European Commission foreshadows proposal for a Common Consolidated Corporate Tax Base with consolidation element postponed

Executive summary

On 27 May 2015, The European Commission's College of Commissioners¹ held an orientation debate on measures designed to make European corporate taxation fairer, more growth-friendly and transparent.

At the meeting, it was agreed that a “new EU approach to corporate taxation is needed to successfully address tax abuse, ensure sustainable revenues and foster a better business environment in the internal market.”

Focusing on four specific objectives and five key actions, the new approach will be delivered in the form of an action plan by the European Commission (the Commission) on 17 June 2015, and such measures will center upon the re-launch of the Common Consolidated Corporate Tax Base (CCCTB) - but with the consolidation element “postponed” - alongside a number of short-term measures designed to integrate the results of the Organisation for Economic Co-operation and Development’s (OECD) Base Erosion and Profit Shifting (BEPS) project.

The debate orientation paper (the Paper) notes that such measures will also include a public consultation in relation to options for public disclosure of tax information. That consultation will commence on 17 June 2015.
The new action plan will form the second package of tax measures within the Commission’s 2015 Work Program, following the 18 March 2015 presentation of a proposed package of tax transparency measures.\(^2\) In order to enable the delivery of the CCCTB regime, the Commission notes that a proposal for an entirely new Directive will be required.

Reflecting on the meeting, Pierre Moscovici, European Commissioner for Economic and Financial Affairs, Taxation and Customs, said: “Our current approach to corporate taxation no longer fits today’s reality. We are using outdated tools and unilateral measures to respond to the challenges of a digitalized, globalized economy. For fairer taxation and less fragmentation in the Single Market, we need to fundamentally review our corporate tax framework in the EU. Big, small and medium sized companies should be able to benefit from the internal market on an equal footing.”

**Detailed discussion**

**Context to the Commission’s upcoming proposals**

In setting out the context behind their decisions, the Paper delivered by the Commission sets out its belief that current rules for corporate taxation no longer fit the modern context, arguing that “Corporate income is taxed at national level, but the economic environment has become more globalised, mobile and digital. Business models and corporate structures have become more complex, making it easier to shift profits. This has made it more difficult to determine which country is supposed to tax a multinational company’s income.”

The Commission notes that, while the main historic focus of tax developments at the European Union level has been to prevent tax obstacles such as double taxation, it also believes that “as corporate tax planning has become more sophisticated and competitive forces between Member States have increased, the tools for ensuring fair tax competition within the EU have reached their limits.”

In regard to this tax competition between Member States, the Commission sets out its view that Member States have progressively lowered their corporate tax rates in order to protect their tax bases and to attract foreign direct investment. In turn, the Commission believes that some governments have also increased the tax burden on less mobile companies and on labor, undermining the efficiency and growth-friendliness of their tax systems. Small and Medium enterprises are particularly affected in this respect, notes the debate orientation briefing.

**Developing a “new approach” to corporate taxation**

The Commission argues that in order to address these issues, a new action plan should propose a new approach to corporate taxation in the European Union. Such an approach, the Commission believes, would ensure that corporate taxation can be growth-friendly, fair and transparent. The Commission further notes that such an approach will assist them to build on integrating the results of the BEPS project at the EU level.

The Commission outlines how the new approach would pursue four specific objectives:

- To re-establish the link between taxation and where economic activity takes place
- To ensure that Member States can correctly value corporate activity in their jurisdiction
- To create a competitive and growth-friendly corporate tax environment for the EU, in line with the recommendations of the European Semester
- To protect the internal market and secure a strong EU approach to external corporate tax issues, including measures to implement OECD BEPS, to deal with non-cooperative tax jurisdictions and to increase tax transparency.

The Commission proposes five key action areas designed to achieve the four objectives, each of which may have significant implications for both national tax systems and businesses operating in Europe. The five actions, described verbatim as they are in the Paper, are as follows:

- Re-launching the CCCTB by making it mandatory, while developing a staged approach for its implementation, implying in particular postponing consolidation
- Bringing taxation closer to where profits are generated, in particular by considering how to ensure effective taxation
of profits, including through improving the EU framework for ensuring that transactions within a cross-border group are taxed based on a comparable market price (transfer pricing) and linking preferential regimes to where value is generated.

- Improving the tax environment for business, in particular by enabling businesses to offset losses from their tax payments, wherever in the EU those losses occur; and by improving existing arrangements to settle divergences between different Member States about double taxation.

- Making further progress on tax transparency, in particular by ensuring a more common approach to third country non-cooperative tax jurisdictions and by launching a public consultation to prepare the Impact Assessment on options for public disclosure of tax information.

- Improving EU coordination tools, in particular by improving Member States’ coordination on tax audits and reforming the Code of Conduct Group and Platform on Tax Good Governance.

As the Commission notes, most of the actions are linked in some form to the re-launch the CCCTB project and the need to complement such re-launch with a number of short term measures which will “further integrate the results of the BEPS project at EU level, to ensure that profits generated in the EU are taxed at the place where actual activities take place and to improve the tax environment for business.”

In detailing the above actions, the Commission sets out the view that, in terms of immediate priorities, measures to re-launch the CCCTB as well as the question of effective taxation of profits in the European Union deserve particular attention. This would seem to point to the work of the Commission in this area continuing for some time into the future.

A more detailed look at the CCCTB

The Paper notes that the current proposal for a CCCTB for Europe has been discussed for more than four years without sufficient progress. In fact, the proposals in their current form find their genesis in 2001, with debate on the possibility of such a system arguably harking back as far as 1998.

With the consolidation element of a CCCTB being a key barrier to progress for many Member States due to the difficulty of accurately apportioning profits, the Commission notes that a widely considered view is that the only way to re-launch the possibility of a CCCTB is to postpone consolidation, while making the common tax base element mandatory. While no specific definition of “postpone” is given in the debate orientation paper presented to members of the College of Commissioners, the move from an optional system (under the 2011 CCCTB proposal) to a mandatory system is a significant change.

The Commission does note, however, that postponing consolidation implies that, until its introduction in the future, losses may be carried forward and offset against current and future profits only within the same country. To partly compensate for this delay of consolidation, the debate orientation paper calls for the Commission to propose the possibility for cross-border entities to offset profits and losses they make in different Member States. To ensure that one Member State does not definitely carry the burden of losses incurred in another Member State, a mechanism to recapture these losses once the entity is profit-making again.

The debate orientation paper notes that in parallel to the CCCTB work, the EU should, wherever possible, try to make concrete progress towards agreement on specific actions to limit base erosion and profit shifting, in line with OECD work on those issues. Here, the Commission refers to BEPS Actions 3 (strengthening controlled foreign company rules), 4 (limiting base erosion through interest deductions) and 7 preventing artificial avoidance of permanent establishment in particular. Work on each of these BEPS action items continues at the OECD and consensus among countries continues to be difficult to secure.

The Paper additionally calls for work to continue on improving the EU framework on transfer pricing rules and on preferential regimes such as patent boxes. On neither point is discussion made of how to align with related activities at the OECD. Finally, the Paper notes that, in order to maintain momentum and to capitalize on agreements in the context of the OECD BEPS project,
the existing CCCTB proposal should continue to be the vehicle to work on solutions for such individual issues. In effect, this means that, once the OECD releases final BEPS recommendations ahead of the November G-20 Leaders’ meeting in Turkey, the Commission will develop a new CCCTB proposal once all procedural requirements are complete. Only at that point will the 2011 proposal be withdrawn. Such an approach, the Paper argues, would “respond to demands to turn the broad OECD-level agreement into a more concrete common EU approach which is compatible with EU law and the Single Market.”

The effective taxation of profits
As the Paper notes, alongside a new CCCTB proposal, a second priority of the Commission is to identify and implement additional measures to prevent base erosion and profit shifting due to low effective taxation. Here, the Commission notes that neither the OECD’s BEPS project nor the 2011 CCCTB proposal includes specific actions to address the issue of low effective taxation.

In seeking to illustrate their arguments against low levels of effective taxation (and “without questioning the prerogative of Member States to apply corporate tax rates they deem to be appropriate”) the Paper sets out “EU law prevents Member States from taxing certain benefits attributed to an entity established in another Member State even if the corporate tax applied in that Member State is extremely low.” While not providing any definition of what does or does not constitute an extremely low tax rate, the Paper uses the example of the Interest and Royalties Directive, where the source Member State is prevented from levying any withholding tax on royalty payments even though in the recipient’s Member State such payments fall under a special patent box regime and are taxed at an “extremely low” tax rate (if any).

The paper sets out that, while this is a topic of significant concern to the Commission, further reflection will be needed on the precise nature and scope of the issue and on the most appropriate ways to address it. In that regard, it remains to be seen whether the proposals due on 17 June will include detailed measures in this area. Should they not include such detail, this will be an important work stream for business to continue to monitor.

While some of the actions set out in the Paper require greater future definition from the Commission, the developments in respect to tax transparency are perhaps more concrete and reflect growing demands from some commentators, as well as growing political pressure, for data to be made public. Here, the Commission will launch a public consultation to prepare an impact assessment on options for public disclosure of tax information. The Paper does not make it clear whether this transparency involves publication of tax data from the Financial Services sector (under the CRD IV reporting requirements) or more widely, by all groups. Further clarification on 17 June will be welcomed.

Implications
The European Commission feels that the CCCTB, first without consolidation and then potentially with it at some point in the future, would better align the 28 EU Member States’ corporate tax rules, both to ease administrative burdens on countries, and perhaps more importantly at the current juncture in the “fair tax” debate, to reduce what it feels are opportunities for some companies to take advantage of the differences in national tax rules.

While any proposal that would potentially make 28 different tax systems more similar to one another may seem a positive step for companies who are dealing with high levels of uncertainty and inconsistency, as multiple studies have evidenced, the proposals – at least in their 2011 form – were seen as highly controversial to some countries and the new proposal also may face similar opposition. In addition, many countries may be concerned that, even without the consolidation element, the carryforward and offset of losses against current and future profits only within the same country may put them on an unavoidable path to a full CCCTB.

More widely, the Commission also will have to address significant variances between the tax bases of different EU Member States. While not insurmountable, this will add significantly to the complexities of the project and it may therefore be assumed that such complexities will take some time to work through in advance of any potential adoption
by Member States. In this regard, the priorities of Member States differ substantially. Both Member States and business will also likely give much consideration to the Commission’s public consultation on options for public disclosure of tax information. In this regard, it is noted that OECD proposals for the exchange of country-by-country reporting data among countries currently call for no public disclosure of the data. Potential future differences between the OECD and European Commission approaches may leave European Union businesses at a competitive disadvantage, depending on the decisions made by each body, as well as the timing of those decisions. Businesses active within the European should therefore reinvigorate their efforts to monitor and assess European Commission developments in the tax area, including full assessment of where any losses may currently sit and what inputs they would like to have into the public consultation on tax transparency.

Endnotes

1. The Commission is composed of the College of Commissioners of 28 members, including the President and Vice-Presidents. The Commissioners, one from each EU country, are the Commission’s political leadership during a 5-year term. Each Commissioner is assigned responsibility for specific policy areas by the President.

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