Comments on document CCCTB\WP\039

Common Consolidated Corporate Tax Base Working Group
– Issues related to Business Reorganisations –

Introduction

The UNICE Task Force on CCCTB is pleased to comment on the important issue of business reorganisations dealt with by the Commission and the Member States ("MS"). The comments refer in particular to the Commission's Working Paper on the same topic (WP039; hereinafter referred to as "Paper").

As usual, the positions taken below may be subject to revision as other areas of the CCCTB are explored.

General Remarks

As repeatedly emphasized by the Commission and also outlined in the first Communication on CCCTB in May 2006, CCCTB shall be optional. We strongly support that approach and would like to stress once again that for the CCCTB to be successful, it is of utmost importance to design a highly competitive and attractive set of tax rules compared to existing domestic rules. Otherwise CCCTB might remain an option which will not facilitate in reaching the important objectives set out in the Lisbon agenda. Considering the rapid and continuous changes in today's economy, attractive and internationally competitive tax rules for business reorganisations which do not hamper economically driven restructurings play an instrumental role in the design of the CCCTB.

For the design of business reorganisation rules under the CCCTB, the Merger Directive - which also under CCCTB continues to be legally binding - could be used as a reference point. However, the Merger Directive should be considered only as a minimum standard. CCCTB rules should offer a broader scope for tax neutral transactions and be even more flexible in order to eliminate tax obstacles to further enhance competitiveness of business within the EU. Therefore, all internal restructurings involving transfer of business assets or shares should be covered, including any kind of transformations such as transfers of the registered office and liquidations. In our opinion, the territorial scope of the CCCTB business reorganisation rules should be global and not be limited to transactions between EU entities only. Such an international approach could even further enhance competitiveness of the EU as economic area.

We fully agree with the Commission that tax consolidation is crucial to the success of CCCTB. The basic concept of consolidation, i.e. the elimination of all intra-group transactions for tax purposes, including business reorganisations, between members of the consolidated group needs to be maintained. Exceptions to this overriding principle should only be considered as last resort. We therefore support the Commission's approach to further analyse how to account for business reorganisations under the sharing mechanism of the tax base instead of treating certain business reorganisations separately from consolidation.

We understand and recognize Member States' interest to avoid the loss of tax revenue due to cross border business reorganizations. We acknowledge that MS may have a legitimate right

to tax hidden reserves built up under their tax sovereignty. However, this right to tax must in any case be exercised in compliance with the basic freedoms of the EC Treaty. In other words, exit taxation regarding intra-group business reorganisations needs, as a minimum, to be deferred until actual sale to third party or disposal of the assets in question. Further, to Member States' legitimate wish to safeguard taxation of hidden reserves, we see no or little room for other tax avoidance provisions, in particular CFC rules, within the consolidated group. Based on ECJ decision on Cadbury Schweppes, it is not abusive to do business in EU MS with lower levels of taxation unless the activity constitutes a *wholly* artificial arrangement. Therefore, in line with the ECJ we are against any anti-avoidance measures which go beyond what is required to retain Member States right to hidden reserves when they lose right to tax.

Notwithstanding the above, any discussion on specific anti-avoidance rules concerning business reorganisation at this stage should be avoided. At this moment it is important to create a simple, attractive system also for business reorganizations. Once such a system, including sharing mechanism of the tax base, is in principle set up, then it could be analyzed if and to what extent there is a need for anti-avoidance rules.

Comments on the scenarios proposed in the Commission's paper

Following the Paper, hereinafter we briefly comment on the following three scenarios for business reorganization:

1. Entities all covered by CCCTB rules and included in a consolidated group.

2. Entities covered by CCCTB rules but not included in a consolidated group.

3. Some entities covered by CCCTB rules and other entities which are not.

Scenario 1: Entities all covered by CCCTB rules and included in a consolidated group

As mentioned above, under tax consolidation rules all intra group transactions should be irrelevant for tax purposes, i.e. taxable income of the group should remain unchanged. This principle should also apply to any kind of internal business reorganisation, irrespective of whether a permanent establishment remains in the country of the transferring entity. We would like to stress that it is important to maintain the consolidation principle. If significant exceptions from consolidation were introduced under CCCTB business reorganisation rules, consolidation itself might be questioned not only from a conceptual but also from a technical and administrative point of view. Any deviation from consolidation will definitely make the CCCTB system more complicated and thus less attractive.

Given the existing differences in the level of taxation of MS, we therefore strongly support the Commission's proposal in the Paper to consider the impact of business reorganisations under the sharing mechanism. Conceptually, in our opinion there is no alternative to this approach. We see, however, also the practical and political difficulties in finding a formulary apportionment which would adequately account for the impact on MS losing economic substance due to business reorganisations as the location of assets, facilities and labour will most likely affect the MS share of the common tax base under the sharing mechanism. Consequently, it might be difficult to safeguard a fair compensation for MS which lose tax revenue as a consequence of transfer of hidden reserves to other MS in the course of cross

border reorganisations. With respect to hidden reserves which have been built up prior to the entry in the consolidated group this issue might be even more problematic. If a solution under formulary apportionment would not be agreeable, the CCCTB rules should in any case provide for tax neutrality of any internal restructuring measures without creating excessive administrative obligations for business (see further comments under Scenario 2 below).

CCCTB rules should provide for a tax neutral carry-over of historical CCCTB tax values of transferred assets, provisions or reserves and the take-over of existing losses by the acquiring entity. There should be no restrictions on the carry-over of tax book values, in particular regarding loss utilization, provided that the transactions concerned are not purely artificial but have some kind of business reason. In any case, we recommend discussing anti-abuse provisions separately at a later stage.

Scenario 2: Entities covered by CCCTB rules but not included in a consolidated group

We understand that under such scenario the Commission addresses both business reorganizations between (i) entities of the same group for which CCCTB rules apply but which are not consolidated and (ii) entities of different CCCTB groups. In both cases exclusively CCCTB rules for business reorganizations without consolidation rules would apply.

In order to be attractive and competitive CCCTB business reorganisation rules should - as mentioned above – offer a broader scope for tax neutral reorganizations than the Merger Directive which should set the minimum standard only. For example, the rules should provide for a tax neutral transfer of seat for entities other than the European Company. Further, tax neutrality for transfer of assets should not be restricted to cases where a permanent establishment remains in the transferring MS. Immediate taxation of hidden reserves should be avoided also for transactions between EU entities which do not fulfil the permanent establishment requirement in order to comply with basic freedoms of the EC Treaty. Under the Merger Directive, even in cases where a permanent establishment remains, taxation of certain assets such as participation and intangibles (in particular goodwill) may not be avoided as these assets - due to the reorganisation (e.g. cross border merger) - may no longer be attributed to the remaining permanent establishment.

Tax neutrality for cases where no permanent establishment remains in the transferring MS or where assets may no longer be attributed to a remaining permanent establishment could be achieved in the following two ways:

(i) Tax deferral of any capital gain upon transfer until actual disposal of assets to a third party without creating excessive administrative burden for business.

(ii) Pro rata taxation of hidden reserves realized (due to the transfer) in the transferring MS and corresponding depreciation of the additional step up in value in the receiving MS over the useful of the transferred assets. This, of course, would require that the receiving MS is obliged to take over the value of the assets as assessed by the transferring MS upon transfer. For non-depreciable assets (e.g. land) tax deferral under above alternative (i) could be applied.

We further support the Commission's view that economic double taxation with respect to transfer of assets and exchange of shares at book value needs to be removed. Under the current Merger Directive rules, the same hidden reserves may be taxed twice in the hands of

two different taxpayers upon subsequent sale of the transferred assets and received shares respectively. These rules remained unchanged upon its last revision in 2005 despite massive criticism and Commission's respective proposal. We agree with the Commission that such double taxation should be avoided under CCCTB rules by providing for a (tax neutral) step up to fair market value of shares received (in exchange for transferred assets). As proposed in the Paper, to counter any short term tax planning techniques a minimum holding period for the shares received of not more than two years could be considered.

Scenario 3: Some entities covered by CCCTB rules and other entities which are not

Scenario 3 was not further discussed in the Paper. Under such scenario, CCCTB rules and domestic rules would apply depending on seat/management of entities concerned and/or whether these entities have opted for CCCTB. Assuming that CCCTB rules for reorganizations would be more attractive than domestic rules this could help to further promote CCCTB rules to MS that do not adopt CCCTB and/or companies who at first decided not to opt for CCCTB.

On behalf of the UNICE Task Force on CCCTB

Krister Andersson

December 6, 2006