Comments on document CCCTB\WP\010 – Common Consolidated Corporate Tax Base Working Group – Capital gains and losses

Introductory remarks

The Working Paper on capital gains gives an excellent overview and focuses on a number of important issues. Considering the character of the topic it appears appropriate that more detailed work is done by SG1. We would also like to stress that the comments in this paper only deal with capital gains and losses on tangible and intangible assets. There is a need to deal separately with capital gains on financial assets, especially with respect to shares. We consequently agree with the approach that capital gains on assets will be discussed first and that a potential specific treatment on financial assets is dealt with at a later stage.

Tax treatment

A CCCTB should be based on the principle that profits or losses arising in a business shall be treated the same way for tax purposes irrespectively of how they have materialized, be it from working capital or from other assets. Capital gains should thus be treated as ordinary business income. This promotes simplicity.

In line with this, ring fencing should be avoided. Apart from being questionable from a principle perspective, ring-fencing gives rise to substantial differentiation problems. This does for example regard how to distinguish between capital gains (and losses) and other business profits (and losses). Such a differentiated treatment also infringes on the principle of neutrality.

It shall furthermore be noted that ring-fencing creates specific problems for small businesses which possess only one or a few high net-worth ring-fenced assets (such as land or buildings). Where such businesses make capital losses, there is a substantial risk that they can not recoup these losses within a reasonable time frame.

As a general rule, capital gains should thus be fully taxed (except if roll over treatment or specific incentive rates apply) and capital losses fully relievable. We do not find it appropriate to adopt some limitations on the deduction of capital losses.

Time of taxation

A core issue is under what circumstances a capital gain shall trigger taxation. A well-founded and internationally accepted principle is that taxation shall be levied only upon realization. It is essential that this principle is recognized within a CCCTB, as a system that provides for taxation of unrealized gains would give rise to unacceptable consequences from a business perspective. For reasons of simplicity, administration costs and the stability of public finances, accrual taxation is not desirable. On these grounds we agree with the Commission and would like to further emphasize that capital gains should be taxed only upon realization.

An interlinked question is how to establish the moment when an asset has been realized for tax purposes. In this respect, the concept of 'disposal' is crucial. In the paper, the Commission suggests that the term 'disposal' should be understood as broadly as possible. In our view, however, a common definition of 'disposal' should reasonably seek to define the moment when a capital gain or loss has occurred for tax purposes (i.e. when it is realized and therefore be available for taxation). We therefore believe that the aim should be to find a definition that is as *accurate as possible* with respect to the principle of realization, rather than as broad as possible. As an example, a change from an economical owner to a legal owner should not be regarded as a disposal triggering taxation.

Roll-over relief

Several countries allow for roll-over relief. This is especially the case for high net-worth assets that are essential for the core business activity.

To the extent capital gains are reinvested, we believe that roll-over relief shall be granted within a CCCTB. This is important to promote reinvestment and growth. Also, if no such relief is available, there is a risk that assets are used longer than appropriate from an economic efficiency perspective. Roll-over relief is furthermore structurally important in order to uphold the principle that tax shall be levied only on income and not on substance.

Calculation

As recognized by the Commission, the calculation of capital gains (and losses) very much depends on the method used for tax depreciation. We therefore suggest that this issue is analyzed in conjunction with the future work on depreciation of assets. From a general perspective, however, we believe that simplicity and prudence must be guiding principles in this respect.

Other issues

With respect to disposal occurring between related companies, it is important that documentation requirements and related rules are avoided to the extent possible and that they are based on the principles of simplicity and prudence, provided such requirements are still appropriate within a CCCTB system.

We would also like to stress that there is no room for domestic flexibility within a CCCTB. The same rules must be used by all countries and be applied in a uniform manner. A system that allows for domestic variations would undermine the core purpose of a common consolidated tax base.

Furthermore, to promote simplicity, indexation for inflation should preferably be avoided and monetary policy should ensure price stability. The negative effects of a low but stable inflation rate could be taken care of by increasing depreciation rates and by lowering tax rates. Inflation is also dealt with by allowing for roll-over relief.

Regarding the issue of exit taxes, it appears appropriate that it is discussed in conjunction with other third country issues at a later stage.

As a concluding remark we would like to emphasize the importance of simplicity and realization as guiding principles for the purpose of designing rules on capital gain within a CCCTB system.

On behalf of the UNICE Task Force on CCCTB

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