



**EUROPEAN COMMISSION**  
DIRECTORATE-GENERAL TAXATION AND CUSTOMS UNION  
Analyses and tax policies  
**Analysis and Coordination of tax policies**

Brussels, 5 May 2006  
Taxud E1, OP

**CCCTB\WP\035\doc\en**  
Orig. EN

## **COMMON CONSOLIDATED CORPORATE TAX BASE WORKING GROUP (CCCTB WG)**

### ***Issues related to group taxation***

**Meeting to be held on 1st June 2006**

Centre de Conférences Albert Borschette  
Rue Froissart 36 - 1040 Brussels

**WORKING DOCUMENT**

## **I Introduction and purpose of the paper**

1. In its Communication issued on 05 April 2006 (COM(2006) 157), the European Commission expressed its preference for consolidation of the common tax base from the beginning and committed itself to start the technical work on the consolidation of the common tax base in 2006. Although ambitious, the Commission considers that this approach will bring the greatest benefits to the Internal Market and contribute most to the Lisbon goals.
2. The alternative of a two-stage process, first a common base without consolidation and second a consolidated base, does not address the problems associated with a lack of cross-border loss relief, nor does it simplify the existing difficulties of transfer pricing. Additionally, unless work is directed towards a consolidated base there is a danger that consolidation may be made more difficult in the long term if, for example, a lower level of common treatment of certain structural elements, or methodologies, is accepted. There are also fewer benefits in simply introducing a 'common' base to operate independently in each Member State which might, over time, revert to twenty five different bases as national interests prevail over the interests of the internal market as a whole. Even if MS were to delay consolidation to a second stage, the designing of a tax base able to be consolidated is advisable in order to avoid the possibility of having to reconsider certain structural elements of the tax base in order to make consolidation possible.
3. However, the most important reason for beginning work on consolidation now is the growing number of demands to discuss consolidation during both recent Working Group and sub-group meetings. It is no longer an issue which can be 'put to one side' for later consideration as experts are rightly pointing out that both the definition of a group and the precise mechanics of how consolidation would work are critical to discussions of other structural elements and the work on international aspects.
4. Work on the mechanism to share the consolidated base between Member States will also be necessary. This can be carried out concurrently as the technical issues are relatively independent, and from a resources point of view will demand different expertise and skills. Indeed some preliminary work has already been carried out internally by Commission staff on possible mechanisms such as formula apportionment and a DG Taxation and Customs Union 'Taxation Paper' 'The Delineation and Apportionment of an EU Consolidated Tax Base for multi-jurisdictional Group Taxation' is currently being finalised.
5. The aim of this working document is to give a general overview of principles and issues to introduce the subject in the CCCTB WG and to decide whether the subject requires further analysis in a new subgroup.
6. The "Draft Work Programme" (CCCTB/WP/003) identified the technical implications of partial implementation by MS (enhanced cooperation), and the extent to which the CCCTB is compulsory or optional for companies under the heading "application issues" and suggesting these should be addressed only after the

initial discussions on the structural elements. Thus, this working document concentrates on the hypothesis that all 25 MS participate in the CCCTB (issues related to implementation by less than twenty five MS and/or use by some, but not all, companies will be addressed at a later stage in line with the Work Programme).

7. The question over whether the consolidated accounts prepared in accordance with IAS 27 (consolidated and separate financial statements) may be used as a starting point for the CCCTB was raised in the 2003 DG TAXUD consultation<sup>1</sup> on '*The application of IAS in 2005 and the implications for the introduction of a consolidated tax base for companies' EU wide activities.*' It was confirmed that for a number of reasons the basic accounting approach to consolidation was not appropriate for taxation, for example the treatment of minority interests in the profit and loss account. In addition as the accounting consolidation includes all of a group, both EU and non EU activities, it would not be possible to start from the consolidated accounts without adjustment and the scale of adjustments would be such that there would be no advantage in starting from the consolidated figures. However, some of the IAS 27 criteria and principles for the determination of the group to be consolidated may constitute a useful reference point, and IAS 27 provides some useful terminology and definitions in a range of languages.
8. This working document deals with the following issues :
  - **distinction between loss relief and consolidation**
  - **definition of a 'group' / companies to include / choice or not**
  - **method for consolidation / tax base calculation**
9. It should be stressed that each individual company should continue to be subject to tax on its share of the consolidated base in the MS where it is located and MS would continue to apply their tax rates. However, when several companies of the same group are located in one MS, this MS is free to decide whether or not only one of these entities should actually pay the tax on behalf of all the group companies.
10. This working document uses the terminology "consolidation", "consolidated group", "consolidated income" in a way that might be different from the current use by some MS legislation. For the CCCTB purposes, consolidation implies that one single tax base is determined for a group of entities and even though tax would be charged at the level of each entity it would be on the share of the consolidated base calculated in accordance with the 'sharing' method, rather than the current individual income calculated on the arm's length basis.

## **II Distinction between loss relief and consolidation**

---

<sup>1</sup> Available on the following web-page:

[http://europa.eu.int/comm/taxation\\_customs/common/consultations/tax/index\\_en.htm](http://europa.eu.int/comm/taxation_customs/common/consultations/tax/index_en.htm)

11. As Members of the Working Group are aware, the Commission Services are currently working on a targeted measure for cross-border loss compensation and a Communication will be issued later this year. However, it is important to recall the differences between these two approaches.
12. The CCCTB as a comprehensive approach goes beyond the issue of just cross-border loss compensation, since it also addresses the harmonisation of the tax base, the elimination transfer pricing problems and the reduction of compliance costs. The CCCTB requires that the tax base is common across the EU and consolidates the profits and losses of the companies participating in a group to calculate a single tax base for 'sharing'.
13. In contrast, the ongoing work toward a targeted measure regarding cross-border loss relief does not necessarily require harmonisation of the tax system or tax base. The measure could in principle be implemented by a single MS (e.g. state of residence of the controlling entity) and no action would be required by the state of residence of the loss making subsidiary. Some MS have already introduced measures of this kind.
14. Group taxation approaches are based on the assumption that each corporate group forms an economic unit and therefore should be treated as if it were a single company<sup>2</sup>. In doing so, a tax system aims to provide (to some extent) businesses the same treatment when carried on through separate dedicated legal entities as businesses operating through separate divisions of one single legal entity. The ambition of the CCCTB is to extend this approach in the case of groups operating in more than one MS, both through subsidiaries and through permanent establishments, so that a group of companies can determine one single tax base to be shared according to an apportionment key between participating MS. Each MS would then apply their tax rate to their share. The implementation of this comprehensive solution by all 25 MS would remove the need for a specific cross border loss relief scheme.

### **III Definition of a group**

15. In practise, a tax group scheme sets out rules in relation to the definition of a group. The definition of a group can be based on two, or a combination of the two,

---

<sup>2</sup> The term “consolidation” in its original meaning is used in accounting for the aggregation of the individual financial statements of all group members with elimination of all intra-group transactions affecting the profit and loss account.

A “genuine tax consolidation” as used for Dutch tax purposes or for the Common Consolidated Tax Base (CCTB) means the aggregation of all individual pre-tax results of group members with elimination of all intra-group transactions; the tax base is the overall net result of the group. Genuine tax consolidation therefore is only applicable within the framework of one single tax base.

The term “pooling” is used for the aggregation of individual tax results of various group members without the elimination of intra-group transactions being a prerequisite. The term “pooling” therefore also includes a genuine tax consolidation. The term “pooling” is consequently only used in reference to one single tax base.

different approaches – a legal approach, an economic approach or a combination of both.

16. A legal definition relies on a legal ownership threshold which may be based on direct ownership only, or also be extended to include indirect ownership. For example if the ownership threshold were 90% this might include only direct subsidiaries held 90%, or include subsidiaries where the combined group holding of several group companies reached 90% through the addition of several holdings via several levels of companies.
17. In contrast, under the economic approach, all the entities which are commonly controlled and which are related to one another as a single economically integrated business would be included. This approach implies as a first criterion ownership control. Then a second set of criteria related to a certain degree of operational and/or economic interdependence between the group units must also be met. These economic relationships could be defined in a number of ways. This second approach could introduce subjectivity and thus create additional practical difficulties and complexities for the definition of a group.
18. Both approaches require clear definitions and criteria to identify which entities are part of a group, and which are not. The definition will also have to clarify whether companies and permanent establishments who are connected only via a parent in a foreign state (ie outside the EU) would be considered to form a group. This specific question has already been raised in discussions in Sub-Group 4 (a non-resident parent with a subsidiary in MS 1 and permanent establishment in MS 2).
19. **Eligible entities** may include any legal entity effectively subject to corporate income tax in one of the EU jurisdictions and thus which does not benefit from any exemption. If entities without any legal personality, who are currently liable to corporate income tax are considered to be within the scope of the CCCTB (entities entitled to fall in the scope of the CCCTB will be discussed separately) then whether they should be eligible for a group regime will have to be addressed (associations, unincorporated entities, transparent entities etc).
20. **Setting legal shareholding requirements** requires the setting of a threshold for the inclusion of subsidiaries in a group and rules for calculating the threshold (direct, indirect etc). Most group regimes currently applied by individual MS in the EU require a relatively high level of shareholding by the parent company for example from 75 % to 95 %. However, some which operate on a proportional basis require only a 50 % shareholding. Companies generally have to maintain the required shareholdings throughout the tax period.
21. Regardless of the level of percentage holding that is required to be part of a group, it will be important to clarify exactly what type of ownership rights would qualify. For example when both voting and non-voting shares are issued, or there are two or more types of share issued which give different rights to the shareholder, or when entities do not have formal shares at all (for example in the insurance sector). The treatment of financial instruments which give rise to future rights to own shares will

also have to be examined, for example debt instruments convertible into shares, or options to purchase shares etc.

22. Rules for calculating the level of the holding will also need to be established to clarify the extent that indirect interests are to be taken into account in complex group structures. In addition to these more basic issues consideration will also have to be given to anti-avoidance measures. Any strict legal threshold creates the opportunity for a group to deliberately include or exclude specific group companies for tax purposes and some form of protective measures may be necessary. For example, requiring 100% ownership is straightforward in that there are no minority interests to be considered, but it is relatively easy for a group to exclude a subsidiary from the group by selling a single share to a third party.
23. Some of the criteria and principles set out in IAS 27 (for example paragraph 13) could be usefully examined to build the common definition of control of the parent company over a subsidiary (without necessarily keeping the threshold mentioned in the accounting standard). IAS 27 extends the criteria to cover some situations focusing on practical influence rather than ownership. Thus, under the following circumstances, control is deemed to exist even though the parent company does not hold the minimum percentage of voting rights: agreement with other investors, power to govern the financial and operating policies, power to appoint or remove the majority of the members of the board of directors or equivalent governing body or power to cast the majority of votes at meetings of the board or equivalent governing body.
24. Consideration should also be given to which **entities should be entitled to be the parent company of the group**. Some current group taxation schemes require that the parent company not be controlled itself by another company so only the company at the highest level of the shareholding chain (the ultimate parent company) is entitled to form a group. Adopting this approach would potentially exclude any group controlled from outside the EU which the Commission Services do not recommend.
25. In respect of **which qualifying subsidiaries (for example those which meet the legal ownership test) should be included in a consolidated group**, it would seem sensible to apply an “all or none” principle. This would limit tax planning opportunities ('cherry-picking') and ensure the consistency of the consolidation (i.e. calculation of an income reflecting the economic profile of the group). Some existing schemes include some flexibility which for example allow groups to leave out very small entities (although this is to avoid re-calculation of the tax base which would not be necessary under the CCCTB as all companies would use CCCTB rules). Or they may require the inclusion of significant entities which are just below the qualifying threshold, for example a 45 % subsidiary might be required to be included in a group even though the threshold were 50% as the subsidiary constitutes a significant division of the group business.
26. Rules will also be required for newly created or newly purchased entities as regards the date when they are to be included in the group. This issue could be connected to

the administrative issue of the necessity for identical tax periods for entities belonging to the same group and the possible flexibility for the year when they are included in group. Another option could be to divide the tax period and include in the consolidation only the relevant part of the profit earned during this period or to consider that the inclusion enters into force for the consolidation purpose only on year following the year of purchase/creation, or there could be a requirement to own the company for a minimum period. Similar considerations apply to when companies leave a group.

27. The inclusion of entities in the same group what ever **activity** they carry on should be discussed as well. This issue is connected with the possibility of some assets being subject to a different tax treatment depending on companies' activities, for example if there were specific rules for banks or insurance companies and whether in this case they should be consolidated. An examination of the specific activities of subsidiaries could also arise if economic criteria were part of the group definition. For example a group with two quite different unconnected activities might not satisfy criteria based on a requirement to be economically integrated (such an approach is sometimes referred to as 'unitary' taxation).

#### **IV Methods for consolidation / tax base calculation**

28. Currently, most EU MS apply some form of group taxation which enables national (ie domestic) companies to offset profits and losses. However, the actual solutions and techniques differ significantly. Only a few extend this to subsidiaries in other States.
29. In some MS consolidation of income and expenses or profits and losses of members of the group is not allowed for corporation tax purposes, but the members of the same group can benefit from a special relief under which it is possible to shift profits or losses amongst companies belonging to the same group (for example in Cyprus, Finland, Ireland, Latvia, Malta, Sweden, and United Kingdom). This type of group taxation scheme enables the group to compensate losses of one company against profits of the other in the current tax period.
30. Most MS require all members of the group to calculate their own tax bases separately first and then the taxable profits and tax relevant losses of fiscal group members are aggregated. For example the German model requires the subordinated members of the group to transfer their profit or loss by mean of special "pooling" agreement to the head company. This so-called "Organschaft" model stands somewhere in between the consolidation of profits and losses and group relief models.
31. As a further variation consolidation can apply in direct proportion to the shareholding or as full consolidation (100 % of profit or losses of the subsidiary disregarding the effective shareholding of the parent company). Current national and international schemes by the same state can also differ in this way. For example the tax base of the national fiscal consolidated group can be calculated on the entire (100%) basis, disregarding the amount of the participation held by minority

shareholders, whereas the tax base of a worldwide consolidated group provides for a proportional aggregation, based on the proportion of the shareholding in the foreign subsidiaries (for example the French system of consolidated profit).

32. Finally, in some MS, no special tax treatment for groups of related companies is available (for example in Belgium, Czech Republic, Greece, Hungary, Lithuania and Slovakia). These MS treat all the members of the group as completely independent taxpayers. Separate legal personality is a fundamental principle. The losses of one group member cannot be set off against the profits of another group member under any conditions.
33. The precise method need not change the final result as the tax liability does not change systematically whether the profits and losses are compensated through consolidation or through deductible contributions or loss relief among group members. The separate legal personality of all members of the group for corporation tax purposes is preserved in all the states. Tax residence is determined in respect to each member of the group even if a consolidation scheme is applicable.
34. Moreover, in existing group regimes where the consolidated income is the aggregation of profits and losses of the entities of the group determined on an entity by entity basis, each entity of a group takes into account all transactions, **including intra-group transactions** and to some extent apply the arm's length principle even in the case of intra-group transactions. However, profits and losses arising from internal transactions may be subsequently eliminated (permanently -or provisionally i.e that it could be added back to the group taxable income when the concerned subsidiary leaves the group) for the computation of the consolidated income.
35. As regards the actual tax payer either the parent company may be the single tax payer entity for the whole group or each entity may be responsible for its own tax liability.
36. As the CCCTB aims to allow cross border consolidation of profits and losses and at the same time reduce compliance costs arising from transfer pricing rules, some differences from existing techniques and practices may be necessary for the CCCTB.
37. Two main approaches of how to eliminate intra-group transactions can be identified, although there are obviously a number of detailed choices to be made about the form of CCCTB consolidation.
38. In the first approach each group company would continue to prepare its tax base calculation in the traditional manner, but in accordance with the new CCCTB rules. However, every intra group transaction would be ignored when calculating the tax base. The tax bases would then be consolidated. Companies could price intra-group transactions as they currently do, but would not have to justify transfer prices for tax purposes; although local company accounting rules might still require a particular policy for accounting. In the tax base there would not be a full record of

intra-group transactions in each company. For example goods purchased by A, sold to B, then sold to C, then sold to a third party would be reflected as costs in A (the initial costs), nothing in B and income in C (the third party income). Overall the consolidated base would include A's costs and C's income.

39. In the second approach each group company would again prepare its tax base in the traditional manner, but all intra group transactions would be recorded at cost. This would remove intra-group profits on such transactions but preserve an 'audit trail' in the tax base. Companies would no longer have to justify transfer prices for tax purposes. In the above example the result would be the same but the consolidated base would include A's costs, A's income from sale to B at cost, B's cost and income from sale to C at cost, C's cost and income from sale to third party. This would require additional work in that transactions would have to be valued at cost but would preserve information through the chain of companies in their tax bases.
40. The first approach is conceptually simpler but consideration should be given to the implications for any subsequent requirement to provide arm's length data. For example when a company is sold or if internal comparables are requested for the purposes of assessing arm's length prices for the purposes of those transactions to connected companies who are not within the CCCTB group. This could be transactions with EU group companies which do not meet the CCCTB group criteria, or with group companies in third countries outside the EU, where arm's length transfer pricing will remain the norm.
41. In addition two main types of intra-group transactions exist, (i) concerning trading transactions - the sale of goods from one group company to another for eventual sale onto a third party (with or without additional work being carried out before final sale) and (ii) the sale of 'capital' assets which are being depreciated for tax purposes by a group company and are then sold or transferred to another group company for further use (and continued depreciation). Each possibility will have to be considered in detail but it is possible to outline the main points as follows.
42. As regards intra-group transactions in assets which are being depreciated it would seem preferable to record in the tax base the transactions at the 'tax written down value' (ie cost less tax depreciation to date) at each transfer to ensure that the tax depreciated value of each asset is recorded in each individual company to ensure that any third party sales can be correctly reflected and any necessary tax audit work carried out locally. This does not seem so necessary for trading transactions hence it may be useful to distinguish between these two types of intra-group transactions.
43. Consideration will also have to be given to the treatment of minority interests if 'full consolidation' is implemented at less than the 100% ownership level. For example a third party shareholder might question why a company has to pay tax when the previous year it made losses, which were absorbed by other group companies in the consolidation process.

44. The Commission Services plan to present some examples to illustrate the possible methods at the Working Group meeting. However, further detailed work in a sub-group is strongly recommended. In order to prepare for the Working Group and for subsequent work experts are invited to consider the following questions and to raise any additional points which they would like to have considered. Although written responses are not expected before the Working Group meeting experts will be invited to respond in writing soon after the meeting.

### ***Questions to experts of the working group***

***Comments on the following issues are requested, experts may find it helpful to make general comments, or prefer to answer the specific questions (or a mixture of both):***

#### ***Issues:***

##### ***Definition of the Group:***

***Legal***

***Economic***

***Mixed – ie legal and economic, including 'unitary' approach***

***Types of eligible entity***

***All eligible entities to be included or not ('cherry picking')***

***Approach to anti-avoidance regarding threshold manipulation, ie deliberately placing a company just above or below a threshold requirement***

##### ***Method:***

***Treatment of intra group transactions***

***Minority Interests***

***Companies joining and leaving the group***

##### ***Specific Questions:***

***(i) Do experts consider that the definition of a group for the CCCTB purposes should be based on the ownership of shares or be based on economic criteria or on a combination of these two approaches?***

***(ii) Do experts who favour the ownership approach (as a single criterion or together with the economic criteria) consider that only voting rights should be taken into account or do other control criteria such as the IAS 27 criteria also have to be taken into account? Do these experts favour a specific shareholding threshold and why?***

***(iii) Do experts who favour the economic approach (as a single criterion or together with the ownership criteria) want to put forward relevant criteria for this economic independence to be considered for the definition of a group?***

***(iv) Do experts agree that only legal entities subject to corporate income tax should be allowed to be included in a group?***

*(v) Do experts consider that special requirements should apply for the parent entity (especially as regards its shareholders)?*

*(vi) Do experts agree that the consolidation in the CCCTB should apply the "all or none" principle? If not, why?*

*(vii) Which rules should be applied as regards newly created or purchased subsidiaries and why?*

*(viii) Do MS agree that all subsidiaries should be included in a group regardless of the connection between their respective businesses? If not, why?*

*(ix) Do experts favour proportionate consolidation or full consolidation and why?*

*(x) Which type of treatment do MS envisage as regards intra group transactions?*