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# **PLATFORM FOR TAX GOOD GOVERNANCE**

**Addressing the remaining cases of double taxation in the single  
market: means to foster arbitration**

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Contact:  
Secretariat Platform, Telephone (32-2) 29.55.762  
E-mail: [taxud-platform@ec.europa.eu](mailto:taxud-platform@ec.europa.eu)

## **A. INTRODUCTION**

1. This issue note refers to the current work undertaken by DG TAXUD to address the unresolved cases of double taxation that still exist in the single market. In order to collect evidence illustrating the problem, DG TAXUD conducted a public consultation in 2010 with the title ‘Double taxation conventions and the internal market: factual cases of double taxation’<sup>1</sup>. Later, the Commission adopted a Communication in 2011 “Double Taxation in the Single Market” COM (2011) 712 where it concluded on the need to take actions against international double taxation. Since then, DG TAXUD has continued its work to analyse the problem and evaluate the tax policy options that could better help to solve them. In December 2012, a Fiscalis Seminar dedicated one of its modules to international double taxation. As part of the seminar a questionnaire was circulated to the Member States (MS) on their practice in eliminating double taxation and on their experience in mutual agreement procedures (MAPs) to solve conflicts in the interpretation of double taxation treaties (DTCs). In addition, Working Party IV of the Commission held meetings with Member States’ delegates and with stakeholders to discuss this issue in April 2013. Subsequently Ernst & Young (the EY study) carried out a further study for DG TAXUD for the identification and description of the most frequent instances of double taxation. There have also been significant developments in international taxation on a wider scale as the OECD BEPS project has developed and the Action Plan endorsed by the G20 in September. As states begin a coordinated campaign to tackle base erosion and profit shifting the need to ensure that double taxation is also tackled remains to ensure that taxation is levied in a fair and transparent manner.
2. DG TAXUD has used all this information to work on an impact assessment to offer support to policy makers in their decision making process. It identifies, describes and measures the size of the problem and evaluates the advantages and disadvantages of the different alternatives to solve the problem. Currently there is a great deal of qualitative data available but comparatively little quantitative data. The 2010 public consultation and the EY study give some quantitative data but this is relatively limited and insufficient as formal statistical data. In addition, a significant number of the reported cases were on transfer pricing which is already covered by the Arbitration Convention and is the subject of separate on-going monitoring work by the Joint Transfer Pricing Forum.

## **B. DOUBLE TAXATION IN THE EU SINGLE MARKET**

3. DG TAXUD work has confirmed that cases of international double taxation on income (transfer pricing cases excluded) in the EU remain. This evidence was collected through both a general public consultation and work carried out by Ernst and Young for the Commission. These fall into two main categories. The first category is linked to problems in the interpretation or application of DTCs that result in conflicts of qualification. This is

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<sup>1</sup> [http://ec.europa.eu/taxation\\_customs/common/consultations/tax/2010\\_04\\_doubletax\\_en.htm](http://ec.europa.eu/taxation_customs/common/consultations/tax/2010_04_doubletax_en.htm).

reflected in the growing number of MAP cases, as reported in OECD statistics, combined with the lengthy duration of these procedures (average of two years reported in 2012). This creates doubts about the effectiveness of the DTC system to resolve legal disputes in a timely and cost efficient manner and as states are not bound to reach an agreement it could be argued there is no effective dispute resolution mechanism.

4. The second category concerns cases where either there is no DTC applicable to the case – either because the bilateral relation is not covered by a DTC or the income or transaction is not covered by it (exit taxes, triangular situations, foreign losses), or the credit method to eliminate double taxation has technical limitations impeding its full application.
5. In summary there are conflicting interpretations of DTCs which could be addressed through more effective tools to ascertain how DTCs should be applicable to particular cases. For this purpose, arbitration as provided for in the Arbitration Convention has proven to be an effective tool. However, there are a number of cases where there is no adequate legal response. This is the case if there is no DTC applicable and, in its absence, the domestic relief measures are insufficient to guarantee a satisfactory elimination of double taxation. This could be addressed through rules distributing taxing rights between MS or providing efficient methods to eliminate double taxation.

#### **C. TAX POLICY OPTIONS ADDRESSING DOUBLE TAXATION AND THEIR EVALUATION**

6. Although quantitative evidence remains limited DG TAXUD considers a number of tax policy options for achieving the envisaged objectives should be evaluated. The basic options were discussed with stakeholders in April 2013 but have been refined a little and are therefore reproduced below:
  - Option 1 – Not taking any action which would leave the solution of the problem to the uncoordinated response by the MS through the closing of the DTCs network or unilateral relief measures. This may worsen the current situation given the expected increase in cross-border capital flows. At the same time, the EU and the OECD projects to tackle international tax avoidance and abuse (respectively, Action Plan to strengthen the fight against tax fraud and tax evasion, COM (2012) 722, and Base Erosion and Profit Shifting) may lead to new and complex tax measures which could disallow the application of DTCs in cases. New legal conflicts may arise in this regard leading to double taxation.
  - Option 2 - Recommend the MS to renegotiate their DTCs in order to include an arbitration clause and thereby ensure that MAPs lead to a binding solution. Agreement in the ECOFIN Council could lead the coordination of the bilateral negotiations through a model protocol and Fiscalis Seminars could contribute to the proper use of this legal remedy. It could offer solutions to many of the identified cases of double taxation (108 out of 219). The cost of the arbitration procedure to address a particular case is estimated at approximately €15.000, including the fees of professionals, allowances and mission costs and those of running a secretariat.

- Option 3 – Propose EU legislation – a directive - which would provide for an arbitration clause with the aim to be solving disputes where MS cannot agree on the application of DTCs: where there are disparities in the interpretation of a DTC between the contracting States they would try to solve through a MAP and during a maximum period of two years; if no solution is found in that period, the taxpayer may request the case be submitted to an arbitration panel in charge of proposing a solution solving the case. This would lay down a uniform procedure throughout the EU and also cover cases involving more than two MS. This initiative would solve a similar number of cases as option 2 to which we should add triangular cases (only 1 documented case).
- Option 4 - Propose EU legislation to oblige the residence State to eliminate international double taxation through exemption or credit where such obligation does not arise from the applicable DTC or the unilateral measures. This would offer a solution to some of the documented cases (84 out of 219). However, this option for choosing between exemption and credit as a method for double tax relief could be considered to be too great an interference in MS' tax policies.
- Option 5 - Propose EU legislation which should distribute taxing rights between the source and residence States and eliminate double taxation in the residence State where taxing rights are shared. This solution would reduce double taxation and compliance costs to a larger extent than option 4 since EU legislation would coordinate the source and residence rules (it would cover 99 cases in total). However, there are risks of legal conflicts in the interpretation of the rules distributing taxing rights. This solution would have an impact on the distribution of taxing rights and would interfere with the MS tax policy as regards DTC – as for Option 4 it could be considered to be too great an interference in MS' tax policies.

#### **D. ISSUES FOR DISCUSSION AND FOLLOW UP**

7. The Commission is considering action in the next few months. However, the restricted number of documented *quantitative* cases causes some concern.
8. On the basis of the above analysis, options 2 and 3 are probably the most realistic as arbitration would resolve most of the cases of double taxation. Options 4 and 5 go further in that they could have important implications for MS tax policies. Member States and stakeholders have already been consulted on several of the issues but there remains some doubt over whether or not all the available quantitative data has been made available. This has implications for the solution and type of measures to be proposed.
9. Given the range of expertise amongst Platform members we should like to discuss a number of specific points to enable us to complete our work in this area.

- 1) Do Platform members consider that the problem is sufficiently important for Community action?**
- 2) Which is the preferred option of the Platform members? Do Platform members have a strong position supporting a particular action? Why?**
- 3) Platform members are requested to submit any further quantitative information on double taxation cases (other than those on transfer pricing)**

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