European Business Initiative on Taxation - EBIT

Contribution to the European Commission Workshop
on the CCCTB, 20 October, 2010

Introduction

On behalf of the European Business Initiative on Taxation (EBIT)[1], we would like to offer the following comments on the four papers sent under cover of the letter t to EBIT by Thomas Neale on behalf of the European Commission of 17 September 2010, ahead of the EC's Workshop on the CCCTB on 20 October 2010.

In developing this submission, EBIT has relied more on the practical and daily experience of its members, who are experienced tax directors of multinational enterprises, than on theory.

1. Eligibility tests for companies and definition of a CCCTB group (CCCTB/RD\001\doc\EN)

- **Introduction**

EBIT welcomes the proposal at paragraph 2 that in the event that the test for consolidation is not successfully passed, a taxpayer may still apply the Directive, only for the purposes of determining its individual tax base according to the common set of CCCTB rules.

Presumably this is offered to assuage state aid concerns, as otherwise, companies in Member States participating in the CCCTB which do not meet all of the paragraph 9 eligibility tests for consolidation throughout the qualifying pre-CCCTB period and the relevant CCCTB year would be denied access to the CCCTB base, which depending on all the circumstances, may be more favourable or less favourable (or equal to) the national tax base for that company for the period in question.

EBIT observes that Member States will presumably factor this into their consideration of participation in CCCTB insofar as the tax base of all companies operating in that member state may be opted into CCCTB as opposed only those companies eligible under the consolidation criteria.

- **Eligible companies**

EBIT notes the proposed definition of an eligible company in paragraph 4 by reference to a company established under the laws of a Member State, taking one of the forms listed in an annexe to the CCCTB directive and subject to a corporate income tax system (or other similar tax) in a Member State as listed in the further annexe, or subject to a similar tax introduced subsequently, together with the extension by analogy as regards EU PE's in participating Member State of third country companies.

EBIT notes the currently ongoing Commission consultation on possible amendments to and possible extension of the interest and royalties directive, including the criteria for eligible companies. Insofar as the Commission were to propose, for example, an extension of the eligibility criteria for that directive to, for example, any body corporate constituting a resident for corporation tax or similar tax purposes in the Member State in question, i.e. going beyond

[1] At the time of this submission EBIT members included: AIRBUS, BOMBARDIER TRANSPORTATION, CATERPILLAR, EADS, GE, DEUTSCHE LUFTHANSA, METRO GROUP, MTU AERO-ENGINES, NUTRECO, ORACLE, ROLLS-ROYCE, ROMPETROL GROUP, SANOFI-AVENTIS, SES and TUPPERWARE. EBIT's Members span the following business sectors: aerospace and defence, aircraft engine manufacturers, airlines, earth moving equipment, food, food containers, healthcare equipment, oil, pharmaceuticals, retail, satellite networks, software, and train manufacture. At least one of EBIT's corporate members is represented on the EU Transfer Pricing Forum.

the annexe list approach, EBIT would urge the Commission to consider a similar extension to the definition of eligible company for CCCTB Directive purposes.

As regards paragraph 5, it would appear this should read "For the purposes of the Directive, a company that is not tax resident in the Member State but TO which the Directive would apply would be eligible to opt for the CCCTB in respect of any PE in a member state."

Subject to the above comments, EBIT supports the eligibility requirements as proposed.

- **Conditions for consolidation**

EBIT would welcome clarification from the Commission as to why the threshold for capital and rights to profit is proposed to be set at greater than 75%, whereas the control threshold is proposed to be set at greater than 50% of voting rights.

EBIT would also request clarification of the paragraph 10 requirement for the thresholds outlined to initially be met for nine months, otherwise the taxpayer would be considered to have never been part of the group. Does this require the taxpayer to meet the CCCTB criteria for a minimum of nine months *prior* to that company being eligible for CCCTB consolidation? If so, EBIT queries whether this could be reduced to six months.

Furthermore, paragraph 10 requires that after the initial nine months (or six months) qualifying period, the eligibility thresholds need to be maintained throughout the relevant tax year for eligibility for consolidation. EBIT queries whether a de minimis exception rule should be added. For example, a group may have a controlling stake in a subsidiary which itself has a listing. It could be the case, because of e.g. group treasury activity ,or share buy-backs, that temporarily, the greater than 75% of capital or entitlement to profits test could be temporarily breached, perhaps for as little as a day or so. It would then appear somewhat draconian for that subsidiary to become ineligible for consolidation.

Subject to clarification of the above, EBIT supports the paragraph 9 three-part test for eligibility for consolidation and also supports the thresholds for participation.

- **Group structures eligible for consolidation**

EBIT suggests (paragraph 15) that provided there is an operational exchange of information article in all the relevant tax treaties, a third country headed group owning one or more resident taxpayers in participating Member States be eligible for consolidation if they are directly or indirectly owned by the same ultimate third country company, which has a form similar to that set out in the annexe to the Directive, and the EU resident taxpayers all meet the three-part test and qualifying period requirement.

As regards the second and third examples on page 7 and the example on page 8, EBIT understands that as is expressly stated at the bottom of page 6 in relation to the structure at the top of page 7, the third country parent company would have to have an exchange of information agreement in place in the tax treaties between it and each of the Member States in which the investee companies are situated. This is implied by the question on page 8. EBIT would be grateful for the Commission's confirmation that this is indeed the case.

2. Business reorganisations in the CCCTB (CCCT/RD\002\doc\EN)

- **Pre- consolidation trading losses**

EBIT supports the approach taken regarding the ring-fencing of pre-consolidation tax losses of a company which is opted into a CCCTB group. EBIT notes that the proposed ring-fencing is similar to the treatment of tax losses of US companies prior to their entering into a US Federal Consolidated Return.

- **Hidden reserves**

EBIT notes and endorses the principles behind the proposals in paragraphs 6 to 9 as regards hidden reserves attributable to fixed assets or the proposals in relation to self-generated intangible assets.

EBIT observes, however, that there may be some debate around the five year periods proposed in paragraphs 7 and 9, i.e. why not four, or indeed, three years (as proposed at paragraph 12).

EBIT recalls that the CCCTB election is five years on a rolling renewable basis. Presumably, therefore, this is the basis for selection of the two five year periods?

EBIT would be grateful if the Commission would confirm that the mechanism envisaged at paragraph 7 whereby, for example, a realised capital gain is added to the share apportioned to the group member which held the economic ownership of the relevant appreciated asset at the time it joined the CCCTB group ,is that it would be added to the property factor for the Member State in which the company is located which had the appreciated asset when that company joined the CCCTB group.

EBIT understands that paragraph 9 should read (last line) "...the asset factor of the relevant group member for a period OF5 years."

Subject to the above comments and clarifications, EBIT considers that the five year rule for hidden reserves attributable to fixed assets when companies join the CCCTB group and the proposal to use as a proxy the cost that a taxpayer incurs for R&D, marketing and advertising over the five years which *precede* its group entry as regards self-generated intangibles owned by a company when it joins a CCCTB group are reasonable.

- **Leaving rules**

As regards the leaving rules, EBIT would comment once again that there may be discussion around the paragraph 12 three years after group exit timeline, and the paragraph 13 five years prior period as regards add back of R&D, marketing and advertising costs to the CCCTB consolidated tax base.

Otherwise, EBIT considers that the leaving rules as proposed are reasonable.

- **Business reorganisations within the group**

EBIT presumes that the proposed 'deemed PE' envisaged at paragraph 17 will continue only as far as the CCCTB election remains in place.

- **Hidden reserves**

EBIT considers that a commercial justification exception should be available to the proposed re-attribution of assets envisaged at paragraphs 19 and 20 and the deemed PE envisaged at paragraph 21.

- **Business reorganisations between two or more CCCTB groups**

Other than noting that there may be some debate around the three year time limit envisaged at paragraph 31 as regards disposal of assets held by members of a CCCTB group which becomes part of another CCCTB group within three years after reorganisation, EBIT has no comments about the entering and leaving rules when two or more CCCTB groups reorganise.

3. Transactions and dealings between the group and entities outside the group (CCCTB\RD\003\doc\EN)

- **International agreements and the CCCTB**

EBIT would endorse the principle expressed at paragraph 3, viz, that "to the extent that they (bilateral tax treaties with third countries) may incorporate rights and obligations that are not in line with the Directive, those agreements will not be affected."

As regards paragraph 4, and the acknowledgement that a third country tax treaty concluded prior to the Directive will override the CCCTB formulary apportionment of CCCTB income as regards an EU located PE of, say, a US company, EBIT requests the Commission to consider the position where, for example, the CCCTB formulary apportionment results in a lower than arm's length tax base being attributed to, say, the French PE of a US company, where the French PE is opted into a CCCTB group.

EBIT's understanding of the Internal Revenue Code is that the US will only give credit for foreign tax actually paid, and even then, only if that is the minimum legally payable, having regard to the US concept of non-creditable "voluntary tax".

Accordingly, EBIT considers that the US would only give credit for the actual CCCTB tax paid in, say, a French PE of a US company where the CCCTB tax base allocated to the French PE is less than it would be under arm's length principles.

- **Switchover clause**

EBIT requests the Commission to clarify that the minimum average statutory corporate tax rate envisaged at paragraph 8 is an average of the corporate tax rates only of those Member States participating in CCCTB.

In paragraph 18; EBIT assumes that the reference to "non-taxpayer" in paragraph 18 is to a taxpayer which is not opted into the CCCTB group in question.

Other than the above, EBIT has no comments on this paper.

4. Anti-abuse rules in the CCCTB (CCTB/RD\004\doc\EN)

- **General anti-abuse rule ("GAAR")**

EBIT questions the need for a GAAR, given the suite of six specific anti-abuse rules. In the experience of EBIT members, purposive based GAARs entail considerable work both for business and tax authorities in establishing what is the purpose or, as indeed here, whether the avoidance of tax is the sole purpose of the transaction or series of transactions.

Moreover, whilst, in the event that a GAAR were to be adopted, EBIT endorses the provision of a genuine commercial activities exception, once again, the definition of what constitutes a genuine commercial activity is likely to be the focus of considerable debate.

EBIT would point to the experience of those, mostly common law, countries, which have a GAAR: e.g. Australia, Canada, Germany, Ireland and South Africa, which has not generally been a happy one. In Australia and Canada in particular, there has been much contradictory litigation.

- **Disallowance of third country source interest deduction ("thin capitalisation")**

EBIT would again ask for confirmation that the 40% average statutory EU tax rate envisaged at paragraph 11 is the average of the statutory corporate tax rates only in the participating Member States who participate in CCCTB.

Whilst appreciating that it is difficult for the Commission to comment on the position under enhanced co-operation, EBIT would request confirmation that the "thin capitalisation" provisions aimed at interest paid to an associated enterprise in a third country will not be extended to loans to companies or PEs opted into a CCCTB group from EU Member States which do not participate in CCCTB, if full unanimity is not achieved.

Other than the above, EBIT endorses the envisaged approach to "thin capitalisation" and in particular, the exceptions envisaged at paragraph 14.

- **Switch-over from tax exemption of foreign income to relief by credit**

Again, EBIT would welcome clarification that in the event that not all Member States participate in CCCTB, the 40% threshold will be an average only of the statutory corporate tax rate of participating Member States.

Moreover, EBIT would welcome confirmation that the reference in paragraph 16 to the switch-over from tax exemption to credit if the income flowing into the group originates in a low tax third country would not be extended to other lower tax EU Member States which did not participate in CCCTB.

- **CFC legislation**

EBIT suggests that at paragraph 19(a) the text should read "A taxpayer, by itself or together with its associated companies, holds MORE THAN 50% of the voting rights or..."

Again, EBIT would welcome confirmation from the Commission that, in the event that not all Member States participate in CCCTB, the CFC rules applicable (paragraph 20) would only be as regards subsidiaries resident in a third country and would not be extended to EU non-CCCTB country subsidiaries.

- **Disallowance of the Participation Exemption in share disposals**

EBIT considers these provisions are reasonable.

- **Rules to tackle double deductions in the so-called "Sandwich" cases**

Again, EBIT considers that the requirement for a third country company in the circumstances envisaged to have operative exchange of information provisions in which both companies one and three are located would be reasonable.

- **Rules to avoid a manipulation of the asset factor**

EBIT has already commented about this as regards to the GAAR. It is assumed that the assets concerned are only those within the apportionment factor.

EBIT encourages the Commission in its further consultation efforts on the CCCTB and hopes that the above suggestions are helpful and will be taken into account during the CCCTB Workshop on 20 October 2010. EBIT's Secretariat represented by Bob van der Made and Peter Cussons will be representing EBIT's corporate members during the Workshop and they are happy to discuss EBIT's submission at any time as appropriate.

Yours sincerely,

European Business Initiative on Taxation – October 2010

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