tangible assets not subject to wear and tear and obsolescence such as land, fine art, antiques, or jewellery;
(b) financial assets.

Article 41 Exceptional depreciation
1. If, in exceptional circumstances, a taxpayer demonstrates that the value of a fixed asset not subject to depreciation has permanently decreased at the end of a tax year, it may deduct an amount equal to the decrease in value. However, no such deduction may be made in respect of assets the proceeds from the disposal of which are exempt.
2. If the value of an asset which has been subject to such exceptional depreciation in a previous tax year subsequently increases, an amount equivalent to the increase shall be added to the tax base in the year in which the increase takes place. However, any such addition or additions, taken together, shall not exceed the amount of the deduction originally granted.

Article 42 Precision of categories of fixed assets
The Commission may adopt delegated acts in accordance with Article 127 and subject to the conditions of Articles 128, 129 and 130 in order to define more precisely the categories of fixed assets referred to in this Chapter.

Comment

Article 34 designates the economic owner of a fixed asset as the taxpayer entitled to depreciation deductions. The term economic owner is defined in article 4 (20) as the person who has substantially all the benefits and risks attached to a fixed asset. The exact meaning of substantially all is not clear. Whether economic ownership can be shared in the case of co-ownership, or of a partnership interest also remains an open question. In leasing situations where the lessor retains the legal title to the asset while economic ownership passes to the lessee (financial lease), paragraph 2 provides that the lessee may deduct the interest element in the lease payments and the lessor must include the interest element in his tax base.

Article 35 provides that improvements to fixed assets follow the depreciation regime which applies to the asset as a whole. As a result, for instance, a new air conditioning installation in a building would have to be depreciated over 40 years, even though a reasonable estimate of its useful life would probably be less than half that number. The solution would be to treat such installations as separate assets, but it is not clear to what extent that is allowed.

There are two different systems of depreciation: straight line and the asset pool system. Article 36 prescribes a straight-line depreciation period of 40 years for buildings and 15 years for other tangible assets with a useful life of over 15 years. Intangible assets are depreciated for the period for which they are legally protected, either by law or by contract. The same terms apply to second hand assets, unless the taxpayer can demonstrate a lower remaining useful life.

Article 37 allows a full year of depreciation in the year in which the asset is acquired and first put to use, so there will be a certain tendency to accelerate investment in fixed assets towards the end of the year. There is no depreciation in the year in which an asset is disposed, but that makes no difference, because the remaining tax value of the asset may be deducted upon disposal anyway. It is noted that article 37 speaks of ‘voluntary or involuntary’ disposal, while the equivalent provision for non depreciable assets (article 20) merely mentions disposal. Why there is a difference is not clear. Like disposal, the terms used in other language versions (‘vervreemd’ / ‘cédee’ / ‘veräussert’) seem to suggest that a deduction is allowed only when the asset disappears from the books as a result of a transaction entered into by the taxpayer and not when an asset is lost or destroyed. Here as well, it seems overly restrictive not to allow a deduction for sunken ships and burnt buildings.
Article 38 is an important provision. It contains the rollover relief rules for replacement assets. If a fixed asset (other than assets in the asset pool which is discussed below) which has been owned for at least three years is disposed and an asset with the same or a similar purpose is acquired within two years from the end of the tax year in which the disposal took place, the capital gain on the old asset may be rolled over into the new asset. The actual wording of the provision suggests that rollover relief is compulsory, but it seems questionable whether that was really what the draftsmen had in mind. If the relief has to be undone because the taxpayer does not acquire a replacement asset within two years, a 10% mark up has to be added to the amount for which relief was originally given. This is done apparently to charge a quasi interest on the tax saved in the year in which the original asset was disposed.

Article 39 describes the other system of depreciation, the asset pool. All assets except the ones which qualify for straight-line depreciation under article 36 and the non depreciable assets in article 40 are taken together in a pool, which is depreciated at 25% of the balance in the pool at the end of the previous year. Investments are added to the pool and the proceeds on disposal of assets are deducted from it and if at the end of any year the balance in the pool is negative. The negative balance shall be added back to the tax base to reset the pool to zero.

Article 40 excludes from depreciation those assets which are not subject to wear and tear or obsolescence and financial assets. Article 41 allows an exceptional depreciation for assets which have permanently decreased in value. Exceptional depreciation is limited to non-depreciable assets, so for instance an investor who has bought an office building but cannot find tenants due to an economic downturn will be forced to sell his property to deduct his loss. In practice, this restriction is likely to lead to artificial arrangements whereby investors dispose of their assets for tax reasons, but retain a beneficial interest in them. It would be preferable in my view to be more generous in allowing exceptional depreciation in such situations.

Thies Sanders

Chapter VII Losses

Article 43 Losses

1. A loss incurred by a taxpayer or a permanent establishment of a non-resident taxpayer in a fiscal year may be deducted in subsequent tax years, unless otherwise provided by this Directive.

2. A reduction of the tax base on account of losses from previous tax years shall not result in a negative amount.

3. The oldest losses shall be used first.

Comment

Article 43 If the tax base is negative in any given year, the loss is allocated to the taxpayers in the group on the basis of the sharing formula for that year. So loss carry forward takes place per taxpayer and not for the consolidated group as a whole. A loss incurred in year one may be allocated for 90% to a company in Member State A if the formula so determines. In year two, the group may have restructured its operations and may have moved most of its assets and staff to Member State B and the result would be that a large proportion of the loss would be trapped in Member State A while the future profits would be mostly allocated to Member State B which has no losses to offset. Loss carry forward on the consolidated level would lead to a smoother compensation. Losses can be carried forward indefinitely and there is no carry back.

Thies Sanders

Chapter VIII Provisions on entry to and exit from the system provided for by this directive

Article 44 General rule on recognition and valuation of assets and liabilities

When a taxpayer opts to apply the system provided for by this Directive, all assets and liabilities shall be recognised at their value as calculated according to national tax rules immediately prior to the date on which it begins to apply the system, unless otherwise stated in this Directive.
Article 45 Qualification of fixed assets for depreciation purposes
1. Fixed assets entering the system provided for by this Directive shall be depreciated in accordance with Articles 32 to 42.
2. Notwithstanding paragraph 1, the following depreciation rules shall apply:
   (a) fixed assets that are individually depreciable both under the national corporate tax law previously applicable to the taxpayer and under the rules of the system shall be depreciated according to Article 36(2);
   (b) fixed assets that were individually depreciable under the national corporate tax law previously applicable to the taxpayer but not under the rules of the system shall enter the asset pool provided for in Article 39;
   (c) fixed assets that were included in an asset pool for depreciation purposes under the national corporate tax law previously applicable to the taxpayer shall enter the system in the asset pool provided for in Article 39, even if they would be individually depreciable under the rules of the system;
   (d) fixed assets that were not depreciable or were not depreciated under the national corporate tax law previously applicable to the taxpayer but are depreciable under the rules of the system shall be depreciated in accordance with Article 36(1) or Article 39, as the case may be.

Article 46 Long-term contracts on entering the system
Revenues and expenses which pursuant to Article 24(2) and (3) are considered to have accrued or been incurred before the taxpayer opted into the system provided for by this Directive but were not yet included in the tax base under the national corporate tax law previously applicable to the taxpayer shall be added to or deducted from the tax base, as the case may be, in accordance with the timing rules of national law.

Revenues which were taxed under national corporate tax law before the taxpayer opted into the system in an amount higher than that which would have been included in the tax base under Article 24(2) shall be deducted from the tax base.

Article 47 Provisions and deductions on entering the system
1. Provisions, pension provisions and bad-debt deductions provided for in Articles 25, 26 and 27 shall be deductible only to the extent that they arise from activities or transactions carried out after the taxpayer opted into the system provided for by this Directive.
2. Expenses incurred in relation to activities or transactions carried out before the taxpayer opted into the system but for which no deduction had been made shall be deductible.
3. Amounts already deducted prior to opting into the system may not be deducted again.

Article 48 Pre-entry losses
Where a taxpayer incurred losses before opting into the system provided for by this Directive which could be carried forward under the applicable national law but had not yet been set off against taxable profits, those losses may be deducted from the tax base to the extent provided for under that national law.

Article 49 General rule for opting-out of the system
When a taxpayer leaves the system provided for by this Directive, its assets and liabilities shall be recognised at their value as calculated according to the rules of the system, unless otherwise stated in this Directive.

Article 50 Fixed assets depreciated in a pool
When a taxpayer leaves the system provided for by this Directive, its asset pool under the system provided for by this Directive shall be recognised, for the purpose of the national tax rules subsequently applicable, as one asset pool which shall be depreciated on the declining balance method at an annual rate of 25%.

Article 51 Long-term contracts on leaving the system
After the taxpayer leaves the system, revenues and expenses arising from long-term contracts shall be treated in accordance with the national corporate tax law subsequently applicable. However,
revenues and expenses already taken into account for tax purposes in the system provided for by this Directive shall not be taken into account again.

Article 52 Provisions and deductions on leaving the system
After the taxpayer leaves the system provided for by this Directive, expenses which have already been deducted in accordance with Articles 25 to 27 may not be deducted again.

Article 53 Losses on leaving the system
Losses incurred by the taxpayer which have not yet been set off against taxable profits under the rules of the system provided for by this Directive shall be carried forward in accordance with national corporate tax law.

Comment

The main principle on entry and exit is the rollover of the existing tax book values. This principle is not only applied for the calculation of the profit under the common base, but also for the asset factor in the apportionment of consolidated profit if a CCCTB group is formed.

The Commission had various options: rollover of national tax book values, revaluation of all assets/liabilities up to market value or something in between. The first method is simple. The second is better in theory but most probably not workable. Not only would such revaluation to market value be a time-consuming and costly exercise, it would also raise the question of how to treat the difference between market value and tax book value. In most cases, immediate taxation by the Member State upon entry would be prohibitive to opting into the system. A tax at a discounted tax rate would accommodate that to a certain extent but whether that would be considered sufficient by taxpayers to opt for the system, will very much depend on the particulars of the case at hand. Spreading gain recognition over a number of years comes close to a rollover of the tax book value (although it would lead to a different profit apportionment within a CCCTB group). The third method would be some kind of compromise if the first method would lead to an unacceptable outcome. The Commission has chosen for simplicity and has proposed the first method. The proposal only provides for a few adjustments to avoid that costs are deducted twice or that income is included in the tax base twice. For the sharing mechanism, some further adjustments have been proposed which are dealt with in Chapter X.

This choice to start with the tax book value applicable under the national tax law at the time the option for the system is exercised (the group is formed), raises the question whether specific rules apply under national law which affect the entrance value in a special way. A few examples:

i depreciation at will may lead to a lower (or higher) tax book value than usual;
ii gain recognition on sales of assets may have been postponed by deducting such gain from the investment costs of the replacing asset. This will lead to a low tax book value;
iii subsidies/incentive payments may have been deducted from the acquisition cost and have reduced the tax book value;
iv differences between MS in the definition of capital expenditures and expenses may lead to different tax book values upon entry;
v differences in the timing or the calculating of provisions may lead to different tax book values.

To the extent these differences have a negative impact on the asset factor of the sharing formula, the Member State concerned would be ‘punished’ twice: once by allowing postponement of recognition of profit under its national law, and a second time by receiving a lower share of the consolidated profit of the CCCTG group due to the lower asset factor. It cannot be excluded that a Member State will introduce rules to mitigate such effect for instance by prescribing a partial or full recapture of special deductions earlier claimed or revaluation up to market value upon opting into the system.

With respect to the lifetime of the asset, article 45 stipulates that upon entry, a lifetime will apply as if all assets are new (depreciation over 40 or 15 years) unless the taxpayer can demonstrate that the estimated remaining useful life of the asset is shorter. This means that for each asset (other than pool assets) the taxpayer may be confronted with a (substantially)
longer depreciation period unless he can demonstrate that the useful life is not longer than the useful life applied prior to opting for the common base. The proposal does not give any guidance as to how much evidence should be produced by the taxpayer. The Commission could have chosen for a different approach: the remaining useful life under the national tax system is continued when opting for the common base (joining the CCCTB group) unless the relevant PTA demonstrates that a different useful life should be applied. Such a system would better safeguard a smooth transition from the national tax system to the common base.

For pool assets, the tax book value under the national corporate tax law will be added to the depreciation base of the pool.

Articles 46 and 47 prevent that due to the transition from national tax law to common base, revenues/expenses/provisions/deductions are taxed (or deducted) twice. Whereas paragraph 1 of article 46 refers to revenues and expenses, paragraph 2 only refers to revenues. However, expenses may have been covered by article 47 (2).

Article 47 (1) stipulates that additions to provisions will only be deductible under the common base to the extent that they arise from activities or transactions carried out after the taxpayer has opted into the common base. However, the provisions of the common base (articles 25, 26 and 27) may lead to a different timing in the recognition of costs than the national corporate tax law of the opting taxpayer. Under the common base, a provision can be formed where at the end of a tax year a taxpayer has a legal obligation or a probable future legal obligation. Under the national corporate tax law of a Member State, this may be different. Differences might also exist in valuing such obligation. For instance, the discounting factor (for the common base, articles 25 (2)(b) and 26 refer to the yearly average of the Euribor) may differ substantially from the long-term interest rate applied under national corporate tax laws. In the case of long-term provisions such as pension rights and dismantlement provisions for nuclear plants, this may lead to substantial differences in the valuation of the provision. Furthermore, we may question whether and to what extent indexation for future price changes, for instance, for pensions built up for past services should be taken into account (when they occur or at the time the services were performed for the estimated value). The question of indexation should be seen in combination with the discounting factor used to determine the present value of the future obligation. The Directive does not offer much guidance in this respect.

Article 47 (2) should protect the taxpayer against an unbalanced outcome: to the extent no deduction was made prior to opting into the common base, 'expenses' shall be deductible. However, article 47 (2) does not stipulate when such expenses can be deducted.

Article 48 stipulates that losses incurred under national law before opting into the common base, will remain available for carry forward against the profit determined under the common base. However, since the loss itself is not a common base loss, the national tax loss carry forward rules remain applicable, the only difference being that taxable profits are now calculated based on the common base (or apportioned based on the sharing formula if the CCCTB group is formed), which may lead to a profit for the taxpayer concerned which is higher or lower than profit based on the national corporate tax base.

For opting out, the proposal contains similar provisions to secure a smooth transition from common base to national corporate tax base. The main provision is that the tax book value under the common base will form the start book value under the national base (article 49).

However, reference is made to articles 67 and 68 of the proposal which set out specific rules for valuation of assets upon leaving a CCCTB group. For assets belonging to a pool under the common base, such pool will be continued under national corporate tax law even if the national corporate tax law of the Member State concerned does not operate such pooling system. The background, most probably, is that: if such pooling has been applied, the tax book value of each separate asset will not be available.

The Commission has kept the transitional rules for entry into and exit from the system as simple as possible. Certainly in the case of a single entity, this makes sense. In most cases, more complex transitional rules would only lead to timing differences. However, in cases where the common base provides for an exemption (article 11, see also articles 73 and 75) and the national corporate tax law does not (or vice versa) this might lead to permanent differences. For instance, if income of a PE in a third country, which is exempt based on article 11(e) under the common base, was included in the taxpayer’s national corporate tax base, the
question may arise how to deal with foreign source losses previously deducted from worldwide income or foreign source income included in the taxpayer’s base for which no avoidance for double taxation was obtained. A similar question could arise with respect to a PE in a Member State. For these types of situation, Member States may want to introduce transitional rules in their national corporate tax law, in particular, if the transitional rules in Chapter VIII of the Directive do not lead to an acceptable outcome.

If a CCCTB group is formed, the switch from national corporate tax base to common base may, due to differences in the applicable tax rates in Member States, lead to permanent differences in the tax payable by the group depending on the apportionment of consolidated income to the various taxpayers of the group (and the Member States involved).

Paul Simonis

Chapter IX Consolidation

Article 54 Qualifying subsidiaries

1. Qualifying subsidiaries shall be all immediate and lower-tier subsidiaries in which the parent company holds the following rights:
   (a) a right to exercise more than 50% of the voting rights;
   (b) an ownership right amounting to more than 75% of the company’s capital or more than 75% of the rights giving entitlement to profit.

2. For the purpose of calculating the thresholds referred to in paragraph 1 in relation to companies other than immediate subsidiaries, the following rules shall be applied:
   (a) once the voting-right threshold is reached in respect of immediate and lower-tier subsidiaries, the parent company shall be deemed to hold 100% of such rights.
   (b) entitlement to profit and ownership of capital shall be calculated by multiplying the interests held in intermediate subsidiaries at each tier. Ownership rights amounting to 75% or less held directly or indirectly by the parent company, including rights in companies resident in a third country, shall also be taken into account in the calculation.

Article 55 Formation of group

1. A resident taxpayer shall form a group with:
   (a) all its permanent establishments located in other Member States;
   (b) all permanent establishments located in a Member State of its qualifying subsidiaries resident in a third country;
   (c) all its qualifying subsidiaries resident in one or more Member States;
   (d) other resident taxpayers which are qualifying subsidiaries of the same company which is resident in a third country and fulfils the conditions in Article 2(2)(a).

2. A non-resident taxpayer shall form a group in respect of all its permanent establishments located in Member States and all its qualifying subsidiaries resident in one or more Member States, including the permanent establishments of the latter located in Member States.

Article 56 Insolvency

A company in insolvency or liquidation may not become a member of a group. A taxpayer in respect of which a declaration of insolvency is made or which is liquidated shall leave the group immediately.

Article 57 Scope of consolidation

1. The tax bases of the members of a group shall be consolidated.

2. When the consolidated tax base is negative, the loss shall be carried forward and be set off against the next positive consolidated tax base. When the consolidated tax base is positive, it shall be shared in accordance with Articles 86 to 102.

Article 58 Timing

1. The thresholds of Article 54 must be met throughout the tax year.

2. Notwithstanding paragraph 1, a taxpayer shall become a member of a group on the date when
the thresholds of Article 54 are reached. The thresholds must be met for at least nine consecutive months, failing which a taxpayer shall be treated as if it had never having become a member of the group.

**Article 59 Elimination of intra-group transactions**

1. In calculating the consolidated tax base, profits and losses arising from transactions directly carried out between members of a group shall be ignored.
2. For the purpose of determining whether there is an intra-group transaction, both parties to the transaction must be group members at the time that the transaction is effected and the associated revenues and expenses fall to be recognised.
3. Groups shall apply a consistent and adequately documented method for recording intra-group transactions. Groups may change the method only for valid commercial reasons, at the beginning of a tax year.
4. The method for recording intra-group transactions shall enable all intra-group transfers and sales to be identified at the lower of cost and value for tax purposes.

**Article 60 Withholding and source taxation**

No withholding taxes or other source taxation shall be charged on transactions between members of a group.

**Comment**

The cross border consolidation offered to EU taxpayers that form part of a group is the most ambitious part of the proposal for a Council Directive. In Recital (6), this is phrased as follows: ‘Consolidation is an essential element of such a system, since the major tax obstacles faced by companies in the Union can be tackled only in that way. It eliminates transfer pricing formalities and intra-group double taxation. Moreover, losses incurred by the taxpayers are automatically offset against profits generated by other members of the same group.’

Provisions dealing with consolidation can be found throughout the Directive in Chapter IX (requirements and consequences of forming a group), Chapter X (specific provisions for entering and leaving the group), Chapter XI (business reorganisations within a group or between groups), and Chapter XVI (apportionment of the consolidated tax base). Other Chapters also contain specific provisions for a group, such as Chapter XII (article 75 which provides for an anti-abuse provision in case of dealings between the group and other entities after intra-group transactions have taken place) and Chapter XVIII (for instance, article 105 dealing with the term of a group, articles 109 and 110 (2) dealing with the tax year of a group, article 114 dealing with tax assessments, article 115 dealing with a central data base to which all competent authorities shall have access, article 116 designation of the principal taxpayer, article 119 dealing with a request for an opinion by the competent authority where two or more group members in different Member States are involved, and article 122 with respect to (coordinated) audits of group members). The various provisions also make clear how far-reaching the consequences of such consolidation will be, not only for the taxpayers but also for the competent authorities of the Member States concerned. It will take considerable time before it becomes clear what the exact consequences of such consolidation will be. The provisions in the proposal for a Directive are the bare minimum of what is required to start the process, but practice will show that reality is more diverse and complicated than anticipated. Guidance by way of more detailed rules from the Commission (the competent authorities) and rulings of the CJ on the impact of CCCTB rules may be needed in numerous respects. From that perspective, we can expect that will take decades rather than years before the tax treatment of groups under the CCCTB becomes clear in all respects. Having said this, we can also conclude that with this proposal for a Council Directive and all the efforts that have been put into this project since autumn 2004 when the CCCTB Working Group started, the Commission has made a big step forward.

With respect to articles 54-60 a few points are further elaborated.

If a taxpayer elects to apply the common base, it is obliged to form a CCCTB group with its
qualifying subsidiaries. Not only is grouping as such mandatory, it also includes all qualifying subsidiaries. In the Explanatory Memorandum, the Commission mentions four policy options which have been compared with the ‘no action’ or ‘status quo’ scenario (option 1). In the proposal, option four (optional CCCTB) has been chosen. Under this scenario, EU resident companies and/or EU situated PEs owned by companies outside the EU, would be entitled to apply the CCCTB, provided that they fulfil the eligibility requirements for forming a group and all eligible members of the same group opt to apply the common rules (‘all-in all-out’). Article 54 defines which subsidiaries are qualifying subsidiaries. The eligibility for group membership is determined based on a two-part test. Such test should ensure a high level of economic integration between the group members as indicated by a control and a high level of participation (see Recital (16)). In paragraphs 9 - 13 of Room Document 1 dated 30 August 2010, the Commission proposed a 3-part test whereby not only the >50% voting rights test should be met but also the >75% capital test and the >75% profit test. Based on the ownership test in the proposed Directive, it is clear that subsidiaries may have to be included in the group even though the bulk of the profit rights or the ownership of the capital is in the hands of third parties. It is sufficient that the taxpayer holds voting control and either >75% of the capital or >75% of the profit rights. For most subsidiaries of an international group, these tests will be met so that opting for the system will also mean that a group will be formed between that taxpayer and its immediate and lower tier EU resident subsidiaries. However, as with many other provisions in the proposal, practice will show that this provision will lead to numerous questions in less straightforward situations. For instance, in the case of third party shareholdings, different classes of shares with different voting rights, paid in capital and different entitlements to profits, specific voting arrangements between (ultimate) shareholders or included in loan documentation, usufruct arrangements and tracking stock, it may become difficult to determine whether or not a lower tier company is a qualifying subsidiary. If share transfers are made or arrangements are amended, it should be verified each time whether the ownership test is met. Based on article 54(1), the thresholds must be met three times throughout the tax year. A group may be entered or left during the year. Once the ownership test is met, a taxpayer shall become a member of a group. However, the thresholds must be met for at least nine consecutive months, otherwise a taxpayer shall be treated as if it had never become a member of the group. This raises the question whether a short-term decrease in the ownership rights, which is restored as soon as possible thereafter, should lead to degrouping followed by a new grouping once the decrease has been restored. The Directive makes no provision for this. In paragraphs 94 - 96 of Working Paper 57 (CCCTB: Possible elements of a technical outline, 26 July 2007), it was suggested to ensure that an insignificant variation in a holding of voting rights would not trigger degrouping, because this would help the stability of the group and avoid potential manipulation of the companies to be consolidated. However, also in that working paper, it was stated that a drop in voting rights below 50% would lead to immediate degrouping. A short-term decrease in ownership rights within the nine-month period will mean that the taxpayer will not become a group member before the decrease has been restored. As from that moment, the taxpayer can become a group member, provided that as from the moment the ownership is restored, the nine consecutive months test is met.

The Commission must have realized that, as a consequence of the multiple mathematical ownership tests, taxpayers do indeed have some room to manoeuvre to group or degroup a company. However, much will depend on how these tests are applied in practice.

With respect to voting rights, article 54 (2)(a) provides that once the voting right threshold is reached in respect of immediate and lower tier subsidiaries, the parent company shall be deemed to hold 100% of such right. This makes sense. If a parent company holds 51% of the voting rights of a subsidiary which in turn holds 51% of voting rights of a sub-subsidiary, the parent in general will have voting control over that sub-subsidiary. Whether and to what extent >50% of the voting rights really gives control also depends, of course, on the provisions in the companies articles of association. If qualified majorities are required for practically all decisions, 51% of the voting rights would only give negative control.
Questions may also arise if a taxpayer can form part of two groups. An example:

Assume that A meets the voting test for B, C and D, but does not meet the >75% capital test so has to rely on the >75% profit right test. The profit rights in the various companies are shown in the diagram. Furthermore, assume that C meets the voting test with respect to D. If C wants to opt for the system, C will most probably force D to opt as well. Management of D will have its own responsibility whether or not to opt into the system and to become a member of the group with C. If so preferred, C and D can agree on specific arrangements (for instance, with respect to sharing of benefits from the offset of losses within the group) at the time of opting into the system. However, if A opts for the system one year later, A can form a group with C (78% profit rights) but not with D (62% profit rights). The question is whether opting into the system by A automatically leads to a group between A and C and degrouping of D. Since C has already opted into the system (and cannot opt out), it seems that C will indeed become a member of the A group without having an option to step out. This would mean that C can decide once whether or not to opt for the system, but that thereafter, C no longer has control over whether or not it will be included in groups with (indirect) shareholders. If C becomes a member of the A group, the group between C and D will cease to exist.

Article 55 stipulates which entities form part of the group. This can be reflected as follows:

It is assumed that the ownership test of article 54 has been met by USCo 1 with respect to all subsidiaries/PEs. Based on article 55(2) USCo 1 will form a group with MS 1, PE MS 2, MS 3, PE MS 4, MS 5, MS 7 and PE MS 8, but not with PE MS 6, because PE MS 6 is, seen from USCo 1 as
taxpayer, covered neither by article 55(2) nor by article 55(1). However, if company MS 1 is the taxpayer, it seems that all MS entities except PE MS 8 are included in the group. PE MS 6 qualifies under article 55(1)(b) because USCo 2 is a qualifying subsidiary resident in a third country. MS 7 is included in the group under article 55(1)(d), assuming USCo 1 fulfils the conditions in article 2(2)(a). This approach could be followed if USCo 1 does not opt into the system. If USCo 1 opts into the system, it seems more logical to follow the first mentioned approach.

If we assume that the ownership test of article 54 is not met by USCo 1 with respect to MS 1, and that MS 1 meets the test with respect to MS 2 – MS 6, there will be 2 groups. Based on article 55(2) USCo 1 will, for its PE MS 8 and MS 7 form a group, whereas MS 1 will form a separate group with PE MS 2 (article 55(1)(a)), MS 3 (article 55(1)(c)), PE MS 4 (article 55(1)(b)), MS 5 (article 55(1)(d)), provided USCo 2 fulfils the conditions in article 2(2)(a), and PE MS 6 (article 55(1)(b)).

In the case of insolvency, article 56 stipulates that a company may not become a member of a group or should leave the group immediately. A company in insolvency or liquidation will have incurred substantial losses (although not necessarily tax deductible losses) and may later on, in case of debt waivers, be confronted with substantial increases in value, for instance, if a settlement is reached with creditors or a buy back of bonds is made at a discount. Upon leaving the group, losses (also to the extent that losses have not yet been offset within the group) will remain with the group. If after degrouping, such debt waivers would not lead to taxable gains under the common base (in principle, after degrouping the common base system will remain applicable to the insolvent company) this might lead to an unbalanced outcome. The gain would not be taxable whereas the losses have been deducted or remain available for carry forward within the remaining group. If such debt waiver would lead to taxable gains under the common base this might also lead to an unbalanced outcome. If such debt waivers would lead to taxable gains in the hands of the insolvent company, this would lead to immediate taxation because the insolvent company is not availed of loss carry forwards. The liquidator and the creditors will not be pleased if the company has not received a decent compensation for losses incurred in the past which were offset by or left with the group. It is not entirely clear what article 56 tries to achieve and whether each Member State will apply the provision in the same way. Perhaps the Commission was concerned that intra-group transfers in anticipation of insolvency might affect the proper functioning of judicial proceedings. The concern might be that the debtor/group would seek to obtain a more favourable legal position (forum shopping). The mere fact that based on CCCTB for tax purposes intra-group transfers are recorded for tax book value should be less of a concern because this tax rule does not relieve management from the duty to act with group companies on a commercially sound (at arm’s length) basis. It remains to be seen how this provision will be applied by the Member States concerned, because Council Regulation (Commission) No. 1346/2000 of 29 May 2000 on insolvency proceedings has not led to harmonisation of national insolvency (liquidation) proceedings as such. The Regulation recognizes that due to the widely differing substantive laws, it is not practical to introduce insolvency proceedings with universal scope.

Articles 57 and 59 set out the scope of the consolidation. The entire tax base of a group member is consolidated, even if third party shareholders hold an interest in such group member.

Furthermore, intra-group profit and losses arising from transactions are ignored. With respect to a group loss, article 57(2) stipulates that such loss is not attributed to the various entities of a group. Such loss remains a ‘group loss’ until it has been offset against group profits or the group as such is terminated. This secures that such loss remains available for carry forward to the consolidated profit, irrespective of whether the composition of the group has changed in the meantime (new entities have joined, or existing group members have left) or the sharing formula has otherwise changed. The potential impact of this provision for a taxpayer/Member State should not be underestimated. If a group with substantial carry forward losses takes over the shares of a profitable company X in another Member State, the consequence will be that this profitable company will not incur tax in the foreseeable future because the loss carry forwards of the group existing at the time taxpayer X joins the group
can be used to offset future profits of taxpayer X. It is irrelevant that, at the time the loss was incurred by the group, taxpayer X was not part of that group and losses have been incurred by other taxpayers in other Member States. It is not relevant whether taxpayer X has a genuine trade or business, or is a cash box company. This system may be seen as an invitation for structures to benefit from the loss carry forward available in a group. The Commission must have considered this because Member States have introduced specific rules in their national corporate tax law to counter trading in losses. Here again, the Commission has chosen for simplicity. The question is whether the general anti-abuse rule of article 80 (artificial transactions carried out for the sole purpose of avoiding taxation shall be ignored for the purpose of calculating the tax base) will sufficiently protect the interests of the Member State. The fact that losses incurred by the group remain group losses until they have been offset, might also negatively affect the possibility to carry forward losses incurred under the national corporate tax laws prior to opting for the system, insofar as these losses under national law can only be carried forward for a limited period of time. Such losses might cease to exist if the period has expired. If group losses have to be attributed to the various group members, and the losses earlier incurred under national corporate tax law are offset first, expiration of such pre-grouping loss might be avoided.

Within a grouping system, the proposal in the Directive not to attribute group losses to the individual group members makes sense. Once formed, such group will usually exist for a number of years and keeping losses at the level of the group until they have been utilized, fits into that concept and avoids many complexities. Taxpayers having concerns whether their pre-grouping losses under national corporate tax law can be utilized in time may consider carrying out transactions to achieve a taxable step up in basis immediately prior to becoming part of the group.

Paul Simonis

Chapter X Entering and leaving the group

Article 61 Fixed assets on entering the group
Where a taxpayer is the economic owner of non-depreciable or individually depreciable fixed assets on the date of its entry into a group and any of these assets are disposed of by a member of a group within five years of that date, an adjustment shall be made in the year of the disposal to the apportioned share of the group member that held the economic ownership over these assets on the date of entry. The proceeds of such disposal shall be added to that share and the costs relating to non-depreciable assets and the value for tax purposes of depreciable assets shall be deducted.

Such an adjustment shall also be made in respect of financial assets with the exception of shares in affiliated undertakings, participating interests and own shares.

If, as a result of a business reorganisation, the taxpayer no longer exists or no longer has a permanent establishment in the Member State in which it was resident on the date of its entry into the group, it shall be deemed to have a permanent establishment there for the purpose of applying the provisions of this Article.

Article 62 Long-term contracts on entering the group
Revenues and expenses which accrued according to Articles 24(2) and (3) before a taxpayer entered the group but had not yet been included in the calculation of tax under the applicable national corporate tax law shall be added to, or deducted from the apportioned share in accordance with the timing rules of national law.

Revenues which were taxed under the applicable national corporate tax law before a taxpayer entered the group in an amount higher than that which would have been charged under Article 24 (2) shall be deducted from the apportioned share.

Article 63 Provisions and Deductions on entering the group
Expenses covered by Articles 25, 26 and 27, which are incurred in relation to activities or transactions carried out before a taxpayer entered the group but for which no provision or deduction had been made under the applicable national corporate tax law shall be deductible only against the
apportioned share of the taxpayer, unless they are incurred more than five years after the taxpayer enters the group.

**Article 64 Losses on entering the group**
Unrelieved losses incurred by a taxpayer or a permanent establishment under the rules of this Directive or under national corporate tax law before entering a group may not be set off against the consolidated tax base. Such losses shall be carried forward and may be set off against the apportioned share in accordance respectively with Article 43 or with the national corporate tax law which would be applicable to the taxpayer in the absence of the system provided for by this Directive.

**Article 65 Termination of a group**
When a group terminates, the tax year shall be deemed to end. The consolidated tax base and any unrelieved losses of the group shall be allocated to each group member in accordance with Articles 86 to 102, on the basis of the apportionment factors applicable to the tax year of termination.

**Article 66 Losses after the group terminates**
Following termination of the group, losses shall be treated as follows:
(a) if the taxpayer remains in the system provided for by this Directive but outside a group, the losses shall be carried forward and be set off according to Article 43;
(b) if the taxpayer joins another group, the losses shall be carried forward and be set off against its apportioned share;
(c) if the taxpayer leaves the system, the losses shall be carried forward and be set off according to the national corporate tax law which becomes applicable, as if those losses had arisen while the taxpayer was subject to that law.

**Article 67 Fixed assets on leaving the group**
If non-depreciable or individually depreciable fixed assets, except for those which gave rise to a reduced exemption under Article 75, are disposed of within three years of the departure from the group of the taxpayer holding the economic ownership over these assets, the proceeds shall be added to the consolidated tax base of the group in the year of disposal and the costs relating to non-depreciable assets and the value for tax purposes of depreciable assets shall be deducted.

The same rule shall apply to financial assets, with the exception of shares in affiliated undertakings, participating interests and own shares.
To the extent to which the proceeds of disposal are added to the consolidated tax base of the group, they shall not otherwise be taxable.

**Article 68 Self-generated intangible assets**
Where a taxpayer which is the economic owner of one or more self-generated intangible assets leaves the group, an amount equal to the costs incurred in respect of those assets for research, development, marketing and advertising in the previous five years shall be added to the consolidated tax base of the remaining group members. The amount added shall not, however, exceed the value of the assets on the departure of the taxpayer from the group. Those costs shall be attributed to the leaving taxpayer and shall be treated in accordance with national corporate tax law which becomes applicable to the taxpayer or, if it remains in the system provided for by this Directive, the rules of this Directive.

**Article 69 Losses on leaving the group**
No losses shall be attributed to a group member leaving a group.

**Comment**
Chapter X sets out special provisions for entering and leaving the group. The main rule in the case of opting in/out for the common base is the rollover of the tax book value. This rule is also followed if the taxpayer becomes a member of a group, but some special provisions were considered necessary because when joining the group, formulary apportionment may lead to a
different allocation of profits to taxpayers and Member States. In particular, if a surplus value has been built up while a taxpayer was not a member of a group, gain recognition and sharing between Member States when the taxpayer is part of a group may result in an unbalanced outcome. The same applies for surplus values built up during the period a taxpayer formed part of a group, which are realized shortly after the taxpayer has left the group. In articles 61 - 69, transitional provisions have been proposed upon entering and leaving the group with respect to fixed assets, long-term contracts, provisions and deductions and self-generated intangible assets.

Article 61 secures that if a taxpayer disposes of a non-depreciable or individually depreciable fixed asset within five years after that taxpayer joined the group, the net proceeds of such disposition will not form part of the consolidated profit which is shared according to the sharing formula, but will be added to the share of that taxpayer. The same applies if prior to such disposition, such an asset has been transferred within the group. The entire gain (the proceeds -/- costs relating to non-depreciable assets and the value for tax purposes of depreciable assets) will be added to the apportioned share of that group member, irrespective of whether and to what extent such gain accrued during the period the group member formed part of that group. A similar adjustment is made in the case of certain financial assets (loans to undertakings with which the company is linked by virtue of participating interests, investments held as fixed assets and other loans). Fixed assets are defined in article 4(14) as all tangible assets acquired for value or created by the taxpayer and all intangible assets acquired for value where they are capable of being valued independently and are used in the business in the production, maintenance or securing of income for more than 12 months, except where the cost of their acquisition, construction or improvements are less than EUR 1,000. The provision does not apply to pool assets or intangible assets 'not acquired for value'. The question is when is an intangible 'acquired for value' and when is an intangible 'created by the taxpayer' For self-created intangibles the taxpayer may have also incurred substantial expenses. The borderline between a purchased intangible and a self-generated intangible may not always be clear. A similar question could arise if prior to opting into the system and becoming part of a CCCTB group, a taxpayer transfers its self-created intangibles (on a rollover basis) to a related entity. Does the intangible qualify as a purchased intangible for that related entity? The distinction made in article 61 between 'intangible assets acquired for value' and other intangible assets can be quite important because intangibles such as brands/trade names, patent rights, know how, customer base, goodwill etc. may represent a substantial surplus value. To the extent such intangibles are not covered by article 61, the income arising from such intangibles will, also in the case of a sale within five years, form part of the consolidated profit which will be shared according to the formula.

Article 61 furthermore contains a specific provision if assets have been transferred within a group due to which business reorganisation the transferor no longer exists (for instance, due to a merger as meant in article 2(a) or a division as meant in article 2(b) of the Merger Directive) or it no longer maintains a PE in the Member State in which it was a resident on the date of entry into the group. In that case, the transferor shall be deemed to have a PE in that Member State for the purpose of applying the provisions of article 61. Apparently, also in that case, the Commission considered it necessary to protect the tax receipts of the Member States concerned by way of such a presumptive provision. It remains to be seen how this will work out in the Member State concerned because in that Member State, the taxpayer will have been deregistered as taxpayer at the time of the business reorganisation. Profit will only be attributed to this notional PE if the assets are disposed of by a member of a group. The apportionment according to the sharing formula is then adjusted for such gain on disposed assets. Although the text of article 61 is not entirely clear in this respect, it seems that the term disposed of by a member of a group refers to a disposal by a group member to a non-group member. Furthermore, the text refers to an adjustment equal to proceeds -/- costs. This raises the question whether the apportioned profit should also be adjusted if proceeds have been generated, but the gain as such has not been realized due to rollover relief for replacement assets (article 38(1)).

Articles 62 (long-term contracts on entering the group), 63 (provisions and deductions on entering the group) and 64 (losses on entering the group) are more or less similar to articles
46, 47 and 48 for entering into the system. Reference is made to the comment on those articles. The purpose of articles 62 - 64 is to secure that these items, which concern the period prior to forming a group, only affect the apportioned share of the taxpayer concerned and not the shares of the other taxpayers that form part of the same group.

Articles 65 and 66 deal with ‘termination’ of the group. This term is not defined in the Directive. Termination of the group should be distinguished from a taxpayer leaving a group. Leaving the group does not terminate the group, provided at least two taxpayers are left behind which form a group based on the ownership test of article 54. If the PTP has become the only member of the group, it must be assumed that the group has been terminated.

The group will also be terminated when the PTP gives a notice of termination to the PTA as referred to in article 105. In general, the PTP will be parent of the group (although exceptions may exist, see article 4(6) and article 116). If the group as such remains in place but the PTP becomes insolvent or is liquidated (article 56) or ceases to exist, it is not clear from the text whether the group is terminated, and a new group is formed or whether this should be treated as a company leaving the group, so that the group can be continued (with the taxpayers for which the ownership test is met), albeit that a new PTP has to be designated. Reference is made to Chapter XI, which contains specific provisions for business reorganisations within a group and between two or more groups. Article 71 stipulates that when, as a result of a business reorganisation, one or more groups or two or more members of a group become part of another group, unrealized losses of the previously existing group or groups’ shall be allocated to each of the members of that previously existing group according to the sharing formula applicable in the tax year of the business reorganisation. This allocation of losses is also prescribed by article 65 in the case of a termination of a group. It is not clear why a sale of shares in one or more group companies to third parties would only lead to degrouping of these companies, whereas a ‘business reorganisation’ whereby two or more members of a group become part of another group as meant in article 71 would lead to termination of the group. The term ‘business reorganisation’ has not been defined. We might even wonder whether a management buy-out of two subsidiaries (a subsidiary together with its 100% daughter company) would lead to termination of the entire transferor group because the subsidiary and its daughter have applied for the common base (cannot opt out) and are obliged to form a group as from the day they leave the transferor group.

The Directive should preferably provide for a list of events leading to termination of the group and a description of the consequences for the companies concerned. At the time of termination, group tax assessments for the more recent years, tax audits etc. will not have been finalized. The question is whether, if shortly after termination the group falls apart, one or more companies are also liquidated or cease to exist, the proper finalisation is sufficiently guaranteed.

Termination of a group with unrelieved losses may have far-reaching consequences for the taxpayers concerned. The allocation of losses to the individual members based on the apportionment factors applicable in the year of termination may lead to an allocation of losses to entities (Member States) which have not contributed to these losses. Furthermore, such attributed losses can no longer be offset against profits of other group members, even if immediately after termination a new group is formed with almost the same taxpayers. In the latter case, the Directive could be improved by adopting a ‘cluster approach’, i.e. the unrelieved losses are not attributed to separate taxpayers but to clusters of taxpayers forming a new group immediately after the old group has been terminated. Such ‘cluster loss’ would be treated as an unrelieved loss of that new group.

Articles 67, 68 and 69 concern provisions for the event a taxpayer leaves a group. Although it could be argued that in the case of termination everybody leaves the group, these articles assume that the group as such is not terminated.

Article 67 provides that the net proceeds of a disposal by such taxpayer of non-depreciable or individually depreciable fixed assets within three years after degrouping are not treated as profits of that taxpayer but as profits of the group in the year of the disposal. Because the taxpayer concerned no longer forms part of that group, this profit will be apportioned to other taxpayers. If a group has existed for five years, or even shorter because degrouping may take place earlier if the ownership test is no longer met, we may wonder whether such fine-tuning
primarily to protect the interest of the Member State is justified. In practice, the application of this type of provision will lead to complications and a number of questions. For instance, does the term ‘dispose’ include tax free reorganisations under the EU Merger Directive, does the gain have to be recognized (is this the case if under CCCTB rules (article 38) a replacement reserve is formed?), do the words, ‘these years’, refer to book years of the CCCTB group, book years of the degrouped taxpayer, to calendar years, or to a period of 3 x 12 months after degrouping? How will this rule be enforced in practice if for whatever reason the degrouped taxpayer (its Member State) does not inform the group or the PTA of the remaining group that a disposal has taken place? And if the entities that form part of the group in the year of disposal are indeed assessed for such gain apportioned to them, it will trigger further questions. For instance, since the proceeds have been received by a taxpayer who does not form part of that group, how will the group members be reimbursed for the tax they have to pay on this apportioned gain? Will this affect the effective tax for the degrouped taxpayer and the remaining group members, if such effective tax is relevant at the level of their shareholders to determine the credit for underlying tax?

The same applies to article 68 which leads to an increase of the consolidated profit by adding to the tax base of the remaining group members the amount of R&D, marketing and advertising costs of the degrouped taxpayer in the previous five years (with a maximum of the market value of the assets at the time of degrouping). An example:

<table>
<thead>
<tr>
<th></th>
<th>With article 68</th>
<th>Without article 68</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regular profit total group</td>
<td>200</td>
<td>200</td>
</tr>
<tr>
<td>Share of departing taxpayer (15%)</td>
<td>30</td>
<td>30</td>
</tr>
<tr>
<td>Share of remaining group members</td>
<td>170</td>
<td></td>
</tr>
<tr>
<td>R&amp;D/M&amp;A-costs departing taxpayer 5 years</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>Profit apportioned to remaining group</td>
<td>220</td>
<td>170</td>
</tr>
<tr>
<td>Profit apportioned to departing taxpayer</td>
<td>-20</td>
<td>30</td>
</tr>
</tbody>
</table>

Although this is not entirely clear from the text, it seems that this adjustment has to be made in the first year after which the taxpayer has left the group. This may be relevant if more than one taxpayer leaves the group at the same time.

The costs attributed to the departing taxpayer shall be treated in accordance with the national corporate tax law (if the common base no longer applies) or with the Directive if the common base remains applicable to the departing taxpayer. Under the common base the –20 attributed to the departing taxpayer will most probably form a loss as meant in article 43(1), unless the general rule of article 69 (no losses shall be attributed to a group member leaving a group) would mean that the loss of 20 stays with the remaining group.

As mentioned before, the question should be raised of what level of detail and complexity is acceptable to protect the tax revenue apportioned to each Member State. The apportionment based on the sharing formula will undoubtedly impact the taxable basis of Member States that sign up for CCCTB.

With the specific anti-abuse provision in article 75, the Member States involved are to certain extent already protected against tax driven degrouping. In view of the global approach followed in the formula apportionment, fine-tuning to amend such apportionment should only be introduced in evident

Paul Simoni

**Chapter XI Business Reorganisation**

**Article 70 Business reorganisations within a group**

1. A business reorganisation within a group or the transfer of the legal seat of a taxpayer which is a member of a group shall not give rise to profits or losses for the purposes of determining the consolidated tax base. Article 59(3) shall apply.

2. Notwithstanding paragraph 1, where, as a result of a business reorganisation or a series of transactions between members of a group within a period of two years, substantially all the assets
of a taxpayer are transferred to another Member State and the asset factor is substantially changed, the following rules shall apply.

In the five years that follow the transfer, the transferred assets shall be attributed to the asset factor of the transferring taxpayer as long as a member of the group continues to be the economic owner of the assets. If the taxpayer no longer exists or no longer has a permanent establishment in the Member State from which the assets were transferred it shall be deemed to have a permanent establishment there for the purpose of applying the provisions of this Article.

Article 71 Treatment of losses where a business reorganisation takes place between two or more groups

1. Where, as a result of a business reorganisation, one or more groups, or two or more members of a group, become part of another group, any unrelieved losses of the previously existing group or groups shall be allocated to each of the members of the latter in accordance with Articles 86 to 102, on the basis of the factors applicable to the tax year in which the business reorganisation takes place, and shall be carried forward for future years.

2. Where two or more principal taxpayers merge within the meaning of Article 2(a)(i) and (ii) of Council Directive 2009/133/EC, any unrelieved loss of a group shall be allocated to its members in accordance with Articles 86 to 102, on the basis of the factors applicable to the tax year in which the merger takes place, and shall be carried forward for future years.

Comment

We may wonder why specific provisions with respect to business reorganisations have been included in this proposal for a Directive. Recital (17) of the proposal stipulates that rules on business reorganisations should be established in order to protect the taxing rights of Member States in an equitable manner, the remainder of the text of that paragraph deals with Chapter X (entering and leaving the group) and not with business reorganisations as such. The explanation will be that Room Document 2 of 2 September 2010 (‘Business Reorganisations in the CCCTB’), dealt not only with Business Reorganisations within a Group (paragraph C) and Business Reorganisations between Two or More CCCTB Groups (paragraph D), but also with entering rules (paragraph A) and leaving rules (paragraph B). In the proposal for a Directive, these paragraphs are dealt with in separate chapters. The term ‘business reorganisations’ is not defined. Chapter XI distinguishes between Business reorganisations within a group (article 70) and Business reorganisations between two or more groups (article 71).

Article 70 For intra-group reorganisations and the transfer of the legal seat of a group member, article 70(1) stipulates that such transfer shall not give rise to profits or losses for purposes of determining the consolidated tax base. This follows from the general principle set out in article 59(1) which reads: ‘In calculating the consolidated tax base, profits and losses arising from transactions directly carried out between members of a group shall be ignored.’ The justification for such treatment is clear and can also be found in paragraph 14 of Room Document 2: ‘Given that a consolidated group is treated as a unity, tax neutrality is justified by the absence of business profit in operation within a single framework of consolidation.’ The relevance of article 70, therefore, lies in the exception to this rule. Article 70(2) provides that the asset factor in the sharing formula be adjusted in case of specific transfers. Such adjustment will be made in the case of a business reorganisation or a series of transactions between members of a group within a period of two years as a result of which, substantially all the assets of a taxpayer are transferred to another Member State and the asset factor is substantially changed. In that case, during a period of five years following such transfer, the asset factor will be adjusted to compensate the Member State for the (potential) loss in revenue. We can question to what extent such complicating provisions should be included in the Directive to protect the taxing rights of a Member States where the main principle adopted with (the factors in the) formulary apportionment is a very global approach. Upon reading article 70(2), the conclusion may be that this exception will only apply in rare cases. However, this will also

1 OJ L 310, 25.11.2009, p. 34.
depend on how the various terms in article 70(2) should be interpreted. A few examples. The first question is which transfers are covered by article 70(2). Whereas article 70(1) refers to a business reorganisation or a transfer of the legal seat, article 70(2) only refers to a business reorganisation. Business reorganisation, although not defined in the proposal, seems to refer to specific transfers, so that not all transfers of assets may be covered by this term. However, article 70(2) also refers to ‘a series of transactions’ within two years. Only if ‘substantially all the assets’ are transferred, will the provision apply. Although ‘substantially all’ has not been defined either, we can consider >90% of the assets. Not only is the term ‘substantially all’ not clear, the Directive also does not stipulate how this should be measured (tax book value or market value at the time of the transfer?). Although the term ‘assets’ has not been defined, based on the text it should also include assets which are not included in the asset factor for the sharing formula and assets not recorded as such on the tax balance sheet. A tainted transfer will only lead to an adjustment of the asset factor in the sharing formula if the ‘asset factor is substantially changed’ by such tainted transfer. Again, it is unclear what ‘substantially’ means (30% or more?) and from whose perspective that should be seen (measured as the change in the asset base of the Member State of the transferor prior to and after the transfer or in relation to total asset factor for the group, or seen from the change in asset base of the recipient Member State of the transferred assets?) Furthermore, the text does not stipulate when the test has to be applied (the moment that the transfer has been completed, or the first balance sheet date after the transfer has been completed) and whether it is a one-time test or whether it has to be applied each year during the five-year period. This may be relevant, for instance, if shortly after the transfer, the transferor replaces the transferred assets by similar assets. If the asset factor has to be adjusted, the question is how such adjustment should be made. The text reads that the ‘transferred assets’ shall be attributed to the asset factor of the transferor. Probably the adjustment is not made as one fixed amount (tax book value of the transferred assets at the time of the transfer) for the entire period of five years. During the five-year period, the tax book value of the transferred assets may change due to depreciation. Some assets may be sold or replaced within the five-year period. Should we take the amount adjusted for each year? Article 70(2) refers to ‘transferred assets’ and not to ‘transferred assets which were included in the asset factor’. However, it seems unlikely that the Commission has meant to adjust the asset factor in the sharing formula with assets which were not included in the asset factor in the first place.

Furthermore, article 70(2) stipulates that if the transferor-taxpayer no longer exists or no longer has a PE in the Member State from which the assets were transferred, it shall be deemed to have a PE there for the purpose of article 70. In paragraph 17 of Room Document 2 dated 2 September 2010, the need for such deemed PE is also explained by protecting the rights of the transferor-taxpayer. If such taxpayer would have pre-consolidation losses at the time of the transfer and after the transfer no profits were allocated based on the sharing formula (which does not depend only on ‘assets’ but on other factors as well), such losses could not be effectively used. This concern could be solved in other ways, for instance, by allowing the taxpayer/group upon request a step up in basis to the lower of the hidden reserves in the transferred business and the amount of the pre-consolidation losses available at the moment of the transfer. However, such step up in basis would not solve the concerns for the Member State of the transferor to protect its tax revenues. From paragraph 19 Room Document 2, it is clear what the Commission tries to achieve with article 70. The possibility to move assets free of tax within the group could encourage tax planning. Article 70 is meant to counteract such planning. Article 70(2), therefore, is an anti-abuse provision to protect the interest of the Member State of which the transferor is a taxpayer. If such provision has to be included in the Directive at all, it should be considered to limit the application to abuse cases only. The minimum requirement for such provision is that it is drafted in such a way that it is clear when and how it should be applied. The current wording leaves too many questions open. However, this is a remark that can be made with respect to many articles of the proposal for a Directive.

**Article 71** provides a specific rule for any unrelieved group loss of a group involved in a business reorganisation. Article 71(1) refers to a business reorganisation as a result of which two or more members of a group become part of another group. As noted in the commentary...
to Chapter X, article 71, it is not entirely clear in which case the test ‘becomes part of another group’ will be met. Is it sufficient that two or more members together form a new group, or should the acquiring vehicle already form part of another group at the time of the reorganisation? Article 71(1) covers more transactions than article 71(2). Article 71(1) applies to a business reorganisation as a result of which one or more groups, or two or more members of a group become part of another group. In the case of relatively simple transactions between two CCCTB groups, this provision will apply. However, if a CCCTB group takes over an entire multinational which has not yet opted into the system, article 71(1) does not apply.

The text of article 71(2) seems to cover only the situation in which a PTP is merged into another PTP or in which two PTPs are merged into a newly formed company. The text does not cover the merger of a PTP into a company that belongs to another group but that is not the PTP of that group. We may wonder whether it was the intention to make a distinction between those transactions. Paragraph 23 of Room Document 2 refers to ‘a reorganisation involving 2 or more CCCTB groups’ and in paragraphs 26 and 27, a distinction is made between ‘acquisition’ and ‘merger by absorption or creation of a new company’. These paragraphs have not been followed in the proposal for a Directive, and the scope of the provisions has changed. From the perspective of the PTP that ceases to exist, it does not make much difference whether the acquiring vehicle is the PTP of another group or a member of that group. A difference between a PTP (usually the parent company of the EU group) and a group member (which is not the parent of the EU group), could be that the latter, due to the issuance of shares in its capital to the shareholders of the PTP that ceases to exist, may no longer form part of the other group. However, it is unclear why a distinction should be made between a PTP as acquiring vehicle and a non-PTP member of a group as an acquiring vehicle. The acquiring group member will not in all cases cease to be a member of the other group, and even if after the merger the ownership test would no longer be met, the acquiring company itself may qualify as PTP for the subsidiaries it held prior to the merger.

If a transaction falls under article 70(1)(2), the unrelieved losses ‘of a group’ shall be allocated to each of the group members in accordance with the sharing formula applicable to the tax year in which the transfer takes place. These apportioned losses will qualify as pre-consolidation (common base) losses and can only be offset against the profit apportioned to the particular member in future years. In paragraph 26 of Room Document 2, it is stipulated that in case of an acquisition only the unrelieved group losses of the acquired CCCTB group have to be allocated to the group members. Paragraph 28 of Room Document 2 made a difference between a merger by absorption (only pre-merger group losses of the absorbed group had to be allocated to the group members) and merger by creation of a new company (pre-merger group losses of both groups had to be allocated to the group members). In the proposal for a Directive, no such distinction is made between a merger by absorption and a merger by creation of a new company. Article 71(2) refers to any unrelieved loss of ‘a group’, and that seems to cover any unrelieved losses of the groups of the merging PTPs. Article 71(2) may apply to both groups irrespective of the type of merger. The PTP of the acquiring group will normally remain the same but the composition of the group may have changed substantially due to the business reorganisation. From that perspective, there is no reason to treat the transferor group differently from the acquiring group.

Although we can understand that unrestricted carry forward of unrelieved group losses to profits of another group which, until the merger/business reorganisation, never formed part of that loss incurring group may lead to unacceptable results, the solution proposed (loss allocation as if the loss incurring group has been terminated) may lead to overkill. The group that incurred the loss will be continued and there is no reason to bring that group into a position that is worse than before the merger/business reorganisation. The aim of the Merger Directive is to facilitate business-driven mergers, divisions and asset transfers by removing tax obstacles. The CCCTB Directive should not introduce new obstacles. The automatic apportionment of losses to group members may form such a tax obstacle for a group with unrelieved group losses.

In view of the potential consequences for these groups, it should be considered to fine-tune this provision. For instance, the allocation of group losses could be limited to the members to specific abuse cases, or upon request, the previous CCCTB group could be allowed to step up
the value of its business to the lower of the amount of group losses available and the hidden reserves existing at the time of the transfer of the group. Unlike paragraph 30 of Room Document 2, which prescribes that the business reorganisations between two or more 'CCCTB groups’ should follow the entering and leaving rules (i.e. should be carried out on a tax neutral basis), the proposal for the Directive does not prescribe such tax neutrality. This could mean that if such business reorganisation is not carried out on a rollover basis but as a taxable transaction, a step up in basis might be possible. However, in the case of a taxable transfer, the step up in basis will be limited to the assets of the group entity (transferor) that are actually transferred in the merger.

A cluster approach could also be followed, whereby the losses would remain available for carry forward to the combined apportioned shares of the entities of the previous group that become part of the new group.

For business reorganisations between two or more CCCTB groups, Room Document 2 also contains specific rules for hidden reserves in fixed assets which are sold within three years after the business reorganisation (paragraph 31), and R&D, marketing and advertising costs of self-generated intangible assets (paragraph 32). These rules are comparable with the rules in the proposal for a Directive dealing with the situation whereby a company leaves the group (see articles 67 and 68 of the Directive). Such specific rules for fixed assets and self-generated intangible assets are not included in Chapter XI.

Paul Simonis

Chapter XII Dealings between the group and other entities

Article 72 Exemption with progression
Without prejudice to Article 75, revenue which is exempt from taxation under Article 11(c), (d) or (e) may be taken into account in determining the tax rate applicable to a taxpayer.

Article 73 Switch-over clause
Article 11(c), (d) or (e) shall not apply where the entity which made the profit distributions, the entity’s shares in which are disposed of or the permanent establishment were subject, in the entity’s country of residence or the country in which the permanent establishment is situated, to one of the following:
(a) a tax on profits, under the general regime in that third country, at a statutory corporate tax rate lower than 40% of the average statutory corporate tax rate applicable in the Member States;
(b) a special regime in that third country that allows for a substantially lower level of taxation than the general regime.

The average statutory corporate tax rate applicable in the Member States shall be published by the Commission annually. It shall be calculated as an arithmetic average. For the purpose of this Article and Articles 81 and 82, amendments to the rate shall first apply to taxpayers in their tax year starting after the amendment.

Article 74 Computation of income of a foreign permanent establishment
Where Article 73 applies to the income of a permanent establishment in a third country, its revenues, expenses and other deductible items shall be determined according to the rules of the system provided for by this Directive.

Article 75 Disallowance of exempt share disposals
Where, as a result of a disposal of shares, a taxpayer leaves the group and that taxpayer has within the current or previous tax years acquired in an intra-group transaction one or more fixed assets other than assets depreciated in a pool, an amount corresponding to those assets shall be excluded from the exemption unless it is demonstrated that the intra-group transactions were carried out for valid commercial reasons.

The amount excluded from exemption shall be the market value of the asset or assets when transferred less the value for tax purposes of the assets or the costs referred to in Article 20 relating to fixed assets not subject to depreciation.

When the beneficial owner of the shares disposed of is a non-resident taxpayer or a nontaxpayer,
the market value of the asset or assets when transferred less the value for tax purposes shall be deemed to have been received by the taxpayer that held the assets prior to the intra-group transaction referred to in the first paragraph.

**Article 76 Interest and royalties and any other income taxed at source**

1. Where a taxpayer derives income which has been taxed in another Member State or in a third country, other than income which is exempt under Article 11(c), (d) or (e), a deduction from the tax liability of that taxpayer shall be allowed.

2. The deduction shall be shared among the members of a group according to the formula applicable in that tax year pursuant to Articles 86 to 102.

3. The deduction shall be calculated separately for each Member State or third country as well as for each type of income. It shall not exceed the amount resulting from subjecting the income attributed to a taxpayer or to a permanent establishment to the corporate tax rate of the Member State of the taxpayer’s residence or where the permanent establishment is situated.

4. In calculating the deduction, the amount of the income shall be decreased by related deductible expenses, which shall be deemed to be 2% thereof unless the taxpayer proves otherwise.

5. The deduction for the tax liability in a third country may not exceed the final corporate tax liability of a taxpayer, unless an agreement concluded between the Member State of its residence and a third country states otherwise.

**Article 77 Withholding tax**

Interest and royalties paid by a taxpayer to a recipient outside the group may be subject to a withholding tax in the Member State of the taxpayer according to the applicable rules of national law and any applicable double tax convention. The withholding tax shall be shared among the Member States according to the formula applicable in the tax year in which the tax is charged pursuant to Articles 86 to 102.

**Comment**

**Exemption with progression**

Article 72 provides that exempt income under article 11 (c) (received profit distributions), 11 (d) (proceeds from a disposal of shares), and 11 (e) (income from a permanent establishment in a third country) may be taken into account in calculating the tax rate applicable to the taxpayer, which is, in particular, relevant in the case of progressive tax rates. Article 72 clearly sets out that such exempt income ‘may’ be taken into account in calculating the tax rate. Member States are thus free, but not obliged, to do so. This is fully in line with Recital (5) of the Directive that determination of tax rates is at the discretion of the Member States only and that the Directive is not to affect such discretion.

**Switch-over – general**

Article 73 provides for a switch-over from an (income) exemption of received profit distributions (article 11 (c)), proceeds from a disposal of shares (article 11 (d)), and income from a permanent establishment in a third country (article 11 (e)) to a tax credit calculated according to the rules of article 76 in case of low taxation of the entity or the permanent establishment in the third country under a general or special tax regime, notwithstanding the activities performed by the low taxed entity or permanent establishment.

**Residence of entity and location of permanent establishment**

The switch-over applies if the entity making the profit distribution, or the shares of which are sold in its country of residence, or the permanent establishment in the country where it is situated, is subject to low taxation. It seems consistent to determine the residence of the entity for tax purposes of article 73 according to the rules of article 6, and thus to determine whether a dual resident entity is low taxed according to the tax regime of the third country where it has its place of effective management. However, in the absence of a reference in article 73 to article 6 and vice versa, the text of the Directive does not provide any basis for such interpretation. This should be clarified in the Directive by including a reference to article 6 in article 73.
Article 73 further refers to the permanent establishment being subject to low taxation in the third country where it is situated. As a permanent establishment is not subject to tax, article 73 seems to be interpreted such that the taxpayer is subject to low taxation in the third country on the profits attributable to its permanent establishment in the third country.

**General regime**

The switch-over rule applies if the entity or the permanent establishment is subject to a tax on profits under a general regime in a third country with a statutory tax rate lower than 40% of the arithmetic average of the corporate tax rates applicable in the Member States (article 73 (a)), as published annually by the Commission. Amendments to tax rates first apply in tax years after the amendment, for purpose of the switch-over rule of article 73, and for article 81 (disallowance of interest deductions) and article 82 (CFC). According to the text of article 73, clearly only the statutory tax rate in the third country is relevant, and not the effective tax rate. Consequently, objective tax exemptions or tax holidays in the general tax regime or State subsidies do not constitute low taxation. On the other hand, taxes other than profit taxes, such as (withholding) taxes on turnover are not taken into account either. Similarly, taxation in third countries other than the third country of residence is not considered. If, for example, an entity resident in third country A has a permanent establishment in third country B, the tax regime in third country B is not relevant in establishing whether the entity is subject to low taxation according to article 73; only the taxation in third country A is considered. Considering the statutory tax rate in the third country of residence only is simple and workable. It is, however, clear that it will result in unbalanced outcomes, which do not seem in line with the purpose of the switch-over rule, i.e. to 'limit tax exemption to situations in situations in which a certain minimum level of taxation was incurred' (Room Document[003]/8), and to provide for a tax ‘credit where exemption is not justified because of low local taxation’ (Working Paper |057/127).

**Special regime**

The switch-over rule also applies if the entity or the permanent establishment is subject to a special regime in the third country that allows for a substantially lower level of taxation than the general regime (article 73 (b)). The Directive does not define what regimes are considered special for purposes of articles 73, 81 and 82. Consider here, however, tonnage regimes and special regimes for investment funds. It is noted that the special regime must result in a substantially lower taxation than the general regime, whatever may be considered ‘substantial’. A comparison is thus to be made of the special tax regime with the general tax regime. It is, however, irrelevant whether the effective or statutory tax rate under the special regime is higher or lower than 40% of the average of the corporate tax rates in the Member States. If, for example, the statutory tax rate under the general tax regime in the third country is 30%, but the (effective) tax rate under the special tax regime is 15%, the special tax regime is likely considered to result in a substantially lower level of taxation than the general tax regime for purposes of article 73. The special regime, however, results in a higher level of taxation than 40% of the average of the corporate tax rates in the Member States, which is currently more around 10%. The intention is again to keep it simple and workable, but the balance with the objective of the switch-over rule seems to be lost.

**Hybrid entities in third countries**

An entity that is transparent for purposes of profit taxes in the country where it is located, is not subject to a tax on profits as referred to in article 73. Such entity may, however, still be considered non-transparent under the rules of article 85. Profit distributions by such hybrid entities are, consequently, per definition not exempt as result of the switch-over rule, even if the partners are subject to sufficient taxation on their share in the entity’s profits. Article 73 should be amended in this respect, such that the (aggregate) taxation at the level of the partners in the hybrid entity is taken into account.
Real economic activities
The switch-over rule of article 73 applies notwithstanding the activities performed by the low taxed entity or permanent establishment. This means that the switch-over rule also applies if the low taxed entity or permanent establishment performs real economic activities (or in the absence of a wholly artificial arrangement). In particular in view of the co-existence of controlled foreign entity rules (articles 82 and 83) and the fact that article 73 may also apply in relation to an entity resident in a Member State, it is unclear why no exception is made for entities engaged in, for example, actively conducting a trade or business. Hopefully, such exception will still be included in the Directive.

Computation of income of a foreign permanent establishment
Article 74 provides, in short, that income of a foreign permanent establishment is determined according to the rules of the Directive in the case of switch-over under article 73. The purpose of this article seems to be clarification only, as article 73 limits the application of article 11, heading and (e), but article 10 (in conjunction with the definition of revenues etc. under article 4) already includes revenues etc. realised abroad.

Tax treaties with third countries
Initially, it was intended that the switch-over rule would not apply if a tax treaty of the Member State of the taxpayer concluded with the third country provides for exemption (whereby it was unclear how to deal with tax treaties that provide for a tax exemption instead of an income exemption, such as article 11) and not an anti-abuse rule comparable to the switch-over rule of article 73 (compare Room Document(003)/9). Article 73, however, does not provide any rules on the precedence of tax treaties over the switch-over rule of article 73. Article 73 needs to be amended on this point. Note that in Room Document(003)/3, the view is taken that, on the basis of the principle of supremacy of EU law, only tax treaties pre-dating the CCCTB take precedence over the CCCTB rules. This is, however, doubtful, as also later tax treaties with third countries provide obligations of the respective Member States, which are to be observed in relation to the third countries.

Disallowance of exempt share disposals – general
Article 75 provides for disallowance of the (income) exemption for share disposals if the taxpayer leaves the group and previously acquired non-pool assets within the group, unless the intra-group transaction was carried out for valid commercial reasons.

Current or previous tax years
The disallowance of the exemption for share disposals is triggered if non-pool assets are transferred within the group to the leaving taxpayer in ‘the current or previous tax years’. It is not clear how the phrase ‘the current or previous tax years’ in the English text of article 75 is to be interpreted and thus, what the precise scope of article 75 is. The phrase ‘the current or previous tax years’ may refer either to the year of sale and all previous years, or to the year of sale and only one previous year. The translation of this phrase in Spanish: ‘durante el ejercicio fiscal en curso o en ejercicios anteriores’, French: ‘pendant l’exercice fiscal en cours ou les exercices precedents' and Dutch: ‘in het lopende of in voorgaande belastingjaren’, support the interpretation that transactions in the year of sale and all previous years are to be considered. However, the German text: ‘im laufenden oder vorangegenden Steuerjahr’, supports the interpretation that transactions in the year of sale and only one previous year are relevant. The German text in this respect is also in line with Working Paper\057/109 and Room Document \003/10, both of which referred to one previous year only. Article 75 would be rather unpractical and result in major overkill if transactions of all previous years are to be considered and the burden of proof thereof would be upon the taxpayer. Consequently, from a conceptual point of view, it makes sense to limit the number of previous years relevant for purposes of article 75 (whereby considering transactions in one previous year only may be considered too generous) or, alternatively, to shift the burden of proof to the PTA. Clearly, the text of article 75 is to be clarified and the wording to be translated consistently into other languages.
Relevant transactions
The disallowance of the exemption is triggered only if non-pool assets are previously transferred within the group to the taxpayer. Non-pool assets previously transferred within the group by the taxpayer, or pool assets and liabilities transferred within the group by or to the taxpayer are not considered. Pursuant to the text of article 75, it is irrelevant whether the taxpayer had already disposed of the non-pool asset it acquired previously within the group. The exemption for the share disposal should not be disallowed in such cases. Article 75 needs to be clarified on this point.

Amount of disallowed exemption
The amount of the disallowed exemption equals the difference between the market value and tax book value at the time of the transfer of the non-pool asset. The market value at the time of the taxpayer leaving the group is not considered, this in contrast to, for example, the equivalent rules in the Netherlands. It is noted that article 75 does not provide for a step up in basis at the level of the leaving taxpayer of the respective non-pool asset to the extent the exemption of the share disposal was disallowed. This clearly results in overkill and the Directive should be amended on this point, for example, in language similar to that in the last sentence of article 67.

Alternative sanction
Instead of the disallowance of the exemption, the difference between the market value and the tax book value of the respective asset at the time of the transfer is taxed at the level of the group (the difference between market value and tax book value is deemed received by the taxpayer that previously held the asset prior to the transaction within the group) if the beneficial owner of the shares disposed of is a non-resident taxpayer or a non-taxpayer. The reasoning for this alternative sanction is that in such cases, the proceeds from share disposal are generally not included in the tax base of article 10.

Tax credit – general
Article 76 provides for an ordinary tax credit, which is shared according to the sharing formula.

Qualifying income
The tax credit of article 76 is available with respect to income derived by the taxpayer which has been taxed in another Member State or in a third country, and which income is not exempt under article 11 (c) (received profit distributions), (d) (proceeds from a disposal of shares), and (e) (income of a permanent establishment in a third country). This generally includes interest and royalties, but also income from real estate abroad (unless a tax treaty with a third country provides otherwise) and income that is not exempt as a result of the switch-over rule of article 73.

Form of credit
The tax credit provided for in article 76 is calculated per type of income and per country (third countries and Member States). The tax credit is limited to the Member State’s tax on the income reduced by related deductible expenses. The related deductible expenses are deemed to be 2% of the income, unless the taxpayer proves these expenses to be lower. In Room Document\003/14, the deduction of 2% deemed expenses is considered a ‘pragmatic or appropriate way’.

Tax treaties with third countries
Tax treaties with third countries providing for more generous relief, have precedence over the tax credit rules of article 76. According to Room Document\003/12, this would only concern tax treaties pre-dating the Directive. This is, however, doubtful, as also later tax treaties with third countries provide obligations of the respective Member State, which are to be observed in relation to the third countries.
No carry forward

Article 76 does not provide for the carry forward of third country tax if this exceeds the tax due in the respective Member State, unless, however, tax treaties concluded with the Member State of residence and the third country provides otherwise. Working Paper 057/137 and Room Document 003/12 indicate that only tax treaties pre-dating the Directive would have precedence over the tax credit rules of article 76. However, the exception in article 76 (5), that tax treaties with third countries have precedence over the tax credit rules of article 76, is not limited to tax treaties pre-dating the Directive.

Sharing

The tax credit is shared among the members of a group according to the sharing formula. The background is that as the income received is shared, the burden of the tax credit is also to be shared. The tax credit is shared according to the sharing formula in the year in which the tax credit is granted. This is the year in which the (withholding) tax was charged, which in general, is the year in which the respective income was paid. The intended balance to share the income received and the tax credit, therefore, is not always fully realised, as the income may partly accrue in another year than the year in which the (withholding) tax is paid. If, for example, a loan agreement provides that interest of year 1 is due on the first business day of year 2 (following business day convention), the interest in year 1 will be part of the tax base in year 1 (accrual basis), but the (withholding) tax will be credited in year 2 (cash basis). The tax credit will thus be shared according to the sharing formula of year 2, which is generally different to the formula of year 1. Although, the burden of the tax credit is thus not always shared according to the same formula as the income is shared, the practical approach of article 76 (2) is understandable.

Withholding tax – general

Article 77 provides for the option for Member States to impose withholding tax on interest and royalties paid to recipients outside the group. The withholding tax charged is shared according to the sharing formula.

Withholding tax

According to article 77, interest and royalties paid by a taxpayer to a recipient outside the group, may be (but do not have to be) subject to a withholding tax in the Member State of the taxpayer. The withholding tax is charged according to the domestic tax system of the respective Member State subject to tax treaties. Article 77 only allows Member States to levy withholding taxes, which means that non-resident corporate taxation of interest and royalties, such as the German non-resident corporate taxation of interest on mortgage secured loans, is apparently not allowed.

Interest and royalties

The term ‘interest’ is defined in article 81(2). Although, there are no cross-references in articles 77 and 81(2), it would seem consistent to apply the definition of the term ‘interest’ of article 81(2) in the context of article 77. The term ‘royalties’ is not defined in the Directive, which seems to imply that the term ‘royalties’ is to be defined according to the definition in the domestic tax law of the Member State imposing the withholding tax.

Sharing

The withholding tax is shared among the Member States according to the sharing formula. The background is that as the deduction of the interest and royalties is shared, the benefit of the withholding tax thereon is to be shared as well. The withholding tax is shared according to the sharing formula in the year in which the withholding tax is charged, which is not necessarily the same year as the year in which the interest and royalties are deducted. Similarly, as with the sharing of the tax credit of article 76, the balance to share the deduction of interest and royalties, and the withholding tax is not always (fully) realised. It is, however, practical to share the withholding tax in the year it is charged.

Matthijs Vogel
Chapter XIII Transactions between associated enterprises

Article 78 Associated enterprises

1. If a taxpayer participates directly or indirectly in the management, control or capital of a non-taxpayer, or a taxpayer which is not in the same group, the two enterprises shall be regarded as associated enterprises.

If the same persons participate, directly or indirectly, in the management, control or capital of a taxpayer and a non-taxpayer, or of taxpayers not in the same group, all the companies concerned shall be regarded as associated enterprises.

A taxpayer shall be regarded as an associated enterprise to its permanent establishment in a third country. A non-resident taxpayer shall be regarded as an associated enterprise to its permanent establishment in a Member State.

2. For the purposes of paragraph 1, the following rules shall apply:
   (a) participation in control shall mean a holding exceeding 20% of the voting rights;
   (b) participation in the capital shall mean a right of ownership exceeding 20% of the capital;
   (c) participation in management shall mean being in a position to exercise a significant influence in the management of the associated enterprise.
   (d) an individual, his spouse and his lineal ascendants or descendants shall be treated as a single person.

In indirect participations, the fulfilment of the requirements in points (a) and (b) shall be determined by multiplying the rates of holding through the successive tiers. A taxpayer holding more than 50% of the voting rights shall be deemed to hold 100%.

Article 79 Adjustment of pricing in relations between associated enterprises

Where conditions are made or imposed in relations between associated enterprises which differ from those that would be made between independent enterprises, then any income which would, but for those conditions, have accrued to the taxpayer, but, by reason of those conditions, has not so accrued, shall be included in the income of that taxpayer and taxed accordingly.

Comment

Chapter XIII deals with transactions between associated enterprises. Article 78 sets out when enterprises are considered associated. Article 79 provides for adjustment of pricing in relations between associated enterprises.

Associated enterprises

According to article 78 (1), enterprises are considered associated in the case of direct or indirect participation in management, control or capital by a group taxpayer in non-taxpayer/non-group taxpayer, or by the same person in both the non-taxpayer/non-group taxpayer and in the group taxpayer. Furthermore, a taxpayer is considered an associated enterprise with its permanent establishment in a third country, and a non-resident taxpayer is considered an associated enterprise with its permanent establishment in a Member State.

Control

Control means a holding exceeding 20% of the voting rights (article 78 (2) (a)). In the case of indirect participations, the voting rights are multiplied, whereby a holding of more than 50% voting rights is deemed 100%. In most cases, voting rights are easy to establish by reference to the articles of association. There are, however, some uncertainties in less straightforward situations, such as different classes of shares with different voting rights (for example, priority shares to appoint the board of directors), specific voting arrangements between (ultimate) shareholders and voting rights provided for in other documents (for example, loan agreements).

Capital and management

Capital means a right of ownership exceeding 20% of the capital (article 78 (2) (b)). In the case of indirect participations, the capital requirement is tested by multiplication of the rates of
holding. Again, in most cases, the amount of capital is easily established on the basis of the articles of association, but in less straightforward situations (for example, different classes of shares), difficulties may arise. Participation in management means to be in a position to exercise a significant influence (article 78 (2) (c)), which means that, for example, directors may establish association within the meaning of article 78.

**Profit participation**

Note that in contrast to article 54, which sets out the relevant tests for consolidation purposes, article 78 does not require any profit participation. This means, for example, that profit participating loans or profit certificates (non-capital) do not establish association within the meaning of article 78, even if these instruments give right to the majority of the profits of the enterprise. In addition, in usufruct arrangements, the bare owner may be considered associated, whilst the holder of the usufruct is entitled to the profits. Similarly, (cumulative) preference shares are not treated differently to ordinary shares, even though the fixed remuneration on (cumulative) preference shares may be more comparable to that of loans.

**Individuals and family**

Note that according to article 78 (2) (d), an individual, his spouse and his lineal ascendants and descendants are treated as one single person. Article 78 does not provide for an exception for bad family relationships; irrespective of whether relationships are good or bad, the respective family members are considered to be one person.

**Adjustment pricing**

Whereas article 78 sets out the rules to establish what enterprises are associated, article 79 provides that non-arm’s length conditions between associated enterprises be adjusted to arm’s length conditions: the income is included and taxed accordingly. As article 79 only mentions ‘income’ and not also ‘expenses’, at first instance, it seems to provide for adjustment only if the taxpayer’s income is too low and not also if the expenses are too low. However, as double taxation is clearly not intended, the word ‘income’ in article 79 is to be interpreted to include both positive and negative income. It is preferable, however, that the Directive be clarified on this point by explicitly mentioning expenses in article 79.

Matthijs Vogel

**Chapter XIV Anti-Abuse rules**

**Article 80 General anti-abuse rule**

Artificial transactions carried out for the sole purpose of avoiding taxation shall be ignored for the purposes of calculating the tax base.

The first paragraph shall not apply to genuine commercial activities where the taxpayer is able to choose between two or more possible transactions which have the same commercial result but which produce different taxable amounts.

**Article 81 Disallowance of interest deductions**

1. Interest paid to an associated enterprise resident in a third country shall not be deductible where there is no agreement on the exchange of information comparable to the exchange of information on request provided for in Directive 2011/16/EU and where one of the following conditions is met:

(a) a tax on profits is provided for, under the general regime in the third country, at a statutory corporate tax rate lower than 40% of the average statutory corporate tax rate applicable in the Member States;

(b) the associated enterprise is subject to a special regime in that third country which allows for a substantially lower level of taxation than that of the general regime.

2. The term ‘interest’ means income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor’s profits, and in particular, income from securities and income from bonds or debentures, including premiums and prizes.
attaching to such securities, bonds or debentures. Penalty charges for late payment shall not be regarded as interest.

3. Notwithstanding paragraph 1, interest paid to an entity resident in a third country with which there is no agreement on the exchange of information comparable to the exchange of information on request provided for in Directive 2011/16/EU shall be deductible, in an amount not exceeding that which would be stipulated between independent enterprises, where one of the following conditions is met:
   (a) the amount of that interest is included in the tax base as income of the associated enterprise in accordance with Article 82;
   (b) the interest is paid to a company whose principal class of shares is regularly traded on one or more recognized stock exchanges;
   (c) the interest is paid to an entity engaged, in its country of residence, in the active conduct of a trade or business. This shall be understood as an independent economic enterprise carried on for profit and in the context of which officers and employees carry out substantial managerial and operational activities.

**Article 82 Controlled foreign companies**

1. The tax base shall include the non-distributed income of an entity resident in a third country where the following conditions are met:
   (a) the taxpayer by itself, or together with its associated enterprises, holds a direct or indirect participation of more than 50% of the voting rights, or owns more than 50% of capital or is entitled to receive more than 50% of the profits of that entity;
   (b) under the general regime in the third country, profits are taxable at a statutory corporate tax rate lower than 40% of the average statutory corporate tax rate applicable in the Member States, or the entity is subject to a special regime that allows for a substantially lower level of taxation than that of the general regime;
   (c) more than 30% of the income accruing to the entity falls within one or more of the categories set out in paragraph 3;
   (d) the company is not a company, whose principal class of shares is regularly traded on one or more recognized stock exchanges.

2. Paragraph 1 shall not apply where the third country is party to the European Economic Area Agreement and there is an agreement on the exchange of information comparable to the exchange of information on request provided for in Directive 2011/16/EU.

3. The following categories of income shall be taken into account for the purposes of point (c) of paragraph 1, in so far as more than 50% of the category of the entity’s income comes from transactions with the taxpayer or its associated enterprises:
   (a) interest or any other income generated by financial assets;
   (b) royalties or any other income generated by intellectual property;
   (c) dividends and income from the disposal of shares;
   (d) income from movable property;
   (e) income from immovable property, unless the Member State of the taxpayer would not have been entitled to tax the income under an agreement concluded with a third country;
   (f) income from insurance, banking and other financial activities.

**Article 83 Computation**

1. The income to be included in the tax base shall be calculated according to the rules of Articles 9 to 15. Losses of the foreign entity shall not be included in the tax base but shall be carried forward and taken into account when applying Article 82 in subsequent years.

2. The income to be included in the tax base shall be calculated in proportion to the entitlement of the taxpayer to share in the profits of the foreign entity.

3. The income shall be included in the tax year in which the tax year of the foreign entity ends.

4. Where the foreign entity subsequently distributes profits to the taxpayer, the amounts of income previously included in the tax base pursuant to Article 82 shall be deducted from the tax base when calculating the taxpayer’s liability to tax on the distributed income.

5. If the taxpayer disposes of its participation in the entity, the proceeds shall be reduced, for the
purposes of calculating the taxpayer’s liability to tax on those proceeds, by any undistributed
amounts which have already been included in the tax base.

Comment

Relation between the general and specific anti-abuse rules
Chapter XIV sets out three anti-abuse rules. Article 80 contains a general anti-abuse rule
(‘GAAR’). Two specific anti-abuse rules are also included. First in article 81, there is a deduction
limitation for interest payments to third countries and second in article 82, there is a rule
which provides for controlled foreign companies in third countries (‘CFC rule’).

This raises the question of what the relationship is of the GAAR to the specific anti-abuse
rules included in this Chapter (the limitation of the deduction of interest and the CFC rule), but
also to the specific anti-abuse rules such as the switch-over clause (article 73) and the dis-
allowance of exempt share disposals (article 75).

In the CCCTB Working Document 65 about anti-abuse rules (published 26 March 2008), it is
observed (point 9): ‘in the Commission Services view (...) would provide the tax administra-
tions with easily and straight forward specific rules to combat specific and well known cases of
abuse and a general rule could be applied to combat possible abuse that was not foreseen
when designing the common rules’. The observation that the GAAR ‘could be applied to
combat possible abuse that was not foreseen when designing the common rules’ is particularly
interesting. It must be noted, namely, that the specific anti-abuse provisions only have limited
effect, and in some situations, it would seem clear that certain structures are still possible. The
question is whether and to what extent these structures can be ‘foreseen’.

GAAR
The GAAR reads: ‘artificial transactions carried out for the sole purpose of avoiding taxation
shall be ignored for the purposes of calculating the tax base’. The wording of the provision is
not the same, but it is closely in line with the wording used by the CJ in judgments on direct
taxation in which abuse is at issue. In Cadbury, for example, the CJ mentions ‘wholly artificial
arrangements’ (see, for instance: ECJ 12 September 2006, C-196/04 Cadbury Schweppes). It
appears from a discussion document of the European Commission (Anti-abuse Rules in the
CCCTB, Room Document no. 4, 20 October 2010) that the GAAR and the CJ’s abuse case law can
be placed on one line. It appears from this same discussion document that it is the intention
that the GAAR ‘targets practices without economic substance’.

For the Member States, application of the GAAR would appear to be mandatory: artificial
transactions ‘shall be ignored’ (in German: ‘werden bei’). In essence, literal interpretation of
this text means that the tax administrations of the various Member States are obliged to
disregard artificial transactions. This is also understandable in light of the objective of the
CCCTB to introduce a set of common rules for computing the tax base of companies. Whether
the GAAR is used to combat certain constructions or not, however, in order to prevent major
discrepancies, this must be coordinated between the Member States. Application of the GAAR
will, in principle, take place by the principle tax authority of the group (although the Member
State of a group member can lodge objection to this; cf article 114 and article 123). I also
observe that the GAAR provides for the calculating of the tax base and not for the apportion-
ment of the consolidated tax base (articles 86 - 103). Abuse of the apportionment rules thus
does not fall under the GAAR.

The GAAR contains an escape clause. This reads: ‘the first paragraph shall not apply to
genuine commercial activities where the taxpayer is able to choose between two or more
possible transactions which have the same commercial result but which produce different
taxable amounts’. Here, the GAAR would appear to be in line with the Opinion of AG Kokott in
the Zwijnenburg case (CJ 20 May 2010, C-352/08, H&I 2010/9.5 (comments by Weber) in
which she observed on the concept of tax avoidance (points 42 - 44): ‘The Netherlands courts
hearing the proceedings are presuming that in this case the principal objective of the proposed
merger was the avoidance of transaction tax. They base that presumption on the fact that,
whilst there were valid commercial reasons for bringing the buildings at Tolstraat 17 and
Tolstraat 19 within one single company, there were no such reasons for the merger method
chosen. The Netherlands courts are therefore drawing a distinction here between the commercial aim of bringing two buildings within one single company, which they consider legitimate, and the merger route chosen for that purpose, which they consider to be an abuse. It seems to me that drawing such a distinction between aim and method excessively restricts economic freedom. A whole number of legally permissible set-ups might often be available to enable a legitimate economic proposal to be achieved, some of which might prove to have a more favourable tax regime than others. The fact that the parties ultimately choose the option that is most favourable for tax purposes cannot by itself be sufficient grounds on which to base charges of tax avoidance under Article 11(1)(a) of Directive 90/434.

Under the GAAR, the route chosen can no longer be brought up for discussion as long as this route only leads to genuine commercial transactions. With this escape clause, the GAAR allows broad tax planning possibilities for taxpayers, although practice will have to demonstrate how this is to be dealt with by the tax administrations and the courts.

**Deduction limitation for interest payments to third countries**

**Article 81** contains a rule on the basis of which, the deduction of interest can be refused. Interest paid to an associated enterprise in a third country shall not be deductible where there is no agreement on the exchange of information comparable to the exchange of information on request provided in the EU Mutual Assistance Directive and where one of the following conditions is met:

- the statutory corporate tax rate in the third State is lower than 40% of the average statutory rate in the EU.
- The associated enterprise is subject to a special regime in that third country which allows for a substantially lower level of taxation than that of the general regime.

Article 81 is only applicable to interest payments to associated enterprises (see for this, article 78) established in a third country. If interest is paid to a third party (for example, a bank), whereby guarantees are provided by an associated enterprise, article 81 is not applicable if strictly interpreted. The question, however, is whether the third party should not be ignored for this payment (so that the interest is in fact due to an associated enterprise).

**Article 73** sets out that the average statutory rate will be published by the Commission each year.

Whether there is a special regime which allows for a substantially lower level of taxation than that of the general regime, we can find inspiration in the problems concerning State aid, in which it is examined whether an aid measure is a selective measure. This selectivity is also assessed in the framework of the general rule of which it forms part. Whether there is a substantially lower level of taxation, the **effective** tax burden, according to my assumption, will be determinative. It is not clear what is meant precisely by a ‘substantially lower level of taxation’. Is this more or less than 50% of the normal tax burden? In this framework, we can also ask the question of whether the special regime test is a test on a case-by-case basis. This would appear to be the case. It would be beneficial to the legal certainty if the European Commission would publish an annual list with regimes of which it is assumed that there is a special regime.

Article 81 provides for an escape clause in the case one of the following conditions has been satisfied.

- interest is included in the tax base as income of the associated enterprise
- the interest is paid to a company whose principal class of shares is regularly traded on one or more recognized stock exchanges
- the interest is paid to an entity engaged, in its country of residence, in the active conduct of a trade or business. Active conduct of a trade or business is described as an ‘independent economic enterprise carried on for profit and in the context of which officers and employees carry out substantial managerial and operational activities’.

I note that it not required that the ‘active conduct of a trade or business’ bear connection to the interest received. Due to this, it is theoretically possible that in the case of an interest payment to an associated enterprise which only conducts an activity which is entirely unrelated to financing activities; the interest can still be deducted on the basis of the subject escape clause.
Finally, I remark that it is striking that where an agreement on the exchange of information is applicable, which contains a provision that is comparable to the exchange of information on request provided in the EU Mutual Assistance Directive, article 81 is no longer applicable. Thus, even if, in such a situation, the interest in the third State is taxed at a statutory corporate tax rate lower than 40% of the average EU corporate rate or in case of a special regime in the third State being applicable. That the deduction of interest paid to a third State is dependent on the existence of information would appear to have been prompted by the fact that the Commission wishes to respect the free movement of capital between the Member States and third countries. Given that the present case law of the CJ prohibits a restriction of the free movement of capital between the Member States and third countries when an agreement is applicable on the basis of which information can be exchanged (see CJ 28 October 2010, C-72/09 Rimbaud, H&I 2011/1.2 (comments by Szudoczky), the Commission only proposes the interest limitation rule when there is no question of such an exchange of information possibility. In light of the fact that increasing numbers of third States are concluding agreements regarding the exchange of information, this means that in many situations article 81 will not be applicable (certainly not if the other escape clauses are taken into consideration). The result is that in many situations, interest is deductible and that the CCCTB is more attractive on this point than many national corporate tax systems.

**CFC rule**

Article 82 contains a rule concerning controlled foreign companies (CFC). Under this rule, the non-distributed income of an entity resident in a third country is taxed under certain circumstances. The CFC rule exists alongside the switch-over clause of article 73 and is applicable without drawing a distinction as to whether the foreign company has active or passive income. The conditions under which the CFC rule may be made applicable are, in short:

- Control requirement: 50% voting rights or 50% capital, 50% right to the profits;
- Low tax jurisdiction: corporate tax rate lower than 40% of the average EU corporate rate or a special regime allowing for a substantially lower level of taxation than the general regime;
- More than 30% of the income accruing to the entity is ‘tainted’ (see article 82 (3));
- The entity’s principal class of shares is not regularly traded on more or more recognized stock exchanges.

An escape clause is set out in article 82 (2), which determines that the CFC rule is not applicable if the third country is party to the European Economic Area Agreement (Iceland, Liechtenstein and Norway) and there is an agreement on the exchange of information comparable to the exchange of information on request provided in the Mutual Assistance Directive. Thus, just as under article 81, an escape clause is applicable under the CFC rule on the basis of the exchange of information, however, with an important restriction that this is only the case for EEA agreement countries. Due to this, the CFC rule is much broader than the interest deduction limitation of article 81.

Article 83 sets out the calculation of the basis of the CFC. Non-distributed income is only taken into consideration in proportion to the entitlement of the taxpayer share in the profit of the foreign entity (para. 3), taxed CFC income, if it is distributed or if the participants are sold, is not taxed again at a later date (see: paras. 4 and 5).

Dennis Weber

## Chapter XV Transparent entities

**Article 84 Rules for allocating the income of transparent entities to taxpayers holding an interest**

1. Where an entity is treated as transparent in the Member State of its location, a taxpayer holding an interest in the entity shall include its share in the income of the entity in its tax base. For the purpose of this calculation, the income shall be computed under the rules of this Directive.

2. Transactions between a taxpayer and the entity shall be disregarded in proportion to the taxpayer’s share of the entity. Accordingly, the income of the taxpayer derived from such transactions shall be considered to be a proportion of the amount which would be agreed between
independent enterprises calculated on an arm's length basis which corresponds to the third party ownership of the entity.

3. The taxpayer shall be entitled to relief for double taxation in accordance with Article 76(1), (2), (3) and (5).

**Article 85 Rules for determining transparency in the case of third country entities**

Where an entity is located in a third country, the question whether or not it is transparent shall be determined according to the law of the Member State of the taxpayer. If at least two group members hold an interest in the same entity located in a third country, the treatment of the latter shall be determined by common agreement among the relevant Member States. If there is no agreement, the principal tax authority shall decide.

**Comment**

Chapter XV sets out the rules for determining the transparency of entities located in Member States (article 84 (1)) and entities located in third countries (article 85), as well as the consequences of transparency in calculating the tax base (article 84).

**Determining transparency**

The location of the respective entity is decisive in determining the transparency. If the entity is treated as transparent in the Member State of its location, it shall be treated as transparent for purposes of calculating the tax base (article 84 (1)). If the entity is located in a third country, the rules of article 85 apply. These rules distinguish between entities in which one taxpayer holds an interest (either alone or together with residents in third countries) and entities in which at least two group members hold an interest. If only one taxpayer holds an interest in the respective entity, the tax treatment in the Member State of this taxpayer is decisive. This should be interpreted as the tax treatment of the Member State where the taxpayer is resident according to article 6. If two or more group members hold an interest in the entity, the tax treatment of the entity is determined by common agreement among the relevant Member States and in the absence thereof, by the PTA. Generally, the PTP will first take a (defendable) position in the tax return (although technically, article 85 may be interpreted such that only the relevant Member State(s) (in common agreement) or the PTA may determine whether or not the entity is transparent). However, if and when challenged it may have to wait up to three years after the final date for filing of the tax return (the maximum term that amended assessments may be issued according to article 114 (3)) to have certainty on the qualification of the entity. In the meantime, the PTP does not seem to have any formal rights to influence the speed of this process. In view of this (potentially) long uncertainty, it can be questioned whether the method of article 85 is the best choice for determining transparency of third country entities instead of, for example, a decision of the PTA only.

**Entities located in more than one Member State and/or third country**

The Directive does not provide rules to determine the location of an entity. Article 6, paragraphs 3 - 5 provide rules to determine the residency of companies. Even if residency and location may be considered similar concepts, article 6 does not always apply to determine the location of entities, as not all entities are also companies. In particular, entities that are used as fund vehicles are often not companies but mere contractual arrangements. This may give rise to difficulties if an entity is considered located in more than one Member State and/or third country. For example: an entity which is not a company, is considered to be located in third country A as it was formed in that country, but also in Member State B as the effective management is located in that State. On the basis of the text of the Directive, there are two options for qualification of this entity: on the basis of article 85 (as the entity is incorporated in third country A), or following the (tax) treatment in Member State B pursuant to article 84 (1) (as the entity is effectively managed in Member State B). It would be consistent to follow the rules of article 6 (4) and, consequently, to determine the transparency on the basis of the Member State in which the entity has its effective management. This would mean that the tax treatment of Member State B is decisive pursuant to article 84. However, this is not provided
for in the text of the Directive. It is recommended that the Directive be amended on this point, for example, by applying article 6 (4) similarly to entities located in more than one Member State and/or third country.

**Consequences of transparency**

Article 84, paragraph 1 provides that if an entity is transparent, the taxpayer holding an interest in this entity includes its share in the income thereof in the tax base, which income is to be computed under the rules of the Directive. Transactions between the taxpayer and the entity are ignored in proportion to the taxpayer’s share on the basis of article 84 (2). Accordingly, income from such transactions is included in proportion to the third party’s share, however, subject to the arm’s length principle. Article 84 (3) stipulates that the taxpayer is entitled to relief for double taxation in accordance with article 76 (1), (2), (3) and (5). This paragraph 3 should be further clarified. Article 84 (1) stipulates that the income from transparent entities (in proportion to the share in the income) is to be computed under the rules of the Directive, which rules include article 11 (exempt revenues) and article 76 (tax credit). Consequently, article 84 (3) does not provide rules for relief for double taxation of income from the transparent entity to the extent of the taxpayer’s share. It rather seems to deal with relief for double taxation of income from transactions between the taxpayer and the entity to the extent of the third party’s interest in the entity, as well as with relief for double taxation of income realised by the transparent entity. In both such cases, double taxation is relieved following the rules of article 76 (1), (2), (3) and (5). As article 84 (3) makes no reference to article 76 (4), no expenses are to be deducted in calculating the limitation of the tax credit according to article 76 (3) and, thus, in such cases the tax credit is limited only to the Member State’s tax on the gross income.

Matthijs Vogel

**Chapter XVI Apportionment of the consolidated base**

**Article 86 General principles**

1. The consolidated tax base shall be shared between the group members in each tax year on the basis of a formula for apportionment. In determining the apportioned share of a group member A, the formula shall take the following form, giving equal weight to the factors of sales, labour and assets:

\[
\text{Share } A = \left( \frac{1}{3} \frac{\text{Sales}_A}{\text{Sales}_{\text{group}}} + \frac{1}{3} \frac{\text{Payroll}_A}{\text{Payroll}_{\text{group}}} + \frac{1}{2} \frac{\text{No of employees}_A}{\text{No of employees}_{\text{group}}} + \frac{1}{3} \frac{\text{Assets}_A}{\text{Assets}_{\text{group}}}. \right) \times \text{Cons’d Tax Base}
\]

2. The consolidated tax base of a group shall be shared only when it is positive.

3. The calculations for sharing the consolidated tax base shall be done at the end of the tax year of the group.

4. A period of 15 days or more in a calendar month shall be considered as a whole month.

**Article 87 Safeguard clause**

As an exception to the rule set out in Article 86, if the principle taxpayer or a competent authority considers that the outcome of the apportionment to a group member does not fairly represent the extent of the business activity of that group member, the principal taxpayer or the authority concerned may request the use of an alternative method. If, following consultations among the competent authorities and, where applicable, discussions held in accordance with Article 132, all these authorities agree to the alternative method, it shall be used. The Member State of the principal tax authority shall inform the Commission about the alternative method used.

**Article 88 Entering and leaving the group**

Where a company enters or leaves a group during a tax year, its apportioned share shall be computed proportionately having regard to the number of calendar months during which the company belonged to the group in the tax year.
**Article 89 Transparent entities**

Where a taxpayer holds an interest in a transparent entity, the factors used in calculating its apportioned share shall include the sales, payroll and assets of the transparent entity, in proportion to the taxpayer’s participation in its profits and losses.

**Article 90 Composition of the labour factor**

1. The labour factor shall consist, as to one half, of the total amount of the payroll of a group member as its numerator and the total amount of the payroll of the group as its denominator, and as to the other half, of the number of employees of a group member as its numerator and the number of employees of the group as its denominator. Where an individual employee is included in the labour factor of a group member, the amount of payroll relating to that employee shall also be allocated to the labour factor of that group member.

2. The number of employees shall be measured at the end of the tax year.

3. The definition of an employee shall be determined by the national law of the Member State where the employment is exercised.

**Article 91 Allocation of employees and payroll**

1. Employees shall be included in the labour factor of the group member from which they receive remuneration.

2. Notwithstanding paragraph 1, where employees physically exercise their employment under the control and responsibility of a group member other than that from which they receive remuneration, those employees and the amount of payroll relating to them shall be included in the labour factor of the former.

   This rule shall only apply where the following conditions are met:
   (a) this employment lasts for an uninterrupted period of at least three months;
   (b) such employees represent at least 5% of the overall number of employees of the group member from which they receive remuneration.

3. Notwithstanding paragraph 1, employees shall include persons who, though not employed directly by a group member, perform tasks similar to those performed by employees.

4. The term ‘payroll’ shall include the cost of salaries, wages, bonuses and all other employee compensation, including related pension and social security costs borne by the employer.

5. Payroll costs shall be valued at the amount of such expenses which are treated as deductible by the employer in a tax year.

**Article 92 Composition of the asset factor**

1. The asset factor shall consist of the average value of all fixed tangible assets owned, rented or leased by a group member as its numerator and the average value of all fixed tangible assets owned, rented or leased by the group as its denominator.

2. In the five years that follow a taxpayer’s entry into an existing or new group, its asset factor shall also include the total amount of costs incurred for research, development, marketing and advertising by the taxpayer over the six years that preceded its entry into the group.

**Article 93 Allocation of assets**

1. An asset shall be included in the asset factor of its economic owner. If the economic owner cannot be identified, the asset shall be included in the asset factor of the legal owner.

2. Notwithstanding paragraph 1, if an asset is not effectively used by its economic owner, the asset shall be included in the factor of the group member that effectively uses the asset. However, this rule shall only apply to assets that represent more than 5% of the value for tax purposes of all fixed tangible assets of the group member that effectively uses the asset.

3. Except in the case of leases between group members, leased assets shall be included in the asset factor of the group member which is the lessor or the lessee of the asset. The same shall apply to rented assets.

**Article 94 Valuation**

1. Land and other non-depreciable fixed tangible assets shall be valued at their original cost.
2. An individually depreciable fixed tangible asset shall be valued at the average of its value for tax purposes at the beginning and at the end of a tax year.

Where, as a result of one or more intra-group transactions, an individually depreciable fixed tangible asset is included in the asset factor of a group member for less than a tax year, the value to be taken into account shall be calculated having regard to the whole number of months.

3. The pool of fixed assets shall be valued at the average of its value for tax purposes at the beginning and at the end of a tax year.

4. Where the renter or lessee of an asset is not its economic owner, it shall value rented or leased assets at eight times the net annual rental or lease payment due, less any amounts receivable from sub-rentals or sub-leases.

Where a group member rents out or leases an asset but is not its economic owner, it shall value the rented or leased assets at eight times the net annual rental or lease payment due.

5. Where, following an intra-group transfer in the same or the previous tax year, a group member sells an asset outside the group, the asset shall be included in the asset factor of the transferring group member for the period between the intra-group transfer and the sale outside the group. This rule shall not apply where the group members concerned demonstrate that the intra-group transfer was made for genuine commercial reasons.

**Article 95 Composition of the sales factor**

1. The sales factor shall consist of the total sales of a group member (including a permanent establishment which is deemed to exist by virtue of the second subparagraph of Article 70(2) as its numerator and the total sales of the group as its denominator.

2. Sales shall mean the proceeds of all sales of goods and supplies of services after discounts and returns, excluding value added tax, other taxes and duties. Exempt revenues, interest, dividends, royalties and proceeds from the disposal of fixed assets shall not be included in the sales factor, unless they are revenues earned in the ordinary course of trade or business. Intra-group sales of goods and supplies of services shall not be included.

3. Sales shall be valued according to Article 22.

**Article 96 Sales by destination**

1. Sales of goods shall be included in the sales factor of the group member located in the Member State where dispatch or transport of the goods to the person acquiring them ends. If this place is not identifiable, the sales of goods shall be attributed to the group member located in the Member State of the last identifiable location of the goods.

2. Supplies of services shall be included in the sales factor of the group member located in the Member State where the services are physically carried out.

3. Where exempt revenues, interest, dividends and royalties and the proceeds from the disposal of assets are included in the sales factor, they shall be attributed to the beneficiary.

4. If there is no group member in the Member State where goods are delivered or services are carried out, or if goods are delivered or services are carried out in a third country, the sales shall be included in the sales factor of all group members in proportion to their labour and asset factors.

5. If there is more than one group member in the Member State where goods are delivered or services are carried out, the sales shall be included in the sales factor of all group members located in that Member State in proportion to their labour and asset factors.

**Article 97 Rules on calculation of factors**

The Commission may adopt acts laying down detailed rules on the calculation of the labour, asset and sales factors, the allocation of employees and payroll, assets and sales to the respective factor and the valuation of assets. Those implementing acts shall be adopted in accordance with the examination procedure referred to in Article 131(2).

**Article 98 Financial institutions**

1. The following entities shall be regarded as financial institutions:
(a) credit institutions authorised to operate in the Union in accordance with Directive 2006/48/EC of the European Parliament and of the Council;
(b) entities, except for insurance undertakings as defined in Article 99, which hold financial assets amounting to 80% or more of all their fixed assets, as valued in accordance with the rules of this Directive.

2. The asset factor of a financial institution shall include 10% of the value of financial assets, except for participating interests and own shares. Financial assets shall be included in the asset factor of the group member in the books of which they were recorded when it became a member of the group.

3. The sales factor of a financial institution shall include 10% of its revenues in the form of interest, fees, commissions and revenues from securities, excluding value added tax, other taxes and duties. For the purposes of Article 96(2), financial services shall be deemed to be carried out, in the case of a secured loan, in the Member State in which the security is situated or, if this Member State cannot be identified, the Member State in which the security is registered. Other financial services shall be deemed to be carried out in the Member State of the borrower or of the person who pays fees, commissions or other revenue. If the borrower or the person who pays fees, commissions or other revenue cannot be identified or if the Member State in which the security is situated or registered cannot be identified, the sales shall be attributed to all group members in proportion to their labour and asset factors.

Article 99 Insurance Undertakings

2. The asset factor of insurance undertakings shall include 10% of the value of financial assets as provided for in Article 98(2).

3. The sales factor of insurance undertakings shall include 10% of all earned premiums, net of reinsurance, allocated investment returns transferred from the non-technical account, other technical revenues, net of reinsurance, and investment revenues, fees and commissions, excluding value added tax, other taxes and duties. For the purposes of Article 96(2), insurance services shall be deemed to be carried out in the Member State of the policy holder. Other sales shall be attributed to all group members in proportion to their labour and asset factors.

Article 100 Oil and gas
Notwithstanding Article 96(1), (2) and (3), sales of a group member conducting its principal business in the field of the exploration or production of oil or gas shall be attributed to the group member in the Member State where the oil or gas is to be extracted or produced.

Notwithstanding Article 96(4) and (5), if there is no group member in the Member State of exploration or production of oil and gas or the exploration or production takes place in a third country where the group member which carries on the exploration or production of oil and gas does not maintain a permanent establishment, the sales shall be attributed to that group member.

Article 101 Shipping, inland waterways transport and air transport
The revenues, expenses and other deductible items of a group member whose principal business is the operation of ships or aircraft in international traffic or the operation of boats engaged in inland waterways transport shall not be apportioned according to the formula referred to in Article 86 but shall be attributed to that group member. Such a group member shall be excluded from the calculation of the apportionment formula.

Article 102 Items deductible against the apportioned share
The apportioned share shall be adjusted by the following items:

(a) unrelieved losses incurred by a taxpayer before entering the system provided for by this Directive, as provided for in Article 64;

(b) unrelieved losses incurred at the level of the group, as provided for in Article 64 in conjunction with Article 66(b) and in Article 71;
(c) the amounts relating to the disposal of fixed assets as provided for in Article 61, revenues and expenses related to long-term contracts as provided for in Article 62 and future expenses as provided for in Article 63;
(d) in the case of insurance undertakings, optional technical provisions as provided for in Article 30(c);
(e) the taxes listed in Annex III where a deduction is provided for under national rules.

Article 103 Tax liability

The tax liability of each group member shall be the outcome of the application of the national tax rate to the apportioned share, adjusted according to Article 102, and further reduced by the deductions provided for in Articles 76.

Comment

The consolidation of the group’s tax base requires a mechanism to allocate such basis to the taxpayers and the Member States concerned. Various possibilities for sharing have been considered by Commission Services, varying from macro-based apportionment based on factors such as gross domestic product or national VAT basis to micro-based apportionment. The latter method has been followed in the proposal for a Directive. The choice for formula apportionment (‘FA’) was also based on the fact that it has been applied in practice for many years in the US and Canada. The factors have also been discussed extensively. Reference is made to Working Paper 47 dated 17 November 2006 (The mechanism for sharing the CCCTB), Working Paper 52 dated 27 February 2007 (An overview of the main issues that emerged during the discussion on the mechanism for sharing the CCCTB), paragraph III of Working Paper 55 dated 28 June 2007 (Summary record of the meeting of the CCCTB Working group) and Working Paper 60 dated 13 November 2007 (CCCTB: Possible elements of the sharing mechanism). In the latter paper, Commission Services presented the initial ideas on a possible apportion mechanism for a CCCTB. A three-factor formula based on company-specific data (labour, split in payroll and number of employees, and assets and sales) was seen as ‘a promising approach’ for sharing. According to Commission Services (WP 60 paragraph 8), the sharing mechanism aims:

• to be as simple as possible to apply for taxpayers and tax administrations and easy to audit for tax administrations;
• to be difficult to manipulate by taxpayers, i.e. the mechanism should not rely on factors, the locations of which are easy to move so as to artificially shift (part of) the consolidated taxable base to benefit from any differential in corporate income tax rates across the EU;
• to distribute the tax base among the various entities concerned in a way that can be considered to be fair and equitable; and
• not to lead to undesirable effects in terms of tax competition.

Commission Services realized that such formula might work out unfairly in particular cases and recommended the introduction of a ‘safeguard clause’ in case the outcome of the apportionment for a specific company would obviously lead to an unfair result. Experts were invited to comment on the ideas presented in WP 60.

From the proposal for a Directive, we may conclude that almost all the initial ideas have been followed. A few points should be noted. The Commission Services considered that the weighing of the factors in the formula is not a technical issue but a political one. Therefore, no specific weighing to factors was given. From article 86 (1) Directive, it follows that the Commission proposes to give equal weight to the factors sales, labour and assets.

The proposed FA will be a key element for the Member States in their decision whether or not to adopt the CCCTB. The allocation of consolidated taxable profit will directly impact tax revenues for the Member State concerned. Despite all the research that has been conducted with respect to the impact assessment for each Member State, the actual outcome can hardly be predicted. The outcome also depends on factors beyond the control of Member States. Whether or not taxpayers will opt for the system will have to be awaited. Per company (group of companies), the apportionment based on the formula may differ substantially from the
apportionment based on the arm's length principle. It is uncertain how this will work out for Member States and whether the outcome will indeed be in line with the impact assessments that were attached to the proposal for a Directive. Apart from the uncertainty with respect to the outcome, the Member States will no longer have a grip on the taxation of resident taxpayers opting for the system.

Article 87, the safeguard clause, may in specific cases lead to an alternative method for apportionment. Although Commission Services has stressed the usefulness of the safeguard clause to amend an unfair result of the FA, we may have doubts as to how often this clause will be applied in practice. From the outset, it is clear that apportionment to taxpayers based on the sharing formula will result in an allocation of the taxable base which differs from an arm’s length allocation. It is not logical to adjust the FA in a specific case in order to arrive in such a case at a result which comes closer to an arm’s length pricing apportionment. The fact that the apportionment to a particular taxpayer may be quite different than under the arm’s length principle, should still be acceptable for Member States if on a macro basis, each Member State receives a fair share. If nevertheless the PTP or one or more competent tax authorities file a request for an alternative method for apportionment, chances of such request being approved seem to be remote. The competent authorities decide whether and to what extent an alternative method should be applied. However, this will only be possible if all competent authorities agree. Based on the proposal, discussions on the safeguard clause are delegated to the Commission in accordance with Article 291 TFEU.

The Commission will review the application of the Directive five years after its entry into force. According to Article 133, this review will, in particular, include an analysis of the impact of the sharing mechanism on the distribution of the tax bases between the Member States. However, the chance of such review leading to drastic changes seems remote, certainly if many groups have opted into the system in the meantime. We can safely assume that once the CCCTB has been accepted, there will be no way back for the Member State involved. Adoption of this Directive, therefore, requires a considerable step which not all Member States may be prepared to take. If the potential impact on the distribution of the tax bases should block further steps forward, even within a select group of Member States based on enhanced cooperation, the Commission could consider a proposal to share the consolidated profit for an interim period based on the actual distribution percentages of the participating Member States in the year(s) prior to the introduction of the CCCTB, irrespective of the distribution resulting from the sharing formula. This would give some time to evaluate the impact of the sharing formula, without immediate pressure to amend the formula. Based on the review after five years, an amendment of the formula could be proposed if the impact of the sharing formula is considered not acceptable. The disadvantage of such distribution based on pre-CCCTB percentages is that changes that take place during the interim period will not be reflected in the distribution of the tax bases.

From the perspective of the taxpayers (groups) that have opted for the system, it makes sense that once CCCTB becomes applicable, the rules will remain unchanged as much as possible. Even without changes, CCCTB will be a challenging exercise for the PTP and its group members. Groups considering to opt for the system will probably, prior to making an election for the system, make a test run based on recent annual (tax) accounts of the group companies concerned. The impact of the FA and the questions it will trigger will only become clear when applied in practice.

The first test is whether the group can produce all data relevant for filing the consolidated return. Based on Article 109(5) the consolidated tax return shall be filed in the nine months that follow the end of the tax year. This may be difficult, because in one or more Member States, past tax years of the various group companies will not have been finally settled at the time the consolidated tax return has to be filed. Determining the factors for the formula apportionment for all group companies concerned may also prove to be difficult. The various studies and discussions within working groups have resulted in one single formula to be applied in all cases, unless otherwise stipulated in the Directive. The formula should lead to a relatively simple mathematical exercise. A test run will also make clear whether this is indeed the case and where more guidance is needed as to how the factors should be applied. From various provisions in the proposal for a Directive, it is clear that more detailed rules can be
introduced at a later stage. However, inclusion of sufficiently detailed rules in the Directive is preferred in order to provide clarity to taxpayers what the consequences of opting for the system will be. This also limits unforeseen amendments once taxpayers are within the system. Once a taxpayer or group has opted in (and as long as it is not able to opt out again), the changes in applicable rules should be kept to a minimum. This also applies to the sharing formula to be applied. As mentioned, it seems unlikely that the safeguard clause will often be applied.

As mentioned before, it seems unlikely that the safeguard clause will often be applied. Even though this may be the case, a more detailed description of the terms and conditions to be fulfilled and the position of the PTP in this process would seem appropriate. We can imagine that such alternative method will only be applicable in future tax years and that the PTP has the right to terminate the group (leave the system). Based on the text of the current proposal, the PTP may request for a different method, but has no say whatsoever in the decision on whether or not the method will be adjusted and if so, in what way.

Article 88 provides a practical rule for companies entering or leaving the group during the year. The PTP files its group tax return on an annual basis. The profit of that year is apportioned to the entering/leaving company on a pro rata (calendar month) basis. This means that developments which occurred during the period the entering/leaving company did not form part of the group will affect the profit apportioned to that company. Nevertheless, this approach makes sense. The alternative, making split year calculations for the entire group, would (also in view of the frequent changes in the corporate structure that might occur and the mandatory nature of the group) introduce a great deal of work.

Once the taxpayer forms part of a group, its total sales, assets, payroll and employees will be included in the formula, even if the group does not hold a 100% interest in the taxpayer concerned. For PEs and transparent entities, the factors used in the calculation of the apportioned share shall include the sales, payroll and assets in proportion to the taxpayer’s participations in profits and losses (article 89). The number of employees is not mentioned here.

Articles 90 - 96 elaborate on the various factors of the formula. With respect to these factors, various comments can be made. For instance, the asset factor does not include intangible assets (article 92(1)) which assets may be the key value drivers of an enterprise. The Commission has considered this point but had concerns that by way of transfers, the sharing formula would be manipulated. Furthermore, valuation of intangibles may be difficult. In paragraphs 8 and 9 of Room Document 2 dated 2 September 2010, the Commission suggested adjusting the asset factor for R&D costs, marketing costs and advertising costs in order to take into account that self-generated assets may represent a substantial factor in the value chain, which should be reflected in the sharing formula. The concept was to use a proxy for the profit that is expected to be earned by adding to the asset base of the relevant group member for a period of five years an amount equal to the total costs for R&D, marketing and advertising incurred by that group member over the five years which precede its group entry. Article 92(2) provides for such an adjustment, albeit that the costs over a six-year period preceding the entry into the group will be included in the asset factor. We can have doubts whether this will indeed lead to a better apportionment in specific cases. However, if the aim is to keep the apportionment formula simple and free from manipulation, it is not easy to come up with a much better adjustment. Amendments to the asset factor can also be found elsewhere in the Directive. Reference is made to article 70(2) (five years adjustment of the asset factor in case of a particular transfer within the group).

Such adjustments of the asset factor in the sharing formula should be distinguished from an adjusted apportionment of consolidated profit by attributing specific income to a group member. Some but not all of these adjustments are summarized in article 102. For instance, article 61 (5) provides for an adjusted profit allocation if within five years after entry into a group certain fixed assets are disposed of by the group. In Chapter X, other adjustments in the apportioned share are mentioned. Article 67 provides for an adjustment for disposals within three years of leaving a group. Article 68 provides for adjustments of the apportioned share in case of self-generated intangible assets if a taxpayer leaves the group.

Remarks can also be made with respect to the other factors in the sharing formula. Various choices have been made which could also have been different. Arguments for and against can
be found in the working papers mentioned above. As mentioned before, the Commission has primarily looked for simplicity and although a fair and equitable apportionment is also one of the aims of the sharing mechanism, it is clear that if Member States wish to offer their taxpayers a workable system, simplicity and stability form key-elements.

On that point, we can wonder whether and to what extent specific provisions to (partially) eliminate the impact on the asset factor of particular transactions should be introduced. The impact of these specific provisions on a macro level will most probably not be substantial and fine-tuning for specific transactions may lead to more complexity than justified. The long-term solution to counteract such transactions is probably that Member States signing up for CCCTB apply tax rates which are within a certain range. However, that thought may not be shared in the capitals of all Member States. We can safely assume that the Commission has well considered all alternatives and has reached the conclusion that simplicity is key if CCCTB should find its way to taxpayers.

Article 97 provides that the Commission may adopt detailed rules on the calculation of the labour and sales factors, the allocation of employees and payroll, assets and sales to the respective factor and the valuation of assets. Although further clarification in the application of the sharing formula will certainly be needed, we hope that the Commission can resist the pressure to address all particulars of taxpayers that have opted for the system in more detailed rules. Also here, once a taxpayer or group has opted in, changes in the applicable rules should be kept to a minimum. Reference is made to the remarks above with respect to the safeguard clause.

In WP 60 paragraph 69, Commission Services considered that in view of the specific characteristics of some economic sectors, the proposed formula may not adequately reflect the profit generating factors. In the view of Commission Services, the sector financial services, transportation services such as airlines and railways, and television and broadcasting services needed special formulas. Amended formulas have been worked out in more detail in the proposal for a Directive in articles 98 - 101 for financial institutions, insurance undertakings, the exploitation and production of oil and gas, shipping and air transport. The adjustment varies per sector: for financial institutions and insurance undertakings, the asset factor and the sales factor are defined differently. For insurance undertakings, article 30(c) also provides for a special rule with respect to equalisation provisions. Such provisions are allowed but, unlike technical provisions in line with Directive 91/67EEC, are not deducted from the consolidated profit but from the apportioned share of the taxpayer (Member State) concerned. For E&P companies, the sales by destination principle is replaced by a source principle (group member in the Member State where the oil and gas is to be extracted or produced). Taxpayers having their principal business in the operations of ships or aircraft in international traffic or the operation of boats engaged in inland waterways transport shall be excluded from the FA. The revenues and expenses of such a group member shall be attributed to that group member. Because in article 101, such taxpayer is still qualified as a ‘group member’, we can wonder whether in determining the ‘revenues and expenses’ intra-group transactions should be eliminated (article 59) and whether the attribution of revenues and expenses takes place before or after loss set off within the group. According to the Directive, ‘apportionment’ only takes place when the consolidated tax base of a group is positive. On the other hand, ‘attribution of revenues and expenses’ suggests that no consolidation takes place at all. From article 104(2), it seems clear that shipping companies subject to a special taxation regime may be excluded from the group.

Paul Simonis

Chapter XVIII Administration and procedures

Article 104 Notice to opt

1. A single taxpayer shall opt for the system provided for by this Directive by giving notice to the competent authority of the Member State in which it is resident or, in respect of a permanent establishment of a non-resident taxpayer, that establishment is situated. In the case of a group, the principal taxpayer shall give notice, on behalf of the group, to the principal tax authority.
Such notice shall be given at least three months before the beginning of the tax year in which the taxpayer or the group wishes to begin applying the system.

2. The notice to opt shall cover all group members. However, shipping companies subject to a special taxation regime may be excluded from the group.

3. The principal tax authority shall transmit the notice to opt immediately to the competent authorities of all Member States in which group members are resident or established. Those authorities may submit to the principal tax authority, within one month of the transmission, their views and any relevant information on the validity and scope of the notice to opt.

Article 105 Term of a Group

1. When the notice to opt has been accepted, a single taxpayer or a group, as the case may be, shall apply the system provided for by this Directive for five tax years. Following the expiry of that initial term, the single taxpayer or the group shall continue to apply the system for successive terms of three tax years unless it gives notice of termination. A notice of termination may be given by a taxpayer to its competent authority or, in the case of a group, by the principal taxpayer to the principal tax authority in the three months preceding the end of the initial term or of a subsequent term.

2. Where a taxpayer or a non-taxpayer joins a group, the term of the group shall not be affected. Where a group joins another group or two or more groups merge, the enlarged group shall continue to apply the system until the later of the expiry dates of the terms of the groups, unless exceptional circumstances make it more appropriate to apply a shorter period.

3. Where a taxpayer leaves a group or a group terminates, the taxpayer or taxpayers shall continue to apply the system for the remainder of the current term of the group.

Article 106 Information in the notice to opt

The following information shall be included in the notice to opt:
(a) the identification of the taxpayer or of the members of the group;
(b) in respect of a group, proof of fulfilment of the criteria laid down in Articles 54 and 55;
(c) identification of any associated enterprises as referred to in Articles 78;
(d) the legal form, statutory seat and place of effective management of the taxpayers;
(e) the tax year to be applied.

The Commission may adopt an act establishing a standard form of the notice to opt. That implementing act shall be adopted in accordance with the examination procedure referred to in Article 131(2).

Article 107 Control of the notice to opt

1. The competent authority to which the notice to opt is validly submitted shall examine whether, on the basis of the information contained in the notice, the group fulfils the requirements of this Directive. Unless the notice is rejected within three months of its receipt, it shall be deemed to have been accepted.

2. Provided that the taxpayer has fully disclosed all relevant information in accordance with Article 106, any subsequent determination that the disclosed list of group members is incorrect shall not invalidate the notice to opt. The notice shall be corrected, and all other necessary measures shall be taken, from the beginning of the tax year when the discovery is made. Where there has not been full disclosure, the principal tax authority, in agreement with the other competent authorities concerned, may invalidate the original notice to opt.

Article 108 Tax year

1. All members of a group shall have the same tax year.

2. In the year in which it joins an existing group, a taxpayer shall bring its tax year into line with that of the group. The apportioned share of the taxpayer for that tax year shall be calculated proportionately having regard to the number of calendar months during which the company belonged to the group.

3. The apportioned share of a taxpayer for the year in which it leaves a group shall be calculated proportionately having regard to the number of calendar months during which the company belonged to the group.
4. Where a single taxpayer joins a group, it shall be treated as though its tax year terminated on the day before joining.

**Article 109 Filing a tax return**

1. A single taxpayer shall file its tax return with the competent authority.

   In the case of a group, the principal taxpayer shall file the consolidated tax return of the group with the principal tax authority.

2. The return shall be treated as an assessment of the tax liability of each group member. Where the law of a Member State provides that a tax return has the legal status of a tax assessment and is to be treated as an instrument permitting the enforcement of tax debts, the consolidated tax return shall have the same effect in relation to a group member liable for tax in that Member State.

3. Where the consolidated tax return does not have the legal status of a tax assessment for the purposes of enforcing a tax debt, the competent authority of a Member State may, in respect of a group member which is resident or situated there, issue an instrument of national law authorising enforcement in the Member State. That instrument shall incorporate the data in the consolidated tax return concerning the group member. Appeals shall be permitted against the instrument exclusively on grounds of form and not to the underlying assessment. The procedure shall be governed by the national law of the relevant Member State.

4. Where a permanent establishment is deemed to exist pursuant to the third paragraph of Article 61, the principal taxpayer shall be responsible for all procedural obligations relating to the taxation of such a permanent establishment.

5. The tax return of a single taxpayer shall be filed within the period provided for in the law of the Member State in which it is resident or in which it has a permanent establishment. The consolidated tax return shall be filed in the nine months that follow the end of the tax year.

**Article 110 Content of tax return**

1. The tax return of a single taxpayer shall include the following information:
   (a) the identification of the taxpayer;
   (b) the tax year to which the tax return relates;
   (c) the calculation of the tax base;
   (d) identification of any associated enterprises as referred to in Article 78.

2. The consolidated tax return shall include the following information:
   (a) the identification of the principal taxpayer;
   (b) the identification of all group members;
   (c) identification of any associated enterprises as referred to in Article 78;
   (d) the tax year to which the tax return relates;
   (e) the calculation of the tax base of each group member;
   (f) the calculation of the consolidated tax base;
   (g) the calculation of the apportioned share of each group member;
   (h) the calculation of the tax liability of each group member.

**Article 111 Notification of errors in the tax return**

The principal taxpayer shall notify the principal tax authority of errors in the consolidated tax return. The principal tax authority shall, where appropriate, issue an amended assessment according to Article 114(3).

**Article 112 Failure to file a tax return**

Where the principal taxpayer fails to file a consolidated tax return, the principal tax authority shall issue an assessment within three months based on an estimate, taking into account such information as is available. The principal taxpayer may appeal against such an assessment.

**Article 113 Rules on electronic filing, tax returns and supporting documentation**

The Commission may adopt acts laying down rules on electronic filing, on the form of the tax return, on the form of the consolidated tax return, and on the supporting documentation required. Those implementing acts shall be adopted in accordance with the examination procedure referred to in Article 131(2).
Article 114 Amended assessments

1. In relation to a single taxpayer, audits and assessments shall be governed by the law of the Member State in which it is resident or in which it has a permanent establishment.

2. The principal tax authority shall verify that the consolidated tax return complies with Article 110(2).

3. The principal tax authority may issue an amended assessment not later than three years after the final date for filing the consolidated tax return or, where no return was filed before that date, not later than three years following issuance of an assessment pursuant to Article 112.

   An amended assessment may not be issued more than once in any period of 12 months.

4. Paragraph 3 shall not apply where an amended assessment is issued in compliance with a decision of the courts of the Member State of the principal tax authority according to Article 123 or with the result of a mutual agreement or arbitration procedure with a third country. Such amended assessments shall be issued within 12 months of the decision of the courts of the principal tax authority or the completion of the procedure.

5. Notwithstanding paragraph 3, an amended assessment may be issued within six years of the final date for filing the consolidated tax return where it is justified by a deliberate or grossly negligent misstatement on the part of a taxpayer, or within 12 years of that date where the misstatement is the subject of criminal proceedings. Such an amended assessment shall be issued within 12 months of the discovery of the misstatement, unless a longer period is objectively justified by the need for further inquiries or investigations. Any such amended assessment shall relate solely to the subject-matter of the misstatement.

6. Prior to issuing an amended assessment, the principal tax authority shall consult the competent authorities of the Member States in which a group member is resident or established. Those authorities may express their views within one month of consultation.

   The competent authority of a Member State in which a group member is resident or established may call on the principal tax authority to issue an amended assessment. Failure to issue such an assessment within three months shall be deemed to be a refusal to do so.

7. No amended assessment shall be issued in order to adjust the consolidated tax base where the difference between the declared base and the corrected base does not exceed the lower of EUR 5,000 or 1% of the consolidated tax base.

   No amended assessment shall be issued in order to adjust the calculation of the apportioned shares where the total of the apportioned shares of the group members resident or established in a Member State would be adjusted by less than 0.5%.

Article 115 Central data base

The consolidated tax return and supporting documents filed by the principal taxpayer shall be stored on a central data base to which all the competent authorities shall have access. The central data base shall be regularly updated with all further information and documents and all decisions and notices issued by the principal tax authority.

Article 116 Designation of the principal taxpayer

The principal taxpayer designated in accordance with Article 4(6) may not subsequently be changed. However, where the principal taxpayer ceases to meet the criteria in Article 4(6) a new principal taxpayer shall be designated by the group.

In exceptional circumstances the competent tax authorities of the Member States in which the members of a group are resident or in which they have a permanent establishment may, within six months of the notice to opt or within six months of a reorganisation involving the principal taxpayer, decide by common agreement that a taxpayer other than the taxpayer designated by the group shall be the principal taxpayer.

Article 117 Record-keeping

A single taxpayer and, in the case of a group, each group member shall keep records and supporting documents in sufficient detail to ensure the proper implementation of this Directive and to allow audits to be carried out.
Article 118 Provision of information to the competent authorities

On a request from the competent authority of the Member State in which it is resident or in which its permanent establishment is situated, a taxpayer shall provide all information relevant to the determination of its tax liability. On a request from the principal tax authority, the principal taxpayer shall provide all information relevant to the determination of the consolidated tax base or of the tax liability of any group member.

Article 119 Request for an opinion by the competent authority

1. A taxpayer may request an opinion from the competent authority of the Member State in which it is resident or in which it has a permanent establishment on the implementation of this Directive to a specific transaction or series of transactions planned to be carried out. A taxpayer may also request an opinion regarding the proposed composition of a group. The competent authority shall take all possible steps to respond to the request within a reasonable time.

Provided that all relevant information concerning the planned transaction or series of transactions is disclosed, the opinion issued by the competent authority shall be binding on it, unless the courts of the Member State of the principal tax authority subsequently decide otherwise pursuant to Article 123. If the taxpayer disagrees with the opinion, it may act in accordance with its own interpretation but must draw attention to that fact in its tax return or consolidated tax return.

2. Where two or more group members in different Member States are directly involved in a specific transaction or a series of transactions, or where the request concerns the proposed composition of a group, the competent authorities of those Member States shall agree on a common opinion.

Article 120 Communication between competent authorities

1. Information communicated pursuant to this Directive shall, to the extent possible, be provided by electronic means, through making use of the common communication network/common system interface (CCN/CSI).

2. When a competent authority receives a request for cooperation or exchange of information concerning a group member pursuant to Directive 2011/16/EU, it shall respond no later than in three months following the date of receipt of the request.

Article 121 Secrecy clause

1. All information made known to a Member State under this Directive shall be kept secret in that Member State in the same manner as information received under its domestic legislation. In any case, such information:

(a) may be made available only to the persons directly involved in the assessment of the tax or in the administrative control of this assessment;

(b) may in addition be made known only in connection with judicial proceedings or administrative proceedings involving sanctions undertaken with a view to, or relating to, the making or reviewing the tax assessment and only to persons who are directly involved in such proceedings; such information may, however, be disclosed during public hearings or in judgements if the competent authority of the Member State supplying the information raises no objection;

(c) shall in no circumstances be used other than for taxation purposes or in connection with judicial proceedings or administrative proceedings involving sanctions undertaken with a view to, or in relation to, the making or reviewing the tax assessment.

In addition, Member States may provide for the information referred to in the first subparagraph to be used for assessment of other levies, duties and taxes covered by Article 2 of Council Directive 2008/55/EC1.

2. Notwithstanding paragraph 1, the competent authority of the Member State providing the information may permit it to be used for other purposes in the requesting State, if, under the legislation of the informing State, the information could, in similar circumstances, be used in the informing State for similar purposes.

Article 122 Audits
1. The principal tax authority may initiate and coordinate audits of group members. An audit may also be initiated on the request of a competent authority. The principal tax authority and the other competent authorities concerned shall jointly determine the scope and content of an audit and the group members to be audited.
2. An audit shall be conducted in accordance with the national legislation of the Member State in which it is carried out, subject to such adjustments as are necessary in order to ensure proper implementation of this Directive.
3. The principal tax authority shall compile the results of all audits.

Article 123 Disagreement between Member States
1. Where the competent authority of the Member State in which a group member is resident or established disagrees with a decision of the principal tax authority made pursuant to Articles 107 or Article 114 paragraphs (3), (5) or (6) second subparagraph, it may challenge that decision before the courts of the Member State of the principal tax authority within a period of three months.
2. The competent authority shall have at least the same procedural rights as a taxpayer enjoys under the law of that Member State in proceedings against a decision of the principal tax authority.

Article 124 Appeals
1. A principal taxpayer may appeal against the following acts:
   (a) a decision rejecting a notice to opt;
   (b) a notice requesting the disclosure of documents or information;
   (c) an amended assessment;
   (d) an assessment on the failure to file a consolidated tax return.
   The appeal shall be lodged within 60 days of the receipt of the act appealed against.
2. An appeal shall not have any suspensory effect on the tax liability of a taxpayer.
3. Notwithstanding Article 114(3), an amended assessment may be issued to give effect to the result of an appeal.

Article 125 Administrative appeals
1. Appeals against amended assessments or assessments made pursuant to Article 112 shall be heard by an administrative body which is competent to hear appeals at first instance according to the law of the Member State of the principal tax authority. If, in that Member State, there is no such competent administrative body, the principal taxpayer may lodge directly a judicial appeal.
2. In making submissions to the administrative body, the principal tax authority shall act in close consultation with the other competent authorities.
3. An administrative body may, where appropriate, order evidence to be provided by the principal taxpayer and the principal tax authority on the fiscal affairs of the group members and other associated enterprises and on the law and practices of the other Member States concerned. The competent authorities of the other Member States concerned shall provide all necessary assistance to the principal tax authority.
4. Where the administrative body varies the decision of the principal tax authority, the varied decision shall take the place of the latter and shall be treated as the decision of the principal tax authority.
5. The administrative body shall decide the appeal within six months. If no decision is received by the principal taxpayer within that period, the decision of the principal tax authority shall be deemed to have been confirmed.
6. Where the decision is confirmed or varied, the principal taxpayer shall have the right to appeal directly to the courts of the Member State of the principal tax authority within 60 days of the receipt of the decision of the administrative appeals body.
7. Where the decision is annulled, the administrative body shall remit the matter to the principal tax authority, which shall take a new decision within 60 days of the date on which the decision of the administrative body is notified to it. The principal taxpayer may appeal against any such new decision either pursuant to paragraph 1 or directly to the courts of the Member State of the principal tax authority within 60 days of receipt of the decision. If the principal tax authority does not take a new decision within 60 days, the principal taxpayer may appeal against the original
decision of the principal tax authority before the courts of the Member State of the principal tax authority.

Article 126 Judicial appeals

1. A judicial appeal against a decision of the principal tax authority shall be governed by the law of the Member State of that principal tax authority, subject to paragraph 3.

2. In making submissions to the courts, the principal tax authority shall act in close consultation with the other competent authorities.

3. A national court may, where appropriate, order evidence to be provided by the principal taxpayer and the principal tax authority on the fiscal affairs of the group members and other associated enterprises and on the law and practices of the other Member States concerned. The competent authorities of the other Member States concerned shall provide all necessary assistance to the principal tax authority.

Comment

Chapter XVII sets out the administrative and procedural framework. Groups of companies should be able to deal with a single principal tax administration (‘PTA’), which should be that of the Member State in which the principal taxpayer (‘PTP’) is resident for tax purposes. It is a well-known fact that there are major differences in the way tax administrations of various Member States approach their taxpayers or may be approached by them. The introduction of a CCCTB might be the impulse to some interesting relocation efforts, to the extent possible under article 4 (6). In this respect, it is remarkable that to date, no attention has been given to the developing concept of enhanced compliance, endorsed by some Member States. The application of that concept by a PTA could be seriously hampered if other Member States exercise their right to request a (classic) tax audit or challenge the decisions made under a compliance agreement. Effort should be given to ‘harmonizing’ the way tax administrations deal with the kind of companies that are likely to opt for CCCTB.

Notice to opt

Article 104 The PTP shall give notice to opt (‘NTO’) to the PTA ‘on behalf of’ the group. The Council Directive does not seem to require co-signing of the NTO by all members of the group. This gives rise to the question of what consequences would be if consent of group members has not been obtained. Would this invalidate the NTO or could a dissenting group member hold the PTP liable? Upon receipt of the NTO, the PTA shall immediately transmit the NTO to the competent tax authorities (‘TAs’) of all Member States in which group members are resident or established. Those TAs must submit their views and any relevant information within one month of the transmission. The NTO should be given at least three months before the beginning of the tax year. This seems only natural, but there are no principal objections to a rule which allows opting-in within three months after the end of the tax year. Opting-in could have adverse consequences for a group member that is in a loss-making position on a standalone basis, as a taxpaying position could arise, for example, if the group, as a whole, is in a taxpaying position. A corporate law issue in this respect could be that opting-in does not seem to be in the corporate interest of such group member, leading to possible liability for the directors. A solution for this issue might be, for example, that members of a group conclude tax-sharing agreements. Shipping companies, subject to a special tax regime, are excluded. This might help avoid an adverse effect of the consolidation on the tax burden. There are other regimes, such as portfolio investment regimes, which might justify a similar rule. The submissions of the TAs of their views on the NTO could be made available to the PTP.

The initial term for applying the system is five tax years, followed by successive terms of three tax years. Notice of termination must be given three months before the end of a term. Please note that the wording does not require the PTP to give notice ‘on behalf of the group’.

Article 105, paragraphs 2 and 3 determine what happens when a group is expanded, joined, split or reduced. It does not, however, make clear what will happen if the group is the subject of a takeover which results in another company, which has not opted to apply the Directive, taking over the role of principal taxpayer. In the event a taxpayer leaves a group or the group
terminates, the system (i.e. the common base, without consolidation) must be applied for the remainder of the current term. Application of the common base thus cannot be avoided by leaving a group.

The tax year can deviate from the calendar year (article 106 (e)). This assumes that the possibility to have a tax year that is not concurrent with the calendar year exists in all Member States.

Article 107 determines that the PTA shall examine whether the group fulfils the requirements. The NTO is deemed to have been accepted unless rejected within three months. A deemed acceptance gives rise to the question of what the tax status of the group will be if the group did not fulfil the requirements. We doubt whether paragraph 2 answers this question since this paragraph seems to deal with irregularities, discovered after the implementation of the CCCTB. On the other hand, it does not seem likely that this article would allow for the indefinite application of the CCCTB to a non-qualifying group solely on the basis of a deemed acceptance. Some clarification would be welcome. If the taxpayer has fully disclosed all relevant information, the NTO will not be invalidated by any subsequent determination that the list of group members is incorrect. The notice will be corrected, and all other necessary measures will be taken, from the beginning of the tax year when the discovery is made. Where there has not been full disclosure, the PTA may invalidate the original NTO. This appears to be intended to allow the PTA, in agreement with the other TAs concerned, to determine whether it is deemed necessary to invalidate the NTO. The reference to ‘the original NTO’ seems to allow retroactive effect to the moment that the Directive was first applied. The question arises whether this entails that only two scenarios can take place: either continuation ‘as is’ or invalidation of the NTO as from the moment the Directive was first applied.

All members of a group shall have the same tax year. Specific provisions apply to taxpayers joining or leaving a group. Please note that in article 108, paragraph 4 provides for a taxpayer that is already in the system.

**Tax return**

The PTP files the consolidated tax return of the group and it shall be treated as an assessment of the tax liability of each group member. A consolidated tax return is treated as an assessment. This will equally be so for group members resident in a Member State which also treats a tax return as an assessment. If it is not a tax assessment, a Member State may issue a pro forma assessment with regard to the group member which is resident or situated in that Member State. The term ‘may’ allows for TAs to determine whether it is necessary to issue such instrument. No appeal is possible against the assessment/instrument as such. A consolidated tax return must be filed within nine months after the tax year, whereby no extension is possible. It should be considered to create an extension regime, as already exists under the national law of some Member States.

Article 110 sets out the information which is to be included in the (consolidated) tax return. A uniform tax return could be expected, for both single and consolidated taxpayers. The consolidated tax return must contain, for example, the calculation of (i) the consolidated tax base; (ii) the apportioned share of each group member; and (iii) the tax liability of each group member. These requirements place a substantial part of the burden of applying the Directive with the taxpayer. Taxpayers are required to fully explore and understand the calculation of the common base and determine the formula apportionment, whereas TAs are not obliged to take a pro-active role. The PTP shall notify the PTA of errors in the tax return and the PTA shall, where appropriate, issue an amended assessment. The term ‘appropriate’ allows for a broad interpretation by the PTA, but the PTP does not appear to have the option to appeal in the event the PTA takes the position that it is not appropriate to issue an amended assessment. It could be considered to ensure that the taxpayer has possibilities to appeal, especially in view of flaws and uncertainties that could arise in the commencement period of implementation of the Directive. Under the Directive in its current form, the consolidated tax return could very well be considered merely to be a first ‘offer’ from the PTP to the PTA/TAs concerned.

Article 113 lays down, as stated in paragraph (25) of the explanatory memorandum, that powers will be conferred on the Commission to ensure uniform conditions for the implementation of this Directive as regards, amongst others, the form of the tax return and the consoli-
dated tax return as well as the required supporting documentation. Please note that paragraph (25) does not include giving the Commission a coordinating role on the application of the tax itself by, for instance, allowing it to issue interpretative rulings or other instruments that bind the Member State on the application and/or interpretation of the CCCTB rules. Some coordinating mechanism could be developed to avoid a difference in treatment by different Member States.

In conjunction with the reference to article 114, paragraph 3, we conclude that although a PTP is obliged to report errors in a consolidated tax return even if three years have elapsed since the filing date, no adjustment (positive or negative) will follow after that period.

Where the taxpayer does not file a tax return, the PTA may issue an assessment ‘within three months’ based on an estimate. This means that the PTA will have to issue such assessment within one year after the end of the tax year. In practice, the PTA is not likely to have sufficient information to make a realistic estimate. Taxpayers might, however, be tempted not to file a tax return in order to have more time to understand the system. The Directive does not seem to set out any provisions for the imposition of penalties.

Amended assessments and (dis)agreements
In the case of a single taxpayer, audits and assessments are governed by the laws of the Member State in which the single taxpayer resides. In case of a group, article 114 contains the rules for issuing an amended assessment. Generally speaking, the TAs have three years to issue such an assessment, six years in case of a deliberate or grossly negligent misstatement and even twelve years where the misstatement is the subject of criminal proceedings. Amendments are limited to the subject of the misstatement. No term applies if an amended assessment is issued based on article 123. A rule, determining that once an amended assessment has been issued no further amendments may be made unless based on facts which were not known or should not have been known by the tax administration, could be considered. The current wording allows for a piecemeal issuing of amended assessments, which is contrary to the principle of certainty of law (rechtszekerheid). The PTA is obliged to consult the TAs of other Member States prior to issuing an amended statement. A competent authority may request the PTA to issue an amended assessment. It is unclear whether this is limited to the consultation procedure described in article 114, paragraph 6 or whether it is meant as a general rule. The PTA may explicitly or implicitly refuse to do so. Article 123 deals with resolution of a conflict that may arise from such refusal: the offended Member State is allowed to take the dispute against the PTA to court, as if it were a taxpayer. Especially in the case of a partial refusal, this could mean that issues will be contested both ways before the same court: on one side by the taxpayer and on the other, by the offended Member State. Obviously there is still a great deal of distrust between Member States, since the alternative means could have been to allow that the PTA be the body to decide on the application of the Directive in individual cases, and have a coordination mechanism in place to deal with differences in opinion between Member States at a higher level.

Article 115 sets out what documents must be stored in a central database. The opinions issued by the competent authorities pursuant to article 119 are not mentioned. It would seem preferable to include such opinions in the database. From the wording, we conclude that the database may not contain information available to the PTA stemming from the period before the group opted for application of the Directive.

Article 116 sets out that the TAs of the Member States may, in ‘exceptional circumstances’, within six months of the NTO or a reorganization, decide by common agreement that a taxpayer other than the taxpayer designated by the group shall be the PTP. The question is, what are ‘exceptional circumstances’. Article 4 (6) (b) and (d) allows the group to ‘designate’ the PTP. It should, therefore, be noted that this exception only seems to apply to the situations mentioned in these provisions. The PTP does not appear to have the possibility to appeal against such decision of the TAs. According to the criteria set out in article 4 (6) a mere holding company could qualify as the PTP. Member States with many European holding companies, such as Luxembourg, could become the PTA of many groups. In situations where the operations of the group take place in other Member States, this results in a large administrative burden at the level of such PTA, likely without receiving a substantial share of the common tax
base under the formula of article 86. It could be considered to allow deviating from the rules of article 4 (6) upon request of the group, and upon approval by the TAs of the Member States concerned. An important benefit of the current proposal however is the simplicity of article 4 (6).

Article 117 sets out that each group member shall keep records and supporting documents in sufficient detail to ensure the proper implementation of the Directive and to allow audits to be carried out. The question arises, how the term ‘sufficient detail’ should be explained. It could, for example, be explained in accordance with the national law of (i) the Member State in which a group member is resident; or (ii) the Member State of the PTA. It is recommended that this be clarified in order to provide certainty to the taxpayers.

Article 118 deals with the providing of information to the TAs. Upon request of the PTA, the PTP shall provide all information relevant to the determination of the consolidated tax base or of the tax liability of any group member. This concerns the apportionment formula, which requires more (detailed) information than the calculation of the common base.

Article 119 provides for an advance ruling mechanism for certain transactions, allowing a taxpayer to request an opinion from the competent authority of the Member State in which it is resident. The competent authority shall take all possible steps to respond to the request within a reasonable time. This provision only requires the TAs to try to respond. Furthermore, the question arises as how to interpret ‘a reasonable time’. In practice, this can give rise to discrepancies in interpretation by the TAs of the various Member States. Provided that all relevant information is disclosed, an opinion issued by the competent authority shall be binding on it, unless the courts of the Member State of the PTA subsequently decide otherwise pursuant to article 123. Article 123 sets out that the TA of the Member State in which a group member is resident or established may challenge a decision of the PTA concerning the NTO or an amended assessment before the courts of the Member State of the PTA. Article 119 provides for an exception to the ‘one stop shop’ main rule; as we read it, the group deals directly with other TAs than the PTA. The question arises what the consequences will be if the PTA does not agree with the opinion issued by another TA. Article 123 sees to disagreement between Member States, but only on certain decisions, not including the issuing of an opinion. If the PTA issues an amended assessment the other TA may challenge the decision of the PTA under article 123, but if there is no decision the only thing left to the TA seems to be to request an audit on the basis of article 122, paragraph 1. Nevertheless, the exception formed by article 123 (and also article 122) to the ‘one stop shop’ rule results in uncertainty and complexity, and can be considered surprising in view of the following remark in paragraph 9 of Working Paper 61: ‘If the issuing of such administrative notices were left to individual national administrations, without coordination, then clearly the concept of a “common” base could soon disappear.’ Situations in which taxpayers directly deal with other TAs than the PTA, as is, for example, the case in articles 85 and 119, seem to result in uncertainty at the level of the taxpayer, while an issue is pending between Member States. It is recommended that the taxpayers do not bear the burden of disagreements between competent authorities of the Member States.

In the case of a request for an opinion concerning group members resident in two or more Member States, the TAs of those Member States must agree on a common opinion. The Directive does not mention a timeframe for such opinion. In practice, coming to such common opinion between Member States often takes a long time, again resulting in uncertainty at the level of the taxpayer.

Article 121 contains the secrecy clause for information exchanged between Member States under this Directive. Such information shall be kept secret in the receiving Member State in the same manner as under its domestic legislation. Generally, such information may be made available only in connection with tax assessments, control thereof and judicial proceedings involving tax assessments. However, such information may be disclosed during public hearings if the competent authority of the Member State supplying the information raises no objection. Paragraph 2 of article 121 states that the supplied information may also be used for other purposes if it could be used for similar purposes in the informing State. With respect to the aforementioned public hearings, the informing Member State seems to have much flexibility to decide whether information can be used, it does not seem limited by its national legislation nor does the taxpayer seem to have possibilities to appeal against a decision of the
Informing State. In view of the political sensitivity of the secrecy clause, it might be considered to limit the disclosure of information in public hearings.

**Article 122** Audits should be initiated and coordinated by the PTA, determining the scope and content jointly with the other TAs, but the authorities of any Member State in which a group member is subject to tax may request that an audit be initiated. An audit shall be conducted in accordance with the national legislation of the Member State in which it is carried out, subject to adjustments to ensure proper implementation of the Directive. The PTA shall compile the results of all audits. We understand that the competent authority in which a group member is resident will perform the audit at the level of that group member. Clarification could be given as to what adjustments to the national legislation are required in the various Member States to ensure proper implementation of the Directive.

**Article 124** sets out that taxpayers may appeal against certain acts: rejection of an NTO; a notice requesting disclosure of documents or information; an amended assessment; and an assessment on the failure to file a consolidated tax return.

**Article 125** sets out that disputes between taxpayers and TAs should first be dealt with by an administrative body which is competent to hear appeals at first instance according to the law of the Member State of the PTA. Paragraph 5 of article 125 states that if no decision is received by the PTP within a six-month period, the decision of the PTA shall be deemed to have been confirmed, which entitles the PTP to put the matter before the court, according to paragraph 6.

Hans Bakker and Imme Kam

**Chapter XVIII Final provisions**

**Article 127 Exercise of the delegation**

1. The power to adopt delegated acts referred to in Articles 2, 14, 34 and 42 shall be conferred on the Commission for an indeterminate period of time.

2. As soon as the Commission adopts a delegated act, it shall notify it to the Council.

3. The power to adopt delegated acts is conferred on the Commission subject to the conditions laid down in Articles 128, 129 and 130.

**Article 128 Revocation of the delegation**

1. The delegation of powers referred to in Articles 2, 14, 34 and 42 may be revoked at any time by the Council.

2. The decision of revocation shall put an end to the delegation of the powers specified in that decision. It shall take effect immediately or at a later date specified therein. It shall not affect the validity of the delegated acts already in force. It shall be published in the Official Journal of the European Union.

**Article 129 Objection to delegated acts**

1. The Council may object to a delegated act within a period of three months from the date of notification.

2. If, on the expiry of this period, the Council has not objected to the delegated act, it shall be published in the Official Journal of the European Union and shall enter into force on the date stated therein.

The delegated act may be published in the Official Journal of the European Union and enter into force before the expiry of that period if the Council has informed the Commission of its intention not to raise objections.

3. If the Council objects to a delegated act, it shall not enter into force. The Council shall state the reasons for objecting to the delegated act.

**Article 130 Informing the European Parliament**

The European Parliament shall be informed of the adoption of delegated acts by the Commission of any objection formulated to them, or the revocation of the delegation of powers by the Council.
Article 131 Committee
1. The Commission shall be assisted by a Committee. That committee shall be a committee within
the meaning of Regulation (EU) No 182/2011.1
2. Where reference is made to this paragraph, Article 5 of Regulation (EU) No 182/2011 shall
apply.

Article 132 Consultations on Article 87
The Committee established by Article 131 may also discuss the application of Article 87 in a given
case.

Article 133 Review
The Commission shall, five years after the entry into force of this Directive, review its application
and report to the Council on the operation of this Directive. The report shall in particular include
an analysis of the impact of the mechanism set up in Chapter XVI of this Directive on the distribu-
tion of the tax bases between the Member States.

Article 134 Transposition
1. Member States shall adopt and publish, by [date] at the latest, the laws, regulations and admin-
istrative provisions necessary to comply with this Directive. They shall forthwith communicate to
the Commission the text of those provisions and a correlation table between those provisions and
this Directive.
   They shall apply those provisions from […].
   When Member States adopt those provisions, they shall contain a reference to this Directive or
   shall be accompanied by such a reference on the occasion of their official publication.
2. Member States shall communicate to the Commission the text of the provisions of national
law which they adopt in the field covered by this Directive.

Article 135 Entry into force
This Directive shall enter into force on the [… ] day following that of its publication in the Official
Journal of the European Union.

Article 136 Addressees
This Directive is addressed to the Member States.
Done at Brussels,
For the Council The President

Comment
The main element of Chapter XVIII is the framework for delegated and implementing acts. As is
true of domestic legislation, legislation at European level can also not cover all eventualities. It is
common for legislative powers to be delegated to a variety of bodies. In this respect, the
Treaty on the Functioning of the European Union (TFEU) distinguishes between legislative,
delegated and implementing acts. The legislative act must contain all the essential elements.
On the basis of Article 290 TFEU, a legislative act can empower the Commission to adopt
delegated acts. Such delegation of powers may only take place in respect of non-essential
elements of a legislative act. The delegation of powers on the basis of Article 291 TFEU goes
one step further. In principle, the Member States are responsible for the implementation of
legislative acts. However, insofar as uniform conditions are required for the implementation,
implementing powers may be delegated to the Commission (and in exceptional cases, to the
Council). The power of control remains with a committee that is staffed by representatives of
the Member States and chaired by a Commission representative. Regulation (EU) No. 182/2011
lays down the rules and general principles concerning the mechanisms for control by Member
States of the Commission’s exercise of such implementing powers.

The following acts are delegated to the Commission in accordance with Article 290 TFEU:
– to adapt Annexes to take into account the changes to the laws of the Member States regarding the relevant company forms and corporate taxes;
– to update the list of non-deductible taxes;
– to lay down rules on the definition of legal and economic ownership in relation to leased assets, the calculation of the capital and interest elements of the leasing payments and of the depreciation base of a leased asset.

The following acts are delegated to the Commission in accordance with Article 291 TFEU, on the basis of which the Commission will be assisted by a committee under the examination procedure of article 5 of Regulation (EU) No 182/2011:
– annual adoption of the list of third country company forms which meet the requirements;
– laying down rules on the calculation of the labour, asset and sales factors, the allocation of employees and payroll, assets and sales to the respective factor as well as the valuation of assets for the asset factor;
– the adoption of a standard form of the notice to opt for the adoption of rules on electronic filing, on the form of the tax return, on the form of the consolidated tax return and on the required supporting documentation;
– discussions on the safeguard clause in respect of the apportionment of the consolidated tax base.

We can question whether a distinction can truly be drawn between delegated acts and implementing acts. Measures referred to under both mechanisms vary from matters of procedures to matters of a more substantive nature. As to the latter, some tax scholars might argue that adding detail and providing guidance in relation to the definition of legal and economic ownership constitutes an essential element.

The recently introduced framework for delegated and implementing acts is too new to have gained much experience. As for delegated acts, initial practice seems to demonstrate that the Commission will only enjoy limited discretion in the adoption of delegated acts, as they have to remain within the boundaries as set in the legislative act. Moreover, under Article 290(2) TFEU, the Council will have quite strong rights of supervision over delegated acts adopted by the Commission. For implementing acts, when the implementing measure relates to taxation and no opinion can be found by a qualified majority of the committee, the Commission may submit the act to an appeal committee (or within two months, an amended draft to the original committee). The appeal committee again has to deliver its opinion by qualified majority. If no opinion can be found, the Commission may adopt the draft act. The outcome seems to be that effectively, the Commission can adopt an implementing act unless it is opposed by a qualified majority of the committee.

Peter Adriaansen

Annexes

Annex I

(c) companies under Belgian law known as ‘société anonyme’/’naamloze vennootschap’, ‘société

² OJ L 294, 10.11.2001, p. 22.
en commandite par actions’/‘commanditaire vennootschap op aandelen’, ‘société privée à responsabilité limitée’/‘besloten vennootschap met beperkte aansprakelijkheid’/‘société coopérative à responsabilité limitée’/‘coöperatieve vennootschap met beperkte aansprakelijkheid’, ‘société coopérative à responsabilité illimitée’/‘coöperatieve vennootschap met onbeperkte aansprakelijkheid’, ‘société en nom collectif’/‘vennootschap onder firma’, ‘société en commandite simple’/‘gewone commanditaire vennootschap’, public undertakings which have adopted one of the abovementioned legal forms, and other companies constituted under Belgian law subject to the Belgian Corporate Tax;

(d) companies under Bulgarian law known as: ‘събирателното дружество’, ‘командитното дружество’, ‘дружеството с ограничена отговорност’, ‘акционерното дружество’, ‘дружеството с акции’, ‘кооперации’, ‘кооперативни съюзи’, ‘държавни предприятия’ constituted under Bulgarian law and carrying on commercial activities;

(e) companies under Czech law known as: ‘akciová společnost’, ‘společnost s ručením omezeným’, ‘veřejná obchodní společnost’, ‘komanditní společnost’, ‘družstvo’;

(f) companies under Danish law known as ‘aktieselskab’ and ‘anpartsselskab’. Other companies subject to tax under the Corporation Tax Act, in so far as their taxable income is calculated and taxed in accordance with the general tax legislation rules applicable to ‘aktieselskaber’;

(g) companies under German law known as ‘Aktiengesellschaft’, ‘Kommanditgesellschaft auf Aktien’, ‘Gesellschaft mit beschränkter Haftung’, ‘Versicherungsverein auf Gegenseitigkeit’, ‘Erwerbs-und Wirtschaftsgenossenschaft’, ‘Betriebe gewerblicher Art von juristischen Personen des öffentlichen Rechts’, and other companies constituted under German law subject to German corporate tax;

(h) companies under Estonian law known as: ‘täisühing’, ‘usaldusühing’, ‘osaühing’, ‘aktsiaselts’, ‘tulundusühiskond’;

(i) companies under Greek law known as ‘αυτόνομη εταιρεία’, ‘εταιρεία περιορισμένης ευθύνης’ (Ε.Π.Ε.);

(j) companies under Spanish law known as ‘sociedad anónima’, ‘sociedad comanditaria por acciones’, ‘sociedad de responsabilidad limitada’, and those public law bodies which operate under private law;

(k) companies under French law known as ‘société anonyme’, ‘société en commandite par actions’, ‘société à responsabilité limitée’, ‘sociétés par actions simplifiées’, ‘sociétés d’assurances mutuelles’, ‘caisses d’épargne et de prévoyance’, ‘sociétés civiles’ which are automatically subject to corporation tax, ‘coopératives’, ‘unions de coopératives’, industrial and commercial public establishments and undertakings, and other companies constituted under French law subject to the French Corporate Tax;

(l) companies incorporated or existing under Irish laws, bodies registered under the Industrial and Provident Societies Act, building societies incorporated under the Building Societies Acts and trustee savings banks within the meaning of the Trustee Savings Banks Act, 1989;

(m) companies under Italian law known as ‘società per azioni’, ‘società in accomandita per azioni’, ‘società a responsabilità limitata’, ‘società cooperative’, ‘società di mutua assicurazione’, and private and public entities whose activity is wholly or principally commercial;

(n) under Cypriot law: ‘εταιρεία’ as defined in the Income Tax laws;

(o) companies under Latvian law known as: ‘akciju sabiedrība’, ‘sabiedrība ar ierobežotu atbildību’;

(p) companies incorporated under the law of Lithuania;


(s) companies under Maltese law known as: ‘Kumpaniji ta’ Responsabilita Limitata’, ‘socijetoj en commandite li l-kapital taghhom maqsum f’azzjonijiet’;
(t) companies under Dutch law known as ‘naamloze vennootschap’, ‘besloten vennootschap met beperkte aansprakelijkheid’, ‘Open commanditaire vennootschap’, ‘Coöperatie’, ‘onderlinge waarborgmaatschappij’, ‘Fonds voor gemene rekening’, ‘vereniging op coöperatieve grondslag’ and ‘vereniging welke op onderlinge grondslag als verzekeraar of kredietinstelling optreedt’, and other companies constituted under Dutch law subject to the Dutch Corporate Tax;
(v) companies under Polish law known as: ‘spółka akcyjna’, ‘spółka z ograniczoną odpowiedzialnością’, ‘spółdzielnia’, ‘przedsiebiorstwo państwowe’;
(w) commercial companies or civil law companies having a commercial form, cooperatives and public undertakings incorporated in accordance with Portuguese law;
(x) companies under Romanian law known as: ‘societăți pe acțiuni’, ‘societăți în comandită pe acțiuni’, ‘societăți cu răspundere limitată’;
(y) companies under Slovak law known as: ‘delsnà družba’, ‘komanditnà delniška družba’, ‘komanditna družba’, ‘družba z omejeno odgovornostjo’, ‘družba z neomejeno odgovornostjo’;
(z) companies under Swedish law known as: ‘aktiebolag’, ‘aktiebolag’, ‘sveriges försäkringsbolag’;
(aa) companies under Finnish law known as ‘osakeyhtiö’/’aktiebolag’, ‘osuuskunta’/’andelslag’, ‘säästöpankki’/’sparbank’ and ‘vakuutusyhtiö’/’försäkringsbolag’;
(bb) companies under Polish law known as ‘spółka akcyjna’, ‘spółka z ograniczoną odpowiedzialnością’, ‘spółdzielnia’, ‘przedsiebiorstwo państwowe’.

 Annex II

Belgien / Belgique
impôt des sociétés/vennootschapsbelasting
........
.............
Česká republika
Daň z příjmů právnických osob
Danmark
selskabsskat
Deutschland
Körperschaftsteuer
Eesti
Tulumaks
Éire/Ireland
Corporation Tax
Ελλάδα
Φορος εισοδηματος υομικων προωπων κερδοσκοπικων χαρακτηρα
España
Impuesto sobre sociedades
France
Impôt sur les sociétés
Italia
Imposta sul reddito delle società
Cyprus/Kibris
Φορος Εισοδηματος
Latvija
uzņēmumu ienākuma nodoklis
Lietuva
pelno mokestis
Luxembourg
impôt sur le revenu des collectivités
Magyarország
Társasági adó
Malta
Taxxa fuq l-income
Nederland
vennootschapsbelasting
Österreich
Körperschaftsteuer
Polska
Podatek dochodowy od osób prawnych
Portugal
imposto sobre o rendimento das pessoas colectivas
România
impozit pe profit
Slovenija
Davek od dobi‘ka pravnih oseb
Slovensko
Daň z príjmov právnických osôb
Suomi/Finland
yhteisöjen tulovero/inkomstskatten för samfund
Sverige
statlig inkomstskatt
United Kingdom
Corporation Tax

Annex III
List of non-deductible taxes under Article 14
Belgien/Belgique
Droits d’enregistrement – Registratiereschten
......
None
Česká republika
None
Danmark
Registreringsafgift af motorkøretøjer
Kommunal grundskyld
Kulbrinteskat
Deutschland
Grunderwerbsteuer
Grundsteuer B
Gewerbesteuerumlage
Versicherungsteuer
Eesti
None
Éire/Ireland
Stamp Duties
Vehicle Registration Tax
Residential Property Tax
Ελλάδα
Φορος Μεταβασης Ακινητων
España
Impuesto sobre Bienes Inmuebles (IBI) / Recargo sobre el IBI
Impuesto sobre Transmisiones Patrimoniales y Actos Jurídicos Documentados
France
Foncier bati
Taxe professionnelle
Taxe sur les salaires
Taxe d’habitation
Italia
Imposta comunale sugli immobili (ICI) – Fabbricati
Imposta regionale sulle attività produttive (IRAP) – (employers’ split)
Κοινός/Κύπρος
Taxes on Holding Gains
Latvija
None
Lietuva
None
Luxembourg
Taxe d’abonnement sur les titres de société
Impôt commercial communal
Magyarország
Különadó
Helyi iparuzésiadó
Malta
Taxes on Holding Gains
Nederland
Overdrachtsbelasting
Overige productgebonden belastingen neg – (energy split)
Österreich
Kommunalsteuer
Polska
Podatek od nieruchomości
Portugal
None
România
None
Slovenija
Davek na izplačane plače
Slovensko
None
Suomi/Finland
None
Sverige
Fastighetsskatt
Allmän löneavgift
Särskild löneskatt
United Kingdom
National Non-Domestic Rates from Businesses
Capital Levies

**Legislative financial statement for proposals**

1 FRAMEWORK OF THE PROPOSAL/INITIATIVE
1.1 Title of the proposal/initiative
1.2 Policy area(s) concerned in the ABM/ABB structure
1.3 Nature of the proposal/initiative
1.4 Objective(s)
1.5 Grounds for the proposal/initiative
1.6 Duration and financial impact
1.7 Management method(s) envisaged
2 MANAGEMENT MEASURES
2.1 Monitoring and reporting rules
2.2 Management and control system
2.3 Measures to prevent fraud and irregularities
3 ESTIMATED FINANCIAL IMPACT OF THE PROPOSAL/INITIATIVE
3.1 Heading(s) of the multiannual financial framework and expenditure budget line(s) affected
3.2 Estimated impact on expenditure
3.2.1 Summary of estimated impact on expenditure
3.2.2 Estimated impact on operational appropriations
3.2.3 Estimated impact on appropriations of an administrative nature
3.2.4 Compatibility with the current multiannual financial framework
3.2.5 Third-party participation in financing
3.3 Estimated impact on revenue
   Tables not included


The Commission has considered the impact of the various policy options in view of the barriers which currently exist for (multinational) enterprises operating in the European Union. The results of this assessment are laid down in an impact assessment. A CCCTB will result in roughly similar tax base for multinational enterprises as compared to the status quo. Furthermore, the compliance burdens for multinational enterprises will decrease. The consequences of the various policy options on tax revenues for Member States are not considered, as these depend on policy choices of Member States with regard to possible adaptations of the mix of the various tax instruments or applied tax rates.

European Commission, 21 March 2011, no. com 2011/316

Commission staff working paper summary of the impact assessment

Accompanying document to the Proposal for a COUNCIL DIRECTIVE on a Common Consolidated Corporate Tax Base (CCCTB) [COM(2011) 121]
[SEC(2011) 315]

Problem definition

Globalisation has reshaped the economic landscape. Not only the geography of production, but also the internal organization of firms operating in international markets has dramatically changed. The framework of steadily progressing market integration changes radically when it comes to corporate taxation. With 27 different tax systems that co-exist and often clash, the EU market remains indeed highly fragmented. This situation places the EU at a significant disadvantage vis-à-vis its major trading partners, the United States and Japan, each being perceived as one single market by businesses.

Firms currently operate through schemes structured to accommodate increased mobility of capital and frequent cross-border transactions between associated companies. Consequently, concepts defined for tax purposes, such as source and residence, traditionally used to address the needs of relatively closed economies, often prove inappropriate to tackle the challenges of commercial activity within an integrated market. Specifically, the coexistence of heterogeneous, frequently changing tax rules represents an obstacle for businesses competing in
international markets. Further, national tax systems become increasingly vulnerable to tax avoidance schemes. In fact, income shifting and treaty shopping are naturally facilitated in a context of high mobility of productive factors.

Against this background, a number of tax obstacles remain for companies with cross-border operations in the EU, namely:

I. Additional compliance costs, which arise from compliance with different national tax systems and with transfer pricing rules. According to evidence reported in the Company Tax Study published by the Commission in 2001, tax related compliance costs amount to roughly 3% of the corporate income tax revenues. In the context of the EU27, this could be translated into an average figure of about €10 billion for the period 2008 - 2009.

II. Double taxation, which takes place when comparable taxes are imposed on the same income in two or more states.

III. Over-taxation, which occurs when cross-border activities create tax liabilities that would not occur in a purely domestic context (e.g. associated companies of different Member States or their permanent establishments are not entitled to share losses, whereas loss consolidation for companies established only in one Member State reduces their taxable profits and tax burden).

2 Analysis of subsidiarity

The current framework with 27 different national corporate tax systems impedes the proper functioning of the Internal market. Member States cannot provide a comprehensive solution to this problem. Non-coordinated action – planned and implemented by each Member State individually – would replicate the current situation, as taxpayers would still need to deal with as many administrations as the number of jurisdictions in which they are liable to tax.

Community action is necessary in view of establishing a juridical framework with common rules. The Commission has taken the initiative having in mind that, under the principle of subsidiarity, Member States retain sovereignty in setting their corporate tax rates. Therefore, they are free to determine the desired size and the composition of their tax revenues.

3 Objectives of EU initiative

The specific policy objectives of the EU initiative are to eliminate the remaining tax obstacles in the Internal market outlined above, that is additional compliance costs related to international activity, as well as instances of double taxation and over-taxation. As a result, a general objective of improving economic efficiency in the allocation of productive capital in the EU could be attained by means of reduced tax distortions to investment decisions and increased opportunities for cross-border investments. As such, the envisaged improvement in the simplicity and efficiency of the corporate income tax system in the EU can significantly contribute to achieving the objectives of the EU2020 strategy, and to strengthening the Internal market, in line with the initiatives advocated in the Single Market Act.

The operational objective is to establish a common set of rules to calculate the taxable base for the relevant companies in the EU.

It should be stressed that the effects on the size and the distribution of corporate taxable bases across the EU are not an intended aim of the policy initiative per se. No objectives are therefore defined in terms of revenue distribution or revenue neutrality for MS.

4 Policy options

The report considers four main policy scenarios, which are compared with the ‘no action’ or status-quo scenario (option 1):

• The adoption of an optional Common Corporate Tax Base (CCTB), i.e. the replacement, for the relevant companies, of the 27 different company tax codes by a common tax base, calculated using a single set of rules (option 2).

• The compulsory introduction of a Common Corporate Tax Base (CCTB) for all EU-based companies (option 3).

• Under an optional Common Consolidated Corporate Tax Base (CCCTB) companies could opt for a
common (e.g., calculated using a single set of tax rules) EU-wide consolidated tax base that would replace the current 27 different company tax codes and the separate accounting mechanism (option 4).

- The same rules would be obligatory for all EU-based companies under a compulsory Common Consolidated Tax Base (CCCTB) (option 5).

Under all possible options, common rules would be established only for the calculation of the tax bases, whereas Member States would be left with fiscal sovereignty in deciding the applicable tax rates.

5 **Assessment of impacts**

5.1 *Impact on the size and on the distribution of the tax base*

The policy options entail changes in the size and the cross-country distribution of the corporate tax bases that is worth quantifying, although such effects are not objectives per se of the tax reforms under analysis. Importantly, no general conclusions should be drawn on the final effect on revenues or on the budgetary position of the different MS, as these will ultimately depend on national policy choices with regard to possible adaptations of the mix of different tax instruments or applied tax rates.

The findings indicate that the introduction of the common tax base provisions unrelated to cross-border loss consolidation (CCTB) could lead on average and for most EU-based companies to broader tax bases than the current ones. However, the magnitude of this increase seems to depend essentially on the depreciation rules applied. In any case, the common tax base would reduce the current substantial variation in tax bases across European countries.

The CCCTB provisions would allow for cross-border consolidation of profits and losses. Calculations on a sample of EU multinational groups based on the Amadeus and ORBIS databases show that, on average every year approximately 50% of non-financial and 17% of financial multinational groups in the respective samples could benefit from immediate cross-border loss compensation. Weighting the separate results for the different sectors indicates that on average for the groups involved the taxable base under the CCCTB scenario would be around 3% lower than in the status-quo scenario.

Under the CCCTB, the question arises on how the overall tax base should be divided among the Member States in which the multinational group operates, and thus requires the definition of ad hoc apportionment mechanisms. Using data from financial accounts to proxy for taxable profits of multinational groups shows that the formula with employee costs, assets and sales by destination equally weighted would lead to increases in the bases mostly in the MS in Central and Eastern Europe, as well as in Germany, Spain, France, Greece and Italy. Survey results indicate that changing the weighting of the apportionment factors has little effect on the relative distribution of the tax base between countries.

5.2 *Impact on compliance costs*

According to survey evidence, the main corporate compliance cost drivers for multinational enterprises are directly or indirectly related to transfer pricing tasks (transfer pricing documentation, clearances and rulings and mutual agreement procedures). Moreover, the compliance burden due to transfer pricing has been increasing over time, mainly as a result of two factors: (i) more demanding documentation requirements from tax authorities accompanied by tax authority reviews; (ii) adjustments and changes of the type and scope of business operations around the world.

According to a study commissioned to Deloitte, the CCCTB is expected to translate into substantial savings in compliance time and outlays in the case of a multinational setting up a new subsidiary in a different Member State. On average, the tax experts participating in the study

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1 Overall, in the sample used, the combined effect of the new tax base provisions unrelated to consolidation (which tend to broaden the tax base) and the introduction of immediate cross-border loss consolidation (which tend to shrink it) realised in the CCCTB scenarios tends to keep the aggregate tax bases roughly constant compared to the current ones (for the companies concerned).
2 Ernst & Young Transfer Pricing Survey.
estimated that a large enterprise spends over €140,000 (0.23% of turnover) in tax related expenditure to open a new subsidiary in another MS. The CCCTB will reduce these costs by €87,000 or 62%. The savings for a medium sized enterprise are even more significant, as costs are expected to drop from €128,000 (0.55% of turnover) to €42,000 or a decrease of 67%. Additional evidence gathered from a sample of existing European multinationals (PWC study) points to more moderate but still significant reduction in the compliance burden for recurring tax related tasks. The savings expected from the introduction of the CCCTB would amount to 8 percentage points of the compliance time.

5.3 Economy wide impacts

The CGE model CORTAX is used to assess the economy-wide impacts of the different reforms. The model, conceived to simulate tax policy changes for the EU Member States, has been extended and refined for the purpose of this impact assessment. However, like any general equilibrium model, CORTAX includes simplifying assumptions and specifications that are not undisputed, and cannot take away the uncertainty about the strength of certain behavioural effects of tax policies. More importantly, CORTAX does not capture the long run dynamic gains from further integration in the Internal Market, e.g. in terms of an increase in the number of internationally active firms. The removal of cross-border tax barriers is expected to translate into reduced distortions in the allocation of capital, as it will increase the substitutability between domestic and cross-border investment, on the one hand, and enhance the attractiveness of the EU as whole for multinational investors, on the other.

The increased allocative efficiency is expected to translate into productivity and employment gains, stemming also from the economies of scale that can be exploited in the larger market.

The four different policy options – optional CCTB, compulsory CCTB, optional CCCTB and compulsory CCCTB – are compared to the status quo scenario. In the optional scenarios it is assumed that all multinationals, but no domestic companies, opt for the alternative tax systems, whereas in the compulsory scenario also domestic companies need to apply the new tax provisions. This assumption might lead to an underestimation of the welfare gains in the optional scenarios as it can be expected that in practice multinational firms would opt in the new system only if that would not lead to lower net profits than dealing with the different national tax systems. In all scenarios it is assumed that corporate tax revenues are kept constant ex-ante adapting the tax rate, so that the government budget is balanced before companies react to the new policy environment.

The important economic mechanisms in the CGE analysis of the CCTB is the trade-off between a low effective marginal tax rate (result of a narrow base and high statutory tax rate), which minimises distortions in investment, and a low statutory corporate tax rate (coupled with a broad base), which reduces multinational profit shifting to outside locations and improves the attractiveness of a location in the case of discrete investment choices. Base-broadening implied by the new definition of the common tax base, and the consequent rate reduction are found to decrease aggregate welfare in the EU.

On the other hand, the main positive effect of the CCTB reform stems from the assumed reduction in compliance costs. All in all, a compulsory CCTB leaves welfare at a European level nearly constant while the introduction of a CCTB optional for multinationals renders slight welfare gains. Compared to the CCTB, the welfare effects of the CCCTB options are more favourable under any of the analysed scenarios. The overall final impact is a small net positive welfare gain of around 0.02% of GDP in aggregated terms for the EU, which amount to roughly €2.4 billion (2009 figure). Disentangling the effects of the different elements of the reforms shows that:

- The lion’s share of the positive economic impact of consolidation and formula apportionment is due to lower compliance costs.

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1 The extensions concern the inclusion of (i) tax havens, to capture the opportunity for profit shifting outside the EU, (ii) loss probabilities, to precisely quantify the economic effects of loss consolidation, and (iii) discrete location choices, to model the infra-marginal choices of firms on where to invest, preliminary to the decision on how much to invest.

2 In the model a policy of base-broadening cum rate-reduction results in welfare gains when applied separately by individual countries, and particularly by high-tax countries that suffer from profit shifting.
• The move from separate accounting to formula apportionment exerts a negligible effect on GDP and welfare. It is the result of different offsetting effects: fewer incentives to shift profits and capital from high tax countries, but additional distortions in the allocation of formula factors to low tax economies.

• Loss consolidation tends to shrink the tax bases. Hence, given the model assumptions, certain increase in corporate tax rates may be required to balance the government budget.

  The combination of a lower tax burden via loss consolidation and a higher tax burden due to higher rates may raise overall the cost of capital. Accordingly, investment slightly falls but employment expands due to lower labour costs. On balance, GDP slightly falls, whereas the net effect on welfare is negligible.

6 Comparison of options

The removal of all the three types of identified corporate tax obstacles – possible under the CCCTB policy options – would allow business to make sounder economic choices thus improving overall economic efficiency in the EU. On the basis of the quantified economic impacts, the optional CCCTB and the compulsory CCCTB are preferred to the alternative options given the savings in compliance costs they can generate. However, the macroeconomic evidence points to the optional CCCTB as the overall preferred policy option of the scenarios analysed.

The reforms under analysis are potentially associated with important dynamic effects in the long run. The reduction in uncertainty and in the costs (actual and perceived) that firms operating in multiple jurisdictions incur is the main channel through which these effects are expected to materialize. Ultimately, this will translate into increased cross border investment.

However, a generalized implementation of such policy at the European level reduces the beneficial effects of lower corporate tax rates. In fact, the comparative location advantage of a country does not improve if all other Member States reduce their tax rate too. Only location choices vis-à-vis third countries will be affected. On balance, a multilateral policy of base broadening and rate reduction is therefore less likely to be welfare improving than a unilateral policy within the EU, stemming both from further expansion of European and foreign multinationals and from de novo investment of purely domestic firms into other Member States. By the same token, to the extent that the current fragmented landscape of corporate tax systems acts as a barrier to entry into international markets, small and medium sized enterprises (SMEs) might be particularly advantaged by the level playing field created by the reforms under analysis.

The elimination of additional compliance costs associated with having to deal with different tax rules and the introduction of the ‘one-stop shop’ principle in tax administration is likely to enhance SMEs’ capacity to expand cross-border.

7 Monitoring and evaluation

The proposed policy intervention will exert effects on a number of variables that should be monitored. At the microeconomic level, the effects of the policy options on firms’ tax related compliance costs and on their investment behaviour across national borders should be assessed. To overcome the well-known difficulties in obtaining reliable estimates of actual and perceived compliance costs, ad hoc surveys should be designed, and particular attention devoted to the representativeness of the selected samples. Propensity to expand abroad by SMEs might be particularly revealing on the expected long term impacts of the policy options.

Such effects can be gauged both by means of surveys among the relevant companies and by analysing observed changes in actual investment choices.

At the macroeconomic level, consistent with the general objectives of improving the allocation of productive capital in the EU, evidence should be gathered on foreign direct investment flows directed to the EU and among EU countries.

The evaluation of the consequences of the application of the legislative measure could take place five years after the entry into force of the legislative measures implementing the Directive. The Commission could then submit to the European Parliament and the Council a report on the technical functioning of the Directive.
The content of such a report would vary according to the scope of the Directive as finally agreed in the Council.

**Comment**

The impact assessment accompanying the proposal for the Council Directive on the CCCTB, (the Impact Assessment) considers the impact of the various policy options on tax base, double taxation and the current compliance burdens. The Impact Assessment compares the various policy options (optional or compulsory common corporate tax base, optional or compulsory common consolidated corporate tax base), as well as the status quo. A CCCTB will result in (i) a roughly similar tax base, and (ii) a lower compliance burden. From a macroeconomic point of view, the investments in and the GDP of Member States are expected to decrease. Welfare and employment are expected to slightly improve.

In carrying out the Impact Assessment, the Commission used, amongst others, the data available in the ORBIS and Amadeus databases. In addition, the Commission conducted its own data study on the basis of these data. One of the most delicate assessments in this respect relates to the expected impact on the distribution of the total consolidated tax base between Member States (table 3 of the Impact Assessment). This is a rather politically sensitive topic – to say the least. Unfortunately, neither the Impact Assessment nor the Annexes shed much light on the applied methodology. This is unfortunate, since table 3 seems to display some remarkable figures. For example, it is estimated that over 20.3% of the current tax base is attributable to the Nordic Member States. Also, from some assessments – for instance, the impact of a CCCTB on the tax base – it is not immediately clear whether the Commission has derived its conclusion directly from the data gathered from the databases, or whether it has modified this data to reach its conclusion.

According to the summary of the Impact Assessment, the rules for a common base lead to an increase of the average tax base in the EU. It can be derived from the Impact Assessment itself, that simulations which were run for a standardised company for a period of ten years, illustrate an increase of value of such tax bases of approximately 1% - 6% under a CCTB. The expected increase of tax base is, to a great extent, compensated by a decrease of such tax base as a result of the consolidation, i.e. an average decrease of the tax base by 2.8%. It is not clear from the Impact Assessment what effect this decrease will have on the value of the tax base. Assuming that the cash value of this decrease is equal to the reduction of the average tax base, this advantage should be roughly similar to the average of the increase of the value of tax base under the CCTB (i.e. 3.5%).

Nevertheless, the foregoing, the impact of a C(C)CTB on the value of the tax base does not mean much in respect of the effects of the C(C)CTB on the amount of tax revenues for Member States and the amount of tax actually due by multinational enterprises, as these depend on the actual rates applied by the various Member States to the tax base attributed pursuant to the formula. This is also indicated in the Impact Assessment. However, the question remains how Member States are to determine whether the CCCTB Directive suits their purpose. A reduction of tax base as a result of the applied formula will decrease tax revenue, whereas an increase of the corporate tax rate to even that out would disadvantage competitiveness. The one thing that is certain, is that even with all research material currently available, it is very difficult for each Member State to assess the impact of the introduction of a CCCTB.

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