



EUROPEAN COMMISSION
DIRECTORATE-GENERAL
TAXATION AND CUSTOMS UNION

Direct taxation, Tax Coordination,
Economic Analysis and Evaluation
Company taxation initiatives

26 July 2010

Consultation paper

Note

This document is being circulated for consultation to all interested parties concerned by a possible initiative in the area of taxation of cross border interest and royalty payments between associated companies. The sole purpose of this consultation is to contribute to the debate, to collect relevant information and to help the Commission develop its thinking in this area.

This document does not necessarily reflect the views of the European Commission.

Each contribution received will be acknowledged.

Contributions received, together with the identity of the contributor, will be published on the Internet, unless the contributor objects to publication of personal data on the grounds that such publication would harm his or her legitimate interest. In that case, the contribution may be published anonymously. Otherwise the contribution will not be published and its content will not, in principle, be taken into account. For more detailed information on how your personal data and contribution will be treated, we recommend that you read the specific privacy statement.

In the interests of transparency, organisations responding to this consultation are invited to provide the public with relevant information about themselves by registering in the Interest Representative Register and by subscribing to its Code of Conduct

(see <https://webgate.ec.europa.eu/transparency/regrin/welcome.do?locale=en>).

If the organisation is not registered, its submission will be published separately from those of registered organisations.

The parties concerned are invited to submit their comments no later than

31/10/2010

1. IDENTIFICATION OF THE STAKEHOLDER

The Commission services would be interested in receiving contributions from all interested parties on the tax policy issues described below. In order to analyse the responses, it will be useful to group the answers by type of responder.

<u>Question 1.</u> -You could be included in one of the following groups ¹ :	
<input type="checkbox"/> Multinational enterprise	<input type="checkbox"/> Large company
<input type="checkbox"/> Medium sized enterprise (SMEs)	<input type="checkbox"/> Small sized enterprise (SMEs)
<input type="checkbox"/> Microenterprise (SMEs)	<input type="checkbox"/> Tax advisor or tax practitioner
<input type="checkbox"/> Academic	
<input type="checkbox"/> Others. Please specify _____	
Name/denomination of your organization/entity/company _____	
Country of domicile _____	
Contact details, including e-mail address _____	
Brief description of your activity or your sector _____	
Do you object to publication of personal data on the grounds that such publication would harm your legitimate interests?	
Yes <input type="checkbox"/>	No <input type="checkbox"/>
Do you agree to having your response to the consultation published along with other responses?	
Yes <input type="checkbox"/>	No <input type="checkbox"/>

¹ For the purposes of identification, please check whether your company is a medium, small or microenterprise, according to the Commission Recommendation (2003) 361 of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises; in its annex, Title I, Article 2, SMEs are defined as enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million. Within the SME category, a small enterprise is defined as an enterprise which employs fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 10 million. Within the SME category, a microenterprise is defined as an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million.

2. INTRODUCTION

The Commission is currently considering recasting and amending Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States (hereinafter "the Directive" or "the Interest and Royalties Directive").

In the case of cross-border interest and royalty payments, the recipient companies may face excessive or double taxation due to withholding taxes charged in the source Member State, which lead to other efficiency losses: namely burdensome administrative formalities linked to payments, resulting in compliance costs and cash-flow problems. The purpose of the Directive is to put cross-border interest and royalty payments between associated companies in the EU on an equal footing with domestic payments by exempting them from taxes imposed by the source States.

However, the effects of the Directive are limited due to its current scope. If this remains unchanged, the inefficiencies affecting the functioning of the single market will not be removed.

The Commission is launching this public consultation with a view to exploring the opinion of stakeholders on the different legislative options that are being considered in order to extend the benefits of the Directive.

The initial selection of topics is based on a Commission report on the operation of the Directive (see below) and debate amongst tax policy makers.

3. BACKGROUND

There are three main factors involved in the recast and the amendment of the Directive. In the first place, the report on the Directive, COM (2009) 179, prepared in accordance with Article 8 and published in April 2009 which refers to the need to introduce some legal amendments aimed at improving its functioning.

Secondly, the tax issue is also governed by Directives 2004/66/EC and 2004/76/EC. The application of the former extends its scope to companies and taxes of the States that became members of the EU after 2004, while the latter grants some of these new Member States temporary derogations from one or more provisions of the Directive. These texts need to be consolidated.

Lastly, in 2003, the Commission adopted a proposal amending the Directive (COM (2003) 841 final of 30.12.2003) which had two objectives: an updated annex listing the types of companies falling within the scope of the Directive (including the European Company and the European Cooperative Society) and a better targeted definition for the subject-to-tax requirement, which the Council requested when the original Directive was

adopted. This proposal has since been withdrawn but these aspects could now be incorporated into the recast of the Directive.

4. QUESTIONS SUBMITTED TO THE PUBLIC AND TO INTERESTED PARTIES

Issue 1 - The extension of the list of entities covered by the Directive

The Directive is only applicable to companies which are of a legal type listed in its annex. The list of entities is drawn up by reference to the national laws. There is an entry for each Member State where reference is made to the legal types covered by the Directive.

Council Directive 90/435/EEC on the common tax regime applicable in the case of parent companies and subsidiaries of different Member States ("the Parent-Subsidiary Directive") is also applicable to the legal types included in its own list. The latter Directive shares the aim of the Interest and Royalties Directive, namely the elimination of double taxation. However, the lists annexed to the two Directives are different. The one annexed to the Parent-Subsidiary Directive is broader and refers to more national legal types. The consequence of this is that economic agents have to adopt a legal type that is included in both lists in order to benefit from all harmonized corporate tax law.

Question 2. - Do you think that there is a need to update the list of companies covered by the Directive?

Yes

No

Do not know

Question 3. – Do you think that the list annexed to the Directive should cover the same legal types as are included in the list of the Parent-Subsidiary Directive, including the European Company and the European Cooperative Society?

Yes

No

Do not know

Question 4.- Do you think that the list should be extended so as to include other types of companies not referred to in the Parent-Subsidiary Directive?

Yes

No

Do not know

If your answer is yes, please specify legal types:

Issue 2 - The extension of the definition of associated companies: indirect shareholdings

The Directive only covers payments between associated companies. For this purpose, an association is deemed to exist when one of the companies has a direct minimum holding of 25 % in the capital of the other company, or a third company has a direct minimum holding of 25 % in the capital of both the payer and the recipient companies.

As mentioned, the scope of the Directive is currently limited to direct holdings, while the scope of the Parent-Subsidiary Directive has no such limitation. The consequence is that, in order to benefit from all harmonized corporate tax law, economic agents must maintain a minimum direct holding of 25%.

Question 5.- Do you consider it beneficial to allow indirect shareholdings to be taken into account when the minimum shareholding is being determined?

Yes

No

Do not know

Issue 3 - The lowering of the shareholding thresholds required in order to be considered as associated companies

The minimum shareholding requirements of the Directive currently differ from those of the Parent-Subsidiary Directive, by requiring 25% rather than the 10% in the Parent-Subsidiary Directive.

Question 6.- Do you think that there is a need to change the minimum shareholding requirements?

Yes

No

Do not know

Question 7.- Do you think that the shareholding requirements of the Interest and Royalties Directive should be reduced to 10% and thus be aligned with those established in the Parent-Subsidiary Directive?

Yes

No

Do not know

Question 8 .- Do you think that the shareholding requirements of the Interest and Royalties Directive should be reduced to below 10%?

Yes

No

Do not know

If your answer is yes, please specify the shareholding requirement:

Issue 4 – Extending the Directive to payments between unrelated undertakings

One option might be for the Directive to eventually encompass unrelated undertakings. It is self-evident that international double taxation, burdensome administrative formalities and cash-flow problems, such as cross-border obstacles to transactions between related companies, are also present in the case of payments between unrelated parties. The current harmonized tax law fosters activities within multinational groups, but does not address the double taxation issues that are hampering the smooth functioning of the single market in the case of transactions between independent parties.

Question 9 .– Do you currently suffer from double taxation and/or additional administrative costs because the Directive does not extend to transactions between unrelated undertakings (non associated)?

Yes

No

Do not know

If your answer is yes, please estimate the annual additional taxes and costs in euros _____

Issue 5 – The tax deductibility requirement applicable to payments made by permanent establishments

The Directive covers payments made by permanent establishments of companies situated in an EU Member State. In this case, the obligation of the source State to refrain from taxing is made conditional on such payments being a tax-deductible expense for the payer. It is clear from the context that the purpose of the 'tax-deductibility' requirement is to ensure that the benefits of the Directive accrue only in respect of those payments that represent expenses which are attributable to the permanent establishment. However, on its wording, the provision would also apply to cases where deduction is denied on other grounds, such as a payment not meeting all the formal requirements for tax deductibility.

Question 10.– Do you think that the text of the Directive should be clarified in order to guarantee that its benefits apply to interest or royalty payments constituting an expense attributable to permanent establishment?

Yes

No

Do not know

Issue 6 – Concerns of SMEs

The Commission services are interested in the potential impact that the above issues and others might have on SMEs. The aim is to reflect on possible initiatives targeted in particular at such stakeholders, so that the tax environment in the Single Market takes better account of their specific needs and fosters their cross-border activities.

The following questions are directed at those qualifying as SMEs as defined above in question 1.

Question 11.- Do you regard withholding taxes charged on your interest or royalty cross-border income as an obstacle to your activities?

- Yes, it is very burdensome as it limits cross-border activities.
- Yes, it is a significant tax obstacle.
- Yes, it is an obstacle, but it can be avoided.
- No

Question 12.- Do you find that the tax compliance costs linked to cross-border interest or royalty payments are:

- High enough to restrict cross-border activities;
- High;
- Bearable and do not distort your activities;
- Negligible.

Question 13 - Do you think that extending the Directive's scope to include all the entities currently covered by the Parent-Subsidiary Directive would ensure that all SMEs will be covered by it:

Yes No Do not know

If your answer is no, please specify what other legal types currently used by SMEs should be included in the list of the Directive _____

5. WHO IS CONSULTED?

Tax professionals in practice, in business and in academia.

6. HOW CAN I CONTRIBUTE?

You are invited to reply to this consultation by completing the questionnaire below and sending it by letter, fax or email before 31/10/2010 to:

Email: TAXUD-D1-Consultation-LANDR@ec.europa.eu

Postal address: European Commission
Directorate-General for Taxation and Customs Union
Rue de Spa 3, Office 8/17
B-1049 Brussels
Belgium
Fax: +32-2-29 56377

7. WHAT WILL HAPPEN NEXT?

At the end of the consultation process the Commission will publish on the website of the Taxation and Customs Directorate General a report summarising the outcome of the consultation (http://ec.europa.eu/taxation_customs/common/consultations/tax/index_en.htm).

In addition, the Commission will carefully analyse the information provided in order to understand the reasons that underlie the reported cases of double taxation in the EU. It will then launch a debate on how these cases could be eliminated and consider whether there is a need for action at EU level.

8. ANY QUESTIONS?

Please contact: TAXUD-D1-CONSULTATION-LANDR@ec.europa.eu
or tel. + 32 2 29 74537
or fax: +32-2-29 56377

We hope you will take this opportunity to contribute your views!