



EUROPEAN COMMISSION  
DIRECTORATE-GENERAL  
TAXATION AND CUSTOMS UNION  
TAX POLICY  
Coordination of Tax Matters

Brussels, 11 March 2003  
C1/LDH/

**DOC: JTPF/005/REV1/2003/EN**

## **EU JOINT TRANSFER PRICING FORUM**

### ***THE ACCESSION OF EU CANDIDATE COUNTRIES TO THE ARBITRATION CONVENTION***

**Meeting of Wednesday 2 April 2003**

**Centre de Conférences Albert Borschette  
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**Working paper**

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## **1.BACKGROUND**

- The Convention 90/436/EEC on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (hereafter: “Arbitration Convention”) was signed on 23 July 1990 and entered into force, after ratification by all Contracting States, for an initial and renewable period of 5 years on 1 January 1995.
- With the accession to the EU of Austria, Finland and Sweden, a new Convention allowing these new Member States to accede to the Arbitration Convention, was signed on 21 December 1995. Since not all Contracting States have ratified this accession Convention, it has not yet entered fully into force.
- As the Arbitration Convention was due to expire on 31 December 1999, all Contracting States signed on 25 May 1999 a Protocol, extending its application by 5 years. The Protocol also provided for its automatic extension every 5 years for 5 year periods unless a Contracting Party objected. Since not all Contracting States have ratified this Protocol yet the Arbitration Convention has not re-entered into force since 1 January 2000.
- In its Communication “Towards an Internal Market without tax obstacles – A strategy for providing companies with a consolidated corporate tax base for their EU-wide activities” COM (2001) 582 of 23 October 2001, the Commission announced its preference to turn the Arbitration Convention into an instrument of Community Law so as to make it subject to interpretation by the ECJ.

## **2.ACCESSION OF CANDIDATE COUNTRIES TO THE EU**

Ten candidate countries will sign on 16 April 2003 a Treaty and Act of Accession to become a formal EU Member State on 1 May 2004.

The draft of the Act concerning the conditions for accession provides in its Articles 5 (2) that:

“The new Member States undertake to accede to the conventions provided for in Article 293 of the EC Treaty and to those that are inseparable from the attainment of the objectives of the EC Treaty, and also to the protocols on the interpretation of those conventions by the Court of Justice, signed by the present Member States and to this end they undertake to enter into negotiations with the present Member States in order to make the necessary adjustments thereto.”

## **3.ACCESSION OF CANDIDATE COUNTRIES TO THE ARBITRATION CONVENTION**

### **3.1.Procedure to be followed**

As was the case in 1995, this new EU enlargement requires a new “Convention on the accession of the candidate countries”, to be signed and ratified by all Contracting States (the 25 Member States of the EU). This new accession Convention should not only refer to the original Arbitration Convention but also to the 1999 Protocol.

The Arbitration Convention and its Protocol will have to be translated into the languages of the new Contracting States.

In the accession Convention, the new Contracting States should specify to which taxes the Arbitration Convention shall apply (Art.2), and which is the “competent authority” (Art.3). Unilateral Declarations regarding Article 7 (independence of domestic judicial bodies) and Art.8 (serious penalties) should also be filed.

### **3.2.Entry into force**

In analogy with the provisions established for the enlargement in 1995, the entry into force of the Convention with the accession countries would read as follows:

“This Convention shall enter into force, as between the States which have ratified it, on the first day of the third month following the deposit of the last instrument of ratification [by the accession countries] and by one State which has ratified the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises.

This Convention shall enter into force for each Contracting State which subsequently ratifies it on the first day of the third month following the deposit of its instrument of ratification.”

## **4.PROBLEMS AND POSSIBLE SOLUTIONS**

The Arbitration Convention being a community convention, it should be noted that it is for the Council Secretariat General to undertake all formal action. However, the Commission services can take the initiative to make certain proposals.

### **4.1.Revision of the Arbitration Convention**

Although the Commission announced in its October 2002 Communication, the intention to revise the Arbitration Convention and turn it into a Community law instrument (i.e a Directive), an initiative supported by the Commission’s Legal Service, the time does not seem ripe yet to propose such a proposal. The EU Joint Transfer Pricing Forum has only met twice and has not reached any conclusions/agreements on the existing Convention so far. Waiting for the outcome of the Forum before taking any initiative as regards enlargement does not seem a valid alternative either considering the need for candidate countries to access as quickly as possible the Convention and the lengthy process for the adoption of a possible Directive.

### **4.2.Arbitration Convention and Protocol**

As stated above, the new accession Convention will need to refer both to the Arbitration Convention and its 1999 Protocol, and will require translation of all acts into all languages and upon signature of the Convention, subsequent ratification by all Contracting States.

Therefore the possibility of **consolidating** the Arbitration Convention and Protocol could be considered.

Consolidation would contribute to transparency and simplicity in particular with respect to forthcoming new enlargement operations. It would also avoid the drafting of a new, current, accession Convention since the new consolidated Arbitration Convention could be signed and ratified as such by all 25 contracting states.

However, this procedure could impede the possible speedier bilateral entry into force of a usual accession Convention between the candidate countries and the Contracting States that could ratify the accession Convention rapidly.

#### **4.3. Entry into force of Arbitration Convention with candidate countries**

Since the Arbitration Convention is a Community convention, the candidate countries cannot accede (sign) before they become EU Member State, ratification taking place after signature is thus even further in future.

In the light of the experience with the 1995 EU enlargement and the 1999 Protocol, it seems important to avoid long transitional periods in which the Arbitration Convention would not be fully applicable in the new accession countries. Candidate countries like Poland and the Czech Republic are likely to have rapidly numerous cases to which the Arbitration Convention could apply.

According to Article 25 of the (UN) Vienna Convention on the law of Treaties, which came into force on 27 January 1980, “a Treaty or part of a Treaty is applied provisionally pending its entry into force if:

- the treaty itself so provides; or
- the negotiating States have in some other manner so agreed.”

This agreement does not require any specific format.

The accession Convention, or the case being the consolidated Arbitration Convention, could contain a provision specifying that upon signature (or starting from a date in the near future) the Arbitration Convention shall be **applied provisionally** pending its entry into force.

Alternatively, a **Joint Declaration** of all Contracting States, could have the same effect.

However, a possible disadvantage of this procedure would be that internal requirements of certain Contracting States could prevent even provisional application without parliamentary approval.

Another possible and more definite solution for a rapid entry into force (which however again could be countered by certain internal requirements) could be found in Article 24(1) of the aforementioned Vienna Convention which stipulates that:

“A treaty enters into force in such manner and upon such date as it may provide or as the negotiating States may agree”

Instead of using the formulation specified under 3.2, Contracting States could agree an entry into force on signature, instead of on ratification or a full entry into force when (X) Contracting States have ratified the Convention.

*Experts from national tax authorities and in particular those from candidate countries are requested to consider the feasibility of these possible solutions in the framework of their internal legislation and report back to the JTPF in order to enable the Commission to forward as soon as possible some concrete proposals to the Council Secretariat General.*

#### **4.4.Candidate countries and OECD guidelines**

Transfer Pricing practices in general and the EU Arbitration Convention are largely underpinned by the OECD “Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration” which sets out the general principles (i.e. the Arms Length Principle), methodologies to be applied, guidance on documentation requirements, etc.

However, eight out of the thirteen EU candidate countries, are not Members of the OECD (Bulgaria, Estonia, Cyprus, Latvia, Lithuania, Malta, Romania and Slovenia).

In tandem with the efforts made by the OECD administration to reinforce these countries’ awareness of the importance of respecting the relevant OECD Guidelines and their association with ongoing work, DG TAXUD is considering the use of the FISCALIS programme (seminars and training) to improve the knowledge of these guidelines and the familiarisation with Mutual Agreement Procedures and the Arbitration Convention in particular.

#### **5.OPERATIONAL CONCLUSIONS**

1. On the basis of the ideas expressed in the JTPF, the Commission will contact the Council Secretariat-General (Tax Questions Group) to discuss proposals in order to achieve a rapid implementation of the Arbitration Convention in the new EU Member States.
2. DG TAXUD will ask for the approval of the FISCALIS programme committee to organise a seminar for all candidate countries’ officials on MAP and the Arbitration Convention in November/December 2003.
3. The JTPF will be informed as soon as possible about the progress on these issues.

## 6. MEMBER STATES AND CANDIDATE COUNTRIES POSITIONS

Country	Provisional application	Entry into force upon signature
Malta	YES, but not earlier than six months after signature	YES, but not earlier than six months after signature
United Kingdom	YES	YES
Spain	YES	YES
Germany	YES, subject to prior Parliamentary approval	NO, constitutionally not possible
Lithuania	YES, subject to prior Parliamentary approval	NO, constitutionally not possible
Estonia	NO	NO
Slovakia	NO, need for ratification by Parliament	NO, need for ratification by Parliament
Latvia	NO, need for ratification by Parliament	NO, need for ratification by Parliament
Italy	NO	NO
Netherlands	YES, The current Dutch legislation dealing with the approval of treaties and conventions in general permits the possibility of provisional application under certain conditions.	?: In principal, the Netherlands cannot commit itself to a treaty or convention without the prior approval of the Dutch parliament. However, there are situations in which current Dutch legislation that deals with the approval of treaties and conventions in general permits such commitment without prior approval of parliament. In those situations it might be possible that a convention enters into force upon the date of signature. One of the possibilities in this respect, is that the Dutch legislation specifically dealing with the approval of

		the respective accession treaties contains a provision that determines that prior approval of parliament is not required for the extension of existing treaties to new Member States. The Dutch government plans to use this possibility. It should be taken into account, however, that the legislation dealing with the approval of the accession treaties will be subject to parliamentary scrutiny