



EU-Japan Centre for Industrial Cooperation

European Commission - DG Taxation and Customs Union

EU Corporate Tax Policy

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Main Themes

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- **General introduction to EU tax policy**
 - Key facts on EU taxation
 - Legal base for Community action
 - Institutional, Economic & Political framework
 - The Nice summit / EU Convention / IGC / enlargement

- **Company Taxation – current initiatives and future priorities**
 - Commission Communication COM(2003)726
 - 'Targeted initiatives'
 - 'Comprehensive solution': Home State Taxation and a Common Consolidated EU Tax Base
 - Pilot schemes for SMEs and/or Societas Europaea?



Some key facts on EU taxation

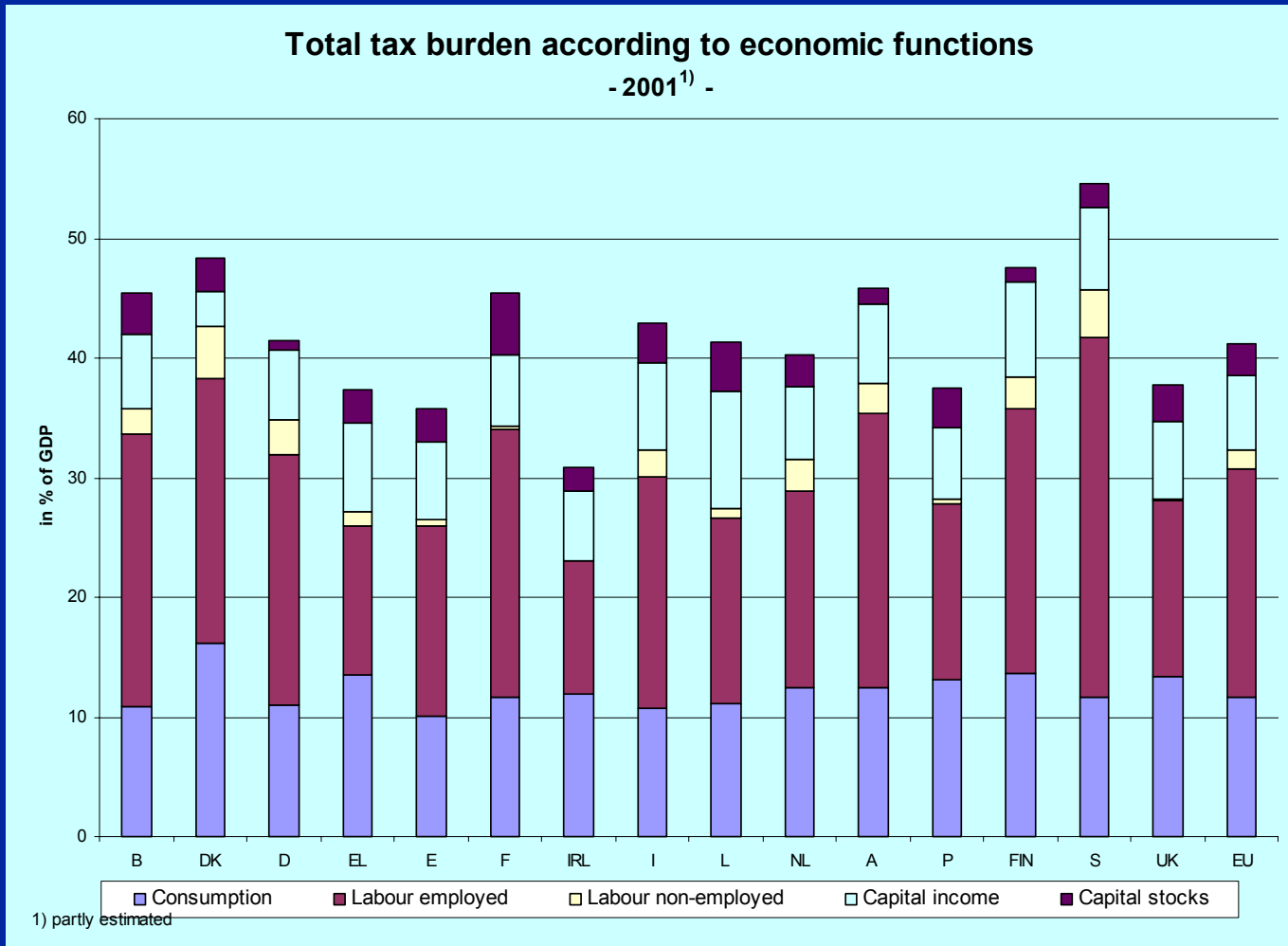
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- **No Community taxes in the strict sense (but VAT own resources)**
- **very different structure of taxation systems in Member States**
 - overall taxes as % of GDP
 - share of different types of taxes



Share of different types of taxes in GDP per Member State

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Legal base for Community action

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- **Article 12: “any discrimination on grounds of nationality shall be prohibited”**
 - also for taxation general rule
 - **Art. 25-27: harmonisation of customs tariffs and other charges related to international trade - already abolished within the EU**
 - **Art. 90: forbids tax discrimination which directly or indirectly offers advantages to domestic “products” as compared to those from other Member States - infringement procedures, ECJ !!!**
 - **Art. 91-93: abolition of export subsidies within the EU and harmonisation of turnover taxes, excises and other indirect taxes (unanimity) - Single Market**
 - **Art. 94, 308: approximation of legislation by means of directives wherever this is necessary to improve the functioning of the Single Market or meet other Community objectives - direct taxes**
 - **link to basic Treaty freedoms: free movement of goods / free movement of workers / freedom of establishment for companies and individuals / freedom to supply services cross border / free movement of capital**
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The role of the European Court of Justice

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- **starting point: the 4 fundamental freedoms - free movement of services, goods, persons; freedom of establishment**
- **Member States must not *discriminate* against foreign EU nationals/residents or *restrict* free movement/establishment**
- **Development of EU Tax Law has largely taken place via these Treaty provisions as interpreted by the ECJ in cases referred by national courts (preliminary rulings)!**
- **The ECJ has taken a “firm” line**
- **The number of cases have increased significantly in recent years**
- **Commission proposes better co-ordination!**



Spectrum of taxation

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Internal Market :

- **Certain aspects of indirect taxation - e.g. VAT - require a high level of harmonization [Legal Base, indirect tax, article 93 EC Treaty]**
- **Some other aspects of Member States' tax systems require an approximation [Legal Base, direct tax, article 94 EC Treaty]**

Other Elements :

- **There are areas where a certain amount of co-ordination is necessary, e.g. the direct taxation of potentially mobile tax bases such as company taxation and taxation of savings; 'soft approach' such as the Code of Conduct**
- **Some other aspects of Member States' tax systems do not need to be harmonized, approximated or co-ordinated (subsidiarity), eg the structure of personal income tax**



Institutional framework

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Institutional : constraints on fiscal policies in the EMU

- **Stability & Growth Pact : budgets must be close to balance or in surplus**
- **Broad Economic Policy Guidelines (2001): lower overall tax burden; improve the efficiency and transparency of tax systems (broad base & low rates)**
- **Employment Guidelines (2001): reduction of taxation on labour, especially low-skilled**



Economic framework

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Economic : taxation in EMU

- **Tax obstacles and the proper functioning of the Single Market: tax distortion to the location of investment**
- **Growing interdependence of Member States' economies and hence tax systems. Economic integration may imply loss of some degree of freedom in taxation**
- **Harmful tax competition and tax base erosion. Increasing burden of taxation falling on labour. Consequences for unemployment levels**



Political framework

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Political :

- **Taxation is seen as a fundamental element of individual state sovereignty**
- **The unanimity requirement !!!**
- **Any change - therefore - is by slow evolution**



The Nice Summit 2000

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Developments on the tax front -

- On overall tax policy : unanimity remains the general rule

But

- further development of ‘enhanced co-operation’.
This will permit a group of Member States to make significant advances, for example in the field of taxation, without being blocked by the veto.
This could be very useful in certain cases.
- Agreement on the ‘European Company Statute’



EU Convention / IGC

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● EU Convention

○ proposal to move to qualified majority voting in selected tax areas, e.g.

- large parts of indirect taxation
- direct tax matters with impact the functioning of the Internal Market
- compromise: flexibility clause

○ discussion about a EU-tax



EU Corporate Taxation: Background

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- **Communication ‘Tax Policy in the European Union (May 2001)**
 - Pragmatic & evolutionary approach, based on the subsidiarity principle
 - ‘... provided that they respect Community rules, Member States are free to chose the tax systems that they consider most appropriate and according to their preferences ...’
- **Company Tax Communication & Company Tax Report (October 2001)**
 - Re-affirmed that rates are for Member States to decide
 - Identified tax obstacles and set out remedies: a twin track strategy for their removal: short term measures & long term consolidated corporate tax base



Pressures for tax co-ordination

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- **Remove the obstacles**
- **Internal Market efficiency – e.g. compliance costs**
- **Code of Conduct – roll back of harmful practices**
- **State Aid – clarification and increased Commission action**
- **ECJ – ongoing series of cases identifying problems with Member State tax systems *vis a vis* the Treaty**



Two-pronged strategy for removing the tax obstacles

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Twin-track strategy for removing the tax obstacles

- **targeted measures to address tax obstacles to cross-border economic activity in the Internal Market**
 - directives
 - non-binding initiatives (EU-guidelines; working parties etc.)
- **comprehensive solution: providing companies in the long-term with one set of corporate tax rules for their EU-wide activities (common tax base)**
 - studies (allocation of tax base etc.)
 - pilot projects (European Company Statute, SMEs)



Follow-up Communication November 2003

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- **Communication "*An Internal Market without company tax obstacles – achievements, ongoing initiatives and remaining challenges*" [COM(2003)726] adopted on 24 November 2003**
- **Review of strategy for removal of cross-border tax obstacles**
- **Website:**
http://europa.eu.int/comm/taxation_customs/whatsnew.htm



Tax obstacles in the Internal Market

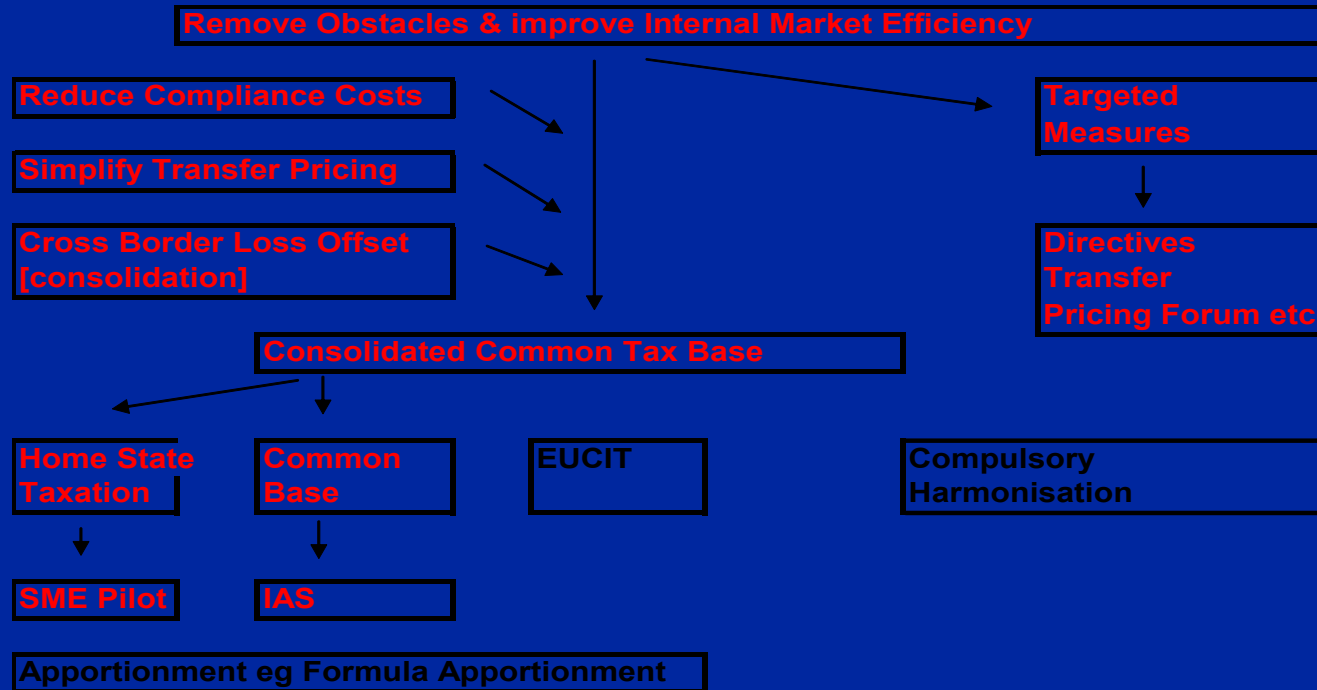
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- **Deficiencies of EU tax directives**
 - **Double-taxation treaties**
 - **Taxation of cross-border restructuring operations**
 - **Cross-border loss-offset**
 - **Transfer pricing**
 - **Compliance cost**
 - **etc.**
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Initiatives Diagram

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State of Play: Targeted Solutions (I)

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- **Amendment of existing Merger and Parent/Subsidiary Directives**
 - presented in July (parent-sub.) and October (merger) 2003
 - extend the scope of the Directives, relax the conditions for companies to benefit from them and resolve some of the shortcomings which have arisen in their application

- **Provision of non-binding guidance to Member States on application of EU law**
 - Discussions started with MS in Commission Working Group (Lankhorst-Hohorst case on thin capitalisation rules)
 - Occupational pensions & Investment funds
 - Dividend Taxation Communication to be presented soon



State of Play: Targeted Solutions (II)

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- **Discussions with a view to preparing a new proposal on cross-border loss-offset**
 - **Old proposal formally withdrawn, discussions 2004 (possibly linked to a consolidated common base)**
 - **Danish model?**
 - **Initiative planned for late 2004/early 2005**

 - **Preparation of a Communication on double taxation treaties in the light of the EC Treaty principles**
 - **Planned for for late 2004/early 2005**
 - **"most favoured nation" clause?**
 - **EU model Treaty or EU variant of OECD model?**
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State of Play: Targeted Solutions (III)

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● Joint EU Transfer Pricing Forum

- **Members: representatives from MS and acceding countries, business community; OECD as observer**
- **objective: exchange of best practice; non-legislative solutions**
- **Numerous meetings; timetable until 2004**
- **intermediary report on dispute settlement procedures to be published in early 2004**
- **next issue: documentation requirements**
- **then: avoidance of double taxation (e.g. advance pricing agreements; requirement of agreement of both tax administrations prior to tp adjustments etc.)**
- **detailed information at website:**

http://europa.eu.int/comm/taxation_customs/taxation/company_tax/de/transfer_pricing.htm



Long Term strategy - a consolidated tax base

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- **Reduce compliance costs of 15 (soon 25) tax systems**
- **Reduce Transfer Pricing problems**
- **Allow cross border loss offset**
- **Simplify EU corporate restructuring**
- **Avoid double taxation**
- **Remove many discriminatory situations and restrictions**

- **i.e. a logical approach to a single market, in line with traditional Member State 'single tax base approach for whole of their jurisdiction'**



Which base?

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● **Communication & April 2002 Conference identified:**

○ **Home State Taxation**

- A multinational group can opt for computing its tax base according to the rules of the Member State where its headquarter is based

○ **Common Consolidated Base Taxation**

- A multinational group can opt for computing its tax base according to completely new harmonised EU rules

○ **European Corporate Income Tax (EUCIT)**

- Corporation tax would be levied at the European level and revenues would go (at least partly) to the EU budget

○ **Compulsory Harmonisation**

- All companies in the EU would compute their tax base according to harmonised rules
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Comprehensive Approaches (continued)

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- **All options would offer companies the possibility of using a single tax base for all their EU-wide activities**
- **All, except EU CIT, would require a mechanism for allocating tax base / tax revenues between Member States**
- **In all cases, except perhaps EU CIT, Member States would set the tax rates**
- **All have specific advantages and disadvantages**



Home State Taxation (HST)

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- **Based on the mutual recognition by Member States of each others tax rules**
- **A group of companies can choose to calculate their tax base according to the rules of the Member State where its headquarters is based – the 'home state'**
- **Each Member State then taxes its share of the overall taxable group profits at its own tax rate**
- **Commission working on a possible pilot project for Small and Medium Sized Enterprises (SMEs) (public consultation earlier this year – wide support)**



Possible Pilot project - HST for SMEs

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- **Aims to simplify, and reduce the costs of, tax compliance**
 - **Need a practical test, relatively narrow application**
 - **5 year test period**
 - **Special rules for changes of ownership, business expansion etc**
 - **Only company taxation – e.g. not VAT**
 - **Simple allocation formula of consolidated tax base (where the Home State permits consolidation)**
 - **Home State tax audit – general rules on mutual assistance in EU continue to apply**
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Progressing a HST pilot scheme

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- **Multilateral or bilateral agreements could establish HST, but**
- **EU framework desirable, as 'soft law' - e.g. Communication, or Council Recommendation setting out 'best practice'**
- **Participating MS would need to monitor the pilot to assess progress**

- **Commission to intensify discussions with interested MS and business representatives during 2004 to further consider technical issues and develop more detailed possible arrangements**



Common Consolidated Base Taxation & IAS

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- **Consultation/Issues Paper published on IAS**
- **‘examines general principles of IAS.....clear that IAS accounts would represent at the most a starting point for arriving at a tax base and not the tax base itself’ [para 1 Summary]**
- **To what extent can IAS financial statements satisfy tax requirements?**
- ***[Allocation Mechanism - e.g. Formula Apportionment - separate issue, preliminary work started]***



IAS - Questions & issues

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● General Principles

- The user - investor orientated accounting standards
- Materiality - precision of accounts compared to tax returns and different levels of materiality depending on size of company
- Substance over form - differing approaches across EU
- Fair value accounting - unrealised gains and losses, objectivity of estimates



IAS - Questions and issues (cont)

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- **Number of companies (discrimination, MS ‘permit/require’)**
- **Consolidation (IAS financial consolidation or new tax specific method)**
- **Dependency**
- **Legislative framework and legitimacy (endorsement process (QMV), Regulation, Directive, Recommendations)**
- **SE as a pilot**



Results of consultation (1)

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- **Summary published July – over 40 detailed submissions**
- **Generally supportive of a common base in principle**
 - **Minority against co-ordination, convergence in principle**
 - **Several industry specific concerns/positions e.g. Banking & Insurance**
- **Some have less enthusiasm for a *consolidated* base**
 - **Real preference for a ‘simple’ common base applied by each Member State?**
 - **Member States unlikely to agree, or**
- **Two step approach for introduction?**



Results of consultation (2)

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- **Some doubts over IAS as starting point [private body, different purpose, volatility of IAS etc] - but no real other suggestions**
- **Some strongly supported IAS as a *neutral* starting point for defining the tax base**
- **Spill-over from accounting difficulties? - eg IAS 32 & 39**
- **Fair value consistently identified as inappropriate, but relatively straightforward to adjust for?**



Results of consultation (3)

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- **Issues identified by Commission confirmed as the major points e.g.**
 - **Materiality - but not considered an issue by many**
 - **Substance over form - fear of legal uncertainty and inconsistency**
 - **Endorsement procedure, Regulations, Directives, and Recommendations - conflicting views**
- **NB - many contributions reflected a ‘national’ approach; rather than a community approach**



Results of consultation (4)

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- **Discrimination - major concern for many**
- **Should be available to *all* companies as an *option***
 - **But - problems for SMEs, SME standard?**
 - **But - Member State difficulties with optionality?**
- **Tender published for study on discrimination & state aid issues**
- **Member States - should Commission wait for MS initiatives?**



Progress on IAS

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- **Wide interest in a common tax base: IAS work raised the level of debate**
 - **IAS a neutral starting point for further discussions**
 - **Tax/Accounting dependency is key – not just for an IAS derived tax base, but any EU-wide common tax base**
 - **Need to study the range of dependency across the EU**
 - **With pure dependency you cannot have a common tax base unless all companies use IAS**
 - **IAS (& Accounting Directives) will not produce a final tax base, therefore some adjustments will be needed**
 - **Need to study in more detail individual tax principles e.g. depreciation, approach this via study of individual IAS**
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Progress on a Common Tax Base

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- **More research - progress on the accounting front and extension of IAS application will be important**
- **Work via the neutral IAS on the form of the tax base would also be applicable to any form of common base**
- **Allocation mechanism for the EU tax base – more research, to include quantitative modelling**
- **Need more input and support from Member States and business**



Summary – Company Tax initiatives

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- **Background**
- Short term targeted measures – progress report, on 'target'
- Longer Term strategy – slower progress, but it is long term
 - Home State Taxation - SME pilot? - Initiative planned for 2004
 - Common Consolidated Tax Base – IAS starting point? – continued research
- **Company Tax Website**

http://europa.eu.int:8082/comm/taxation_customs/taxation/company_tax/index.htm
