

COLLOQUIUM

THE TAXATION OF CORPORATE GROUPS: STRUCTURAL ISSUES AND LATEST DEVELOPMENTS

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Summary

1. Structural issues:

- a. The nature of the tax problem (Closed and Open Setting Frameworks)
- b. Policy guidelines

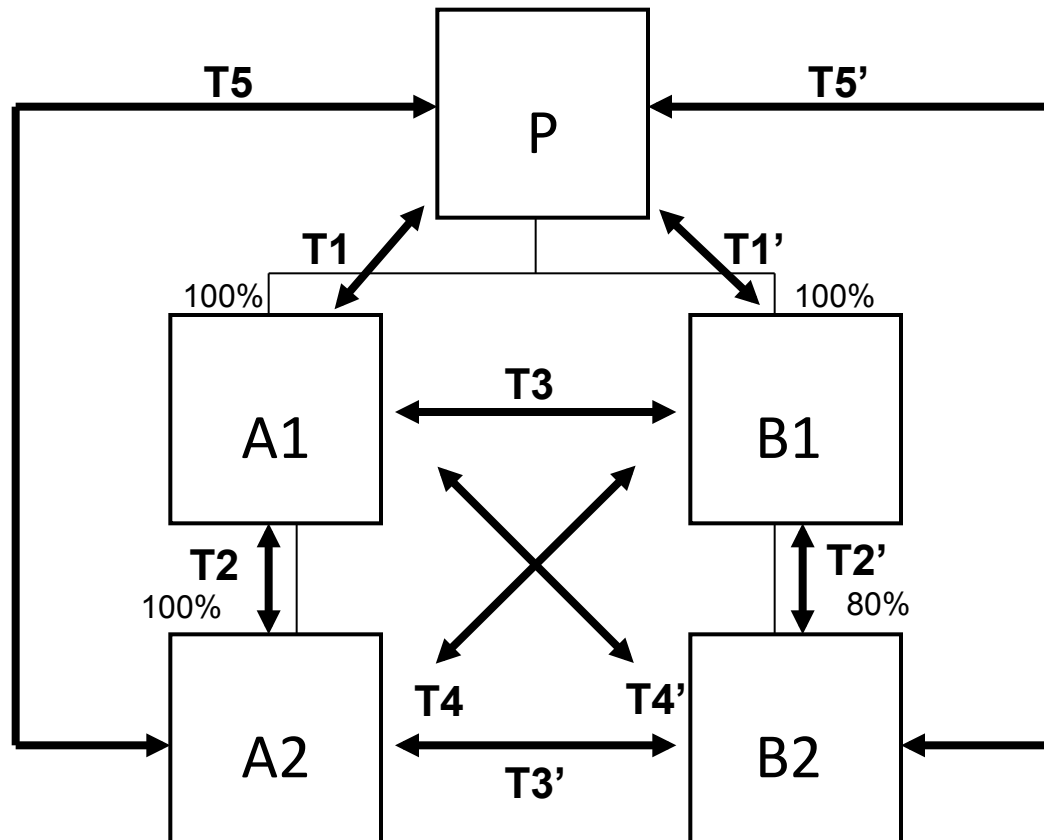
2. Latest developments:

- a. EU level
- b. International level

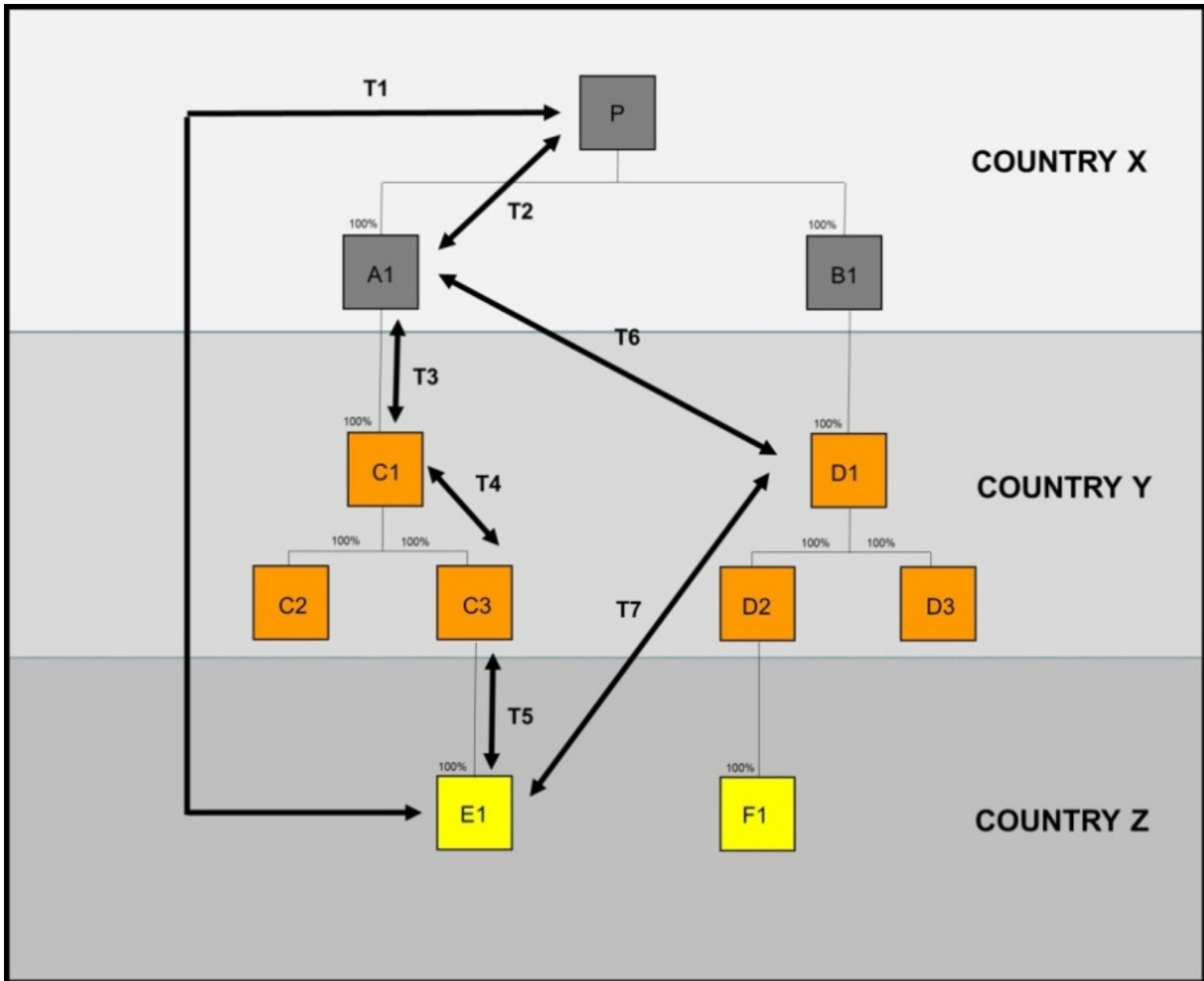
The Nature of Corporate Groups

1. “Chameleon-like” governance structures
2. “Organizationally-bound” property rights
3. Functional structures that may deviate from legal structures
4. Organized internal markets

VERY FLEXIBLE FORM OF ENTERPRISE

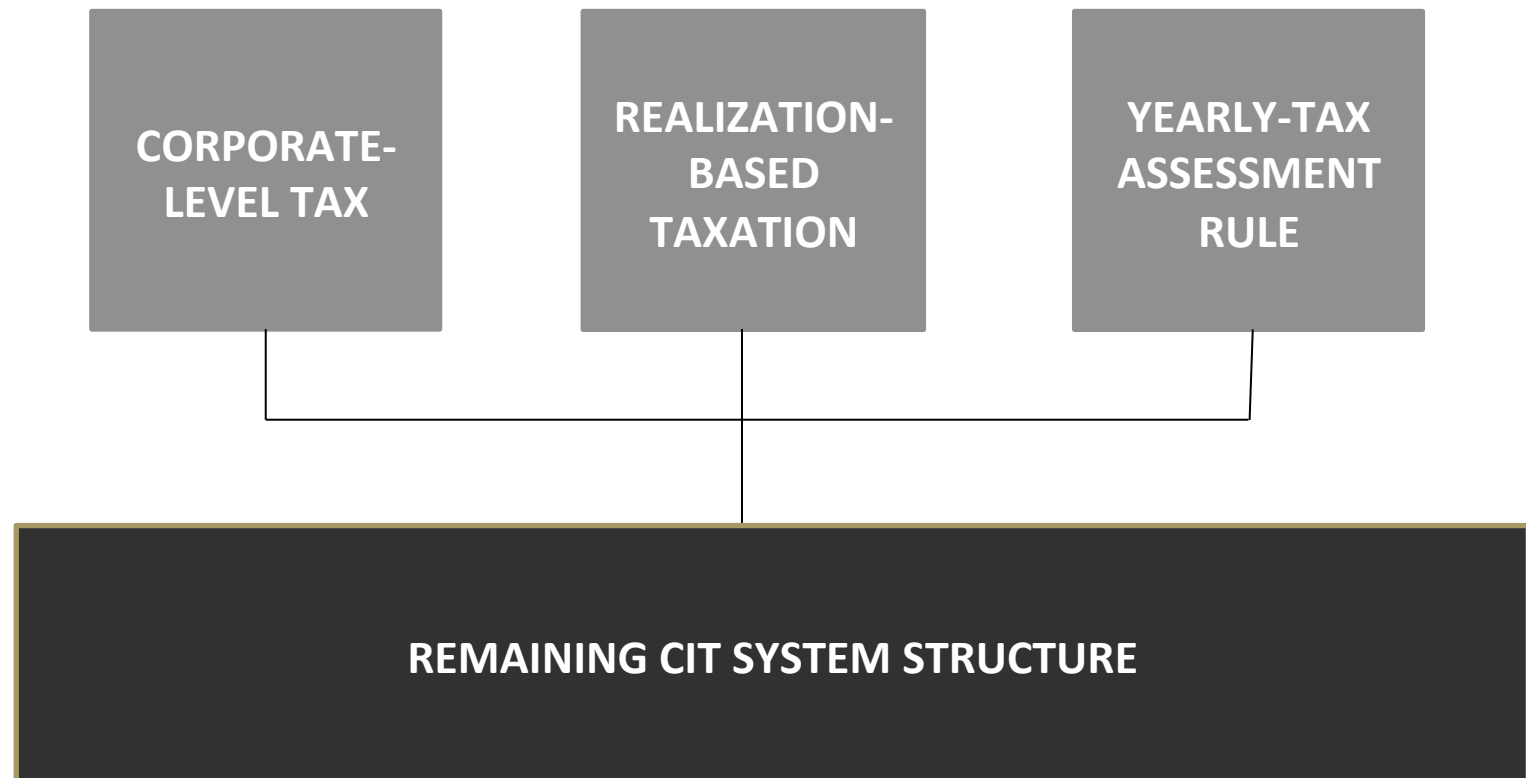


TRANSACTIONAL FLOWCHART

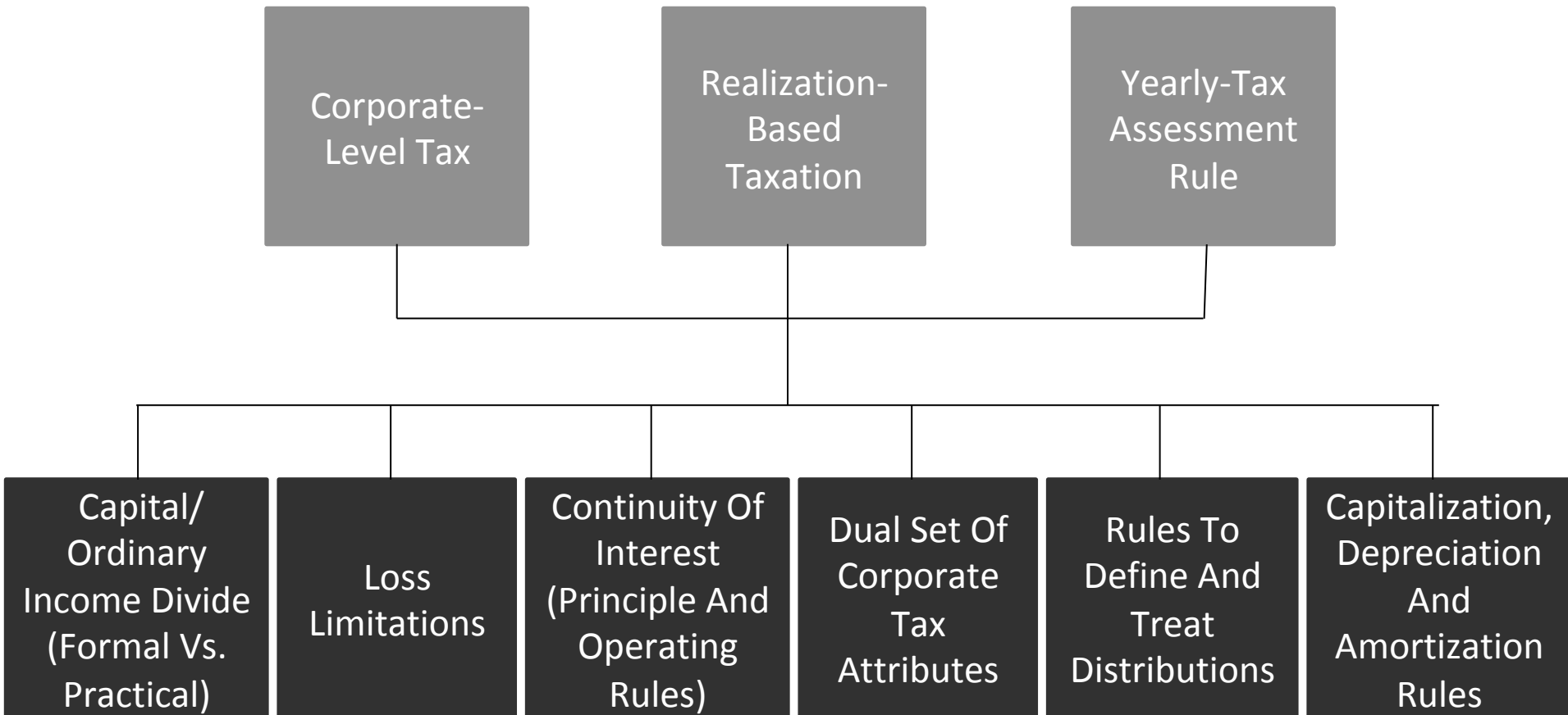


TRANSACTIONAL FLOWCHART | OPEN SETTING FRAMEWORK

The Core Structural Pillars of CIT Systems



The Mechanical Structure of CIT Systems

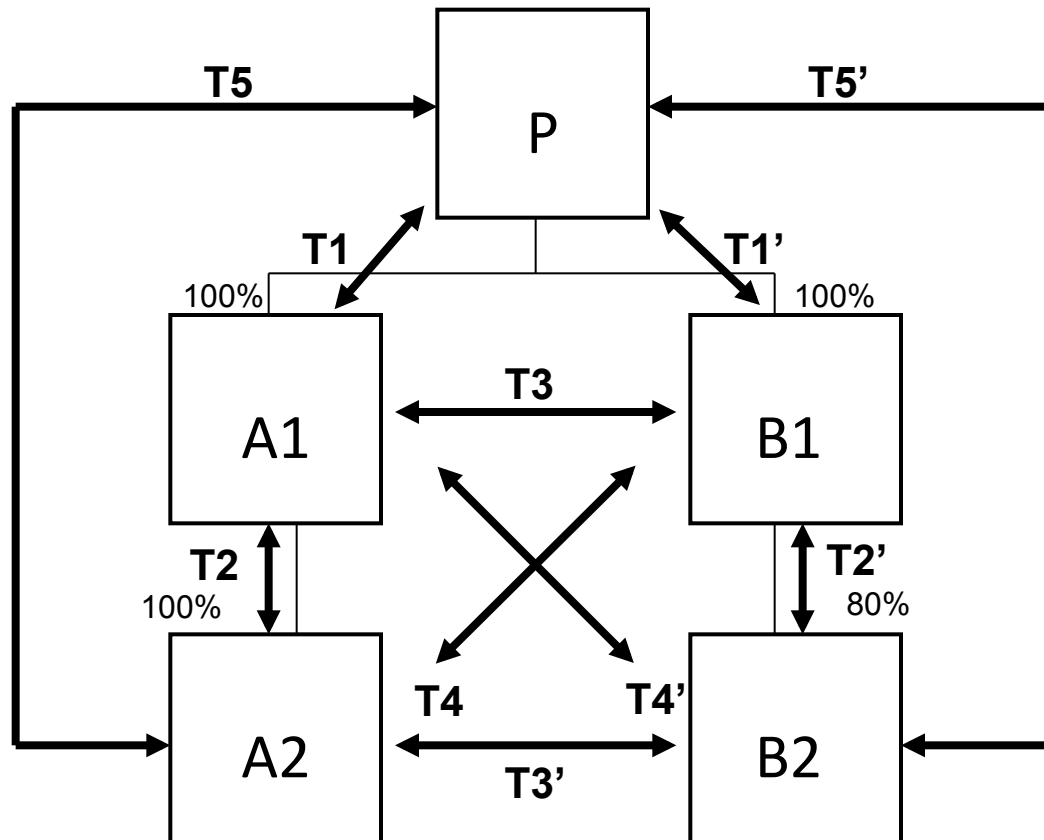


Transactional Mechanics of CIT

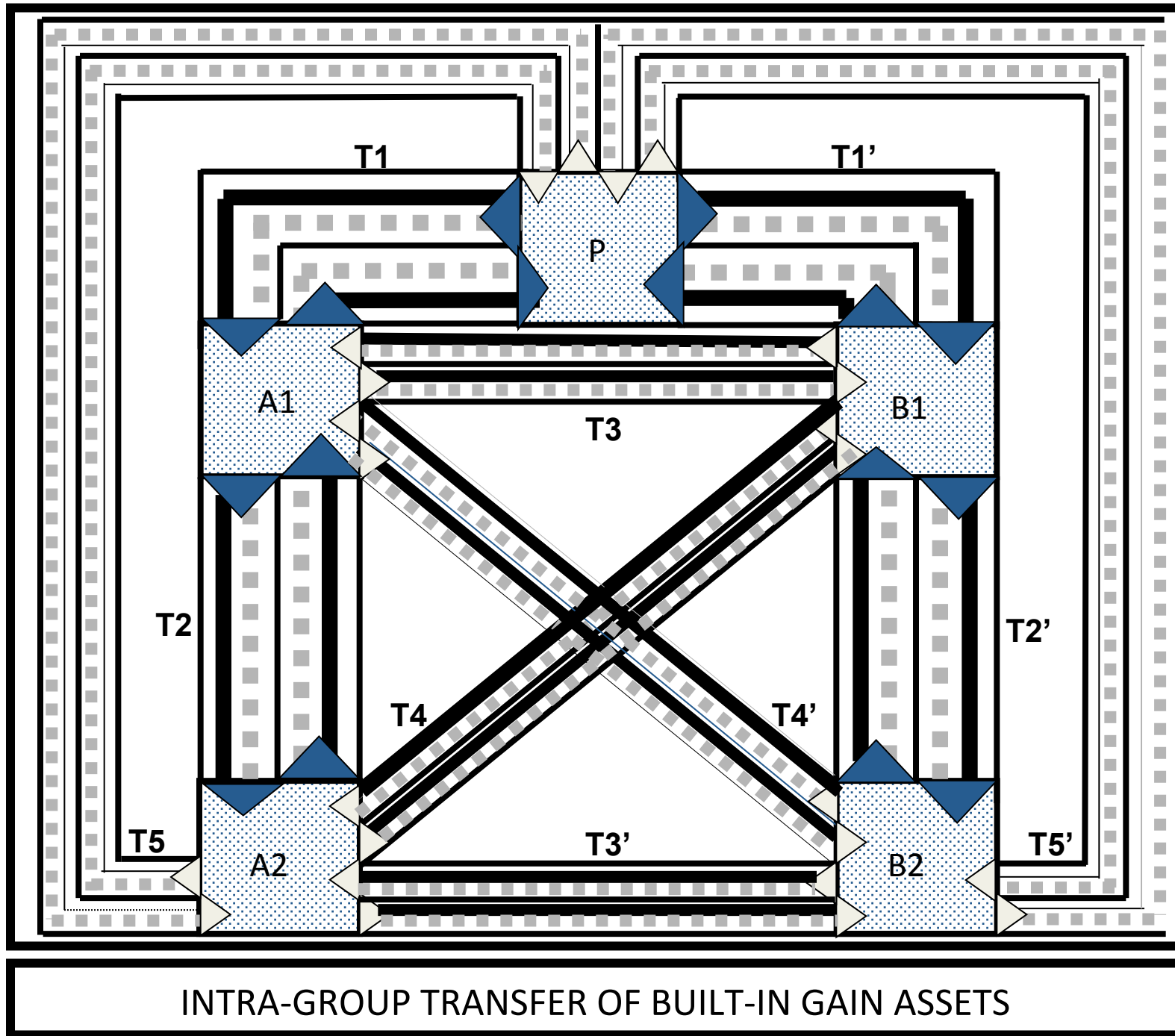
Systems: The Importance of

TRANSACTIONAL FORM

1. The nature of the good transferred (cash vs services vs assets vs stock);
2. The direction of the transactional flow;
3. The relationship of transferee and transferor corporations; and
4. The legal instrument adopted to implement the transfer (e.g., sales contract vs lease contract vs merger deed)



TRANSACTIONAL FLOWCHART



Manipulation of CIT System

MANIPULATION FOCUSES ON VALUE (Transfer Pricing),
TIMING (Lock-in and Lock-out Behavior),

AND

LEGAL CHARACTERIZATION OF INTRA-GROUP
TRANSFERS:

- A group may easily select different transactional routes and legal forms to implement an intra-group transfer of assets or cash.
- In addition, group may also alter its legal or functional structures in order to obtain a more advantageous tax treatment (“Global Tax Planning” Concept).

SUBSTITUTIVE BEHAVIOR

When taxpayer substitutes a transaction, instead of implementing transaction that it would implement based on regular business considerations, it implements an alternative transaction.

The alternative transaction should lead to a similar economic result, but with a differing, more advantageous tax treatment.

Variables of SUBSTITUTIVE BEHAVIOR

- The current and expected future tax position of the taxpayer:
 - Inside basis (tax value of assets) and outside tax basis (tax value of stock);
 - taxable income (present and future);
 - available carryovers of tax losses;
 - possibility offered by transaction to carryover tax attributes.
- The existence and direct cost of alternative transactional routes;
- The existence of tax law restrictions;
- The relative importance of competing non-tax goals (e.g., financial reporting issues)
- The existence of frictions in other regulatory fields;
- The risk-taking profile of the firm;
- The firm's organizational design; and
- The stage of development of the firm.

Problems of SUBSTITUTION

Inefficiencies may include:

- Transfer of resources to a corporate member that does not provide the best economic return for their use;
- Adoption of sub-optimal functional structure;
- Adoption of sub-optimal legal structure; and
- Adoption of more complex transactions.

Problems of SUBSTITUTION

End economic results:

- Increase of tax overhead costs both for corporate groups and the state;
- Reduction of corporate groups' ability to shift capital to its most efficient use;
- Agency problems; and
- Rigid and potentially sub-optimal corporate structures.

Policy Guidelines (Closed Setting)

- **Efficiency**:
 - Minimization of Substitution Effects (i.e., changes in taxpayer decisions or behavior due to the tax system) and
 - Minimization of Tax Overhead Costs (i.e., the quantity of resources that are required to make the tax system work).
- Minimize asymmetries of CIT systems: tax equally all “*closest economic substitutes*”
- Favor long carryover periods
- Reduce CIT discontinuity
- ...
- **Equity** should be sought primarily at individual shareholder’s level (Personal Income Tax)

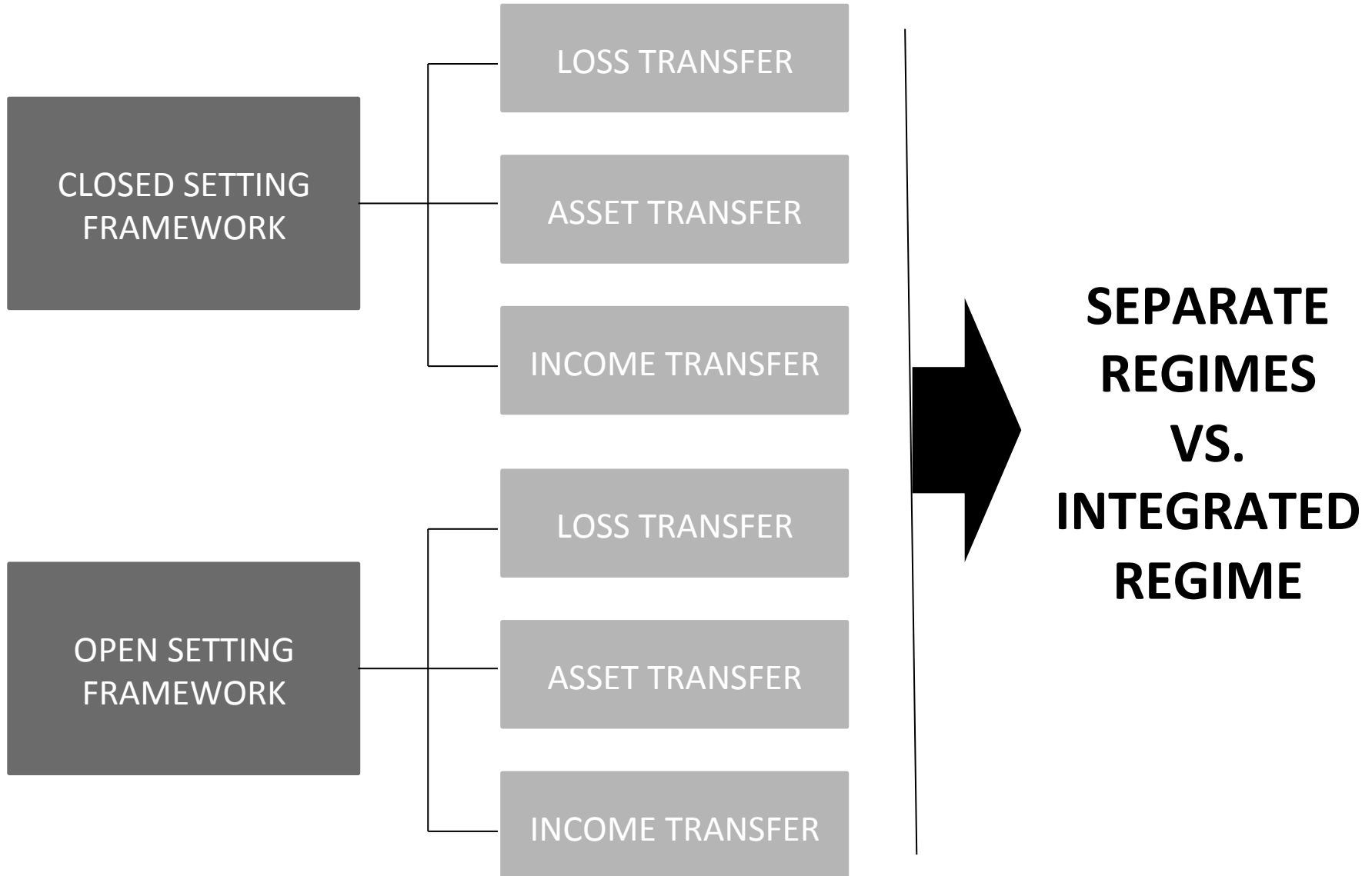
THE TAX INTEGRATION OF CORPORATE GROUPS

- In several jurisdictions, there are special taxation regimes that, while maintaining the separate tax existence of corporate group members, allow for their **integration for tax purposes**.
- Provided there is significant CONTROL, these regimes allow, to various degrees and in different ways, for the **offset of profits and losses among corporate group members** and, in certain cases, for the **deferral of tax on intra-group transfers of assets and income**.
- Several group taxation models with different rules to achieve one or both objectives.

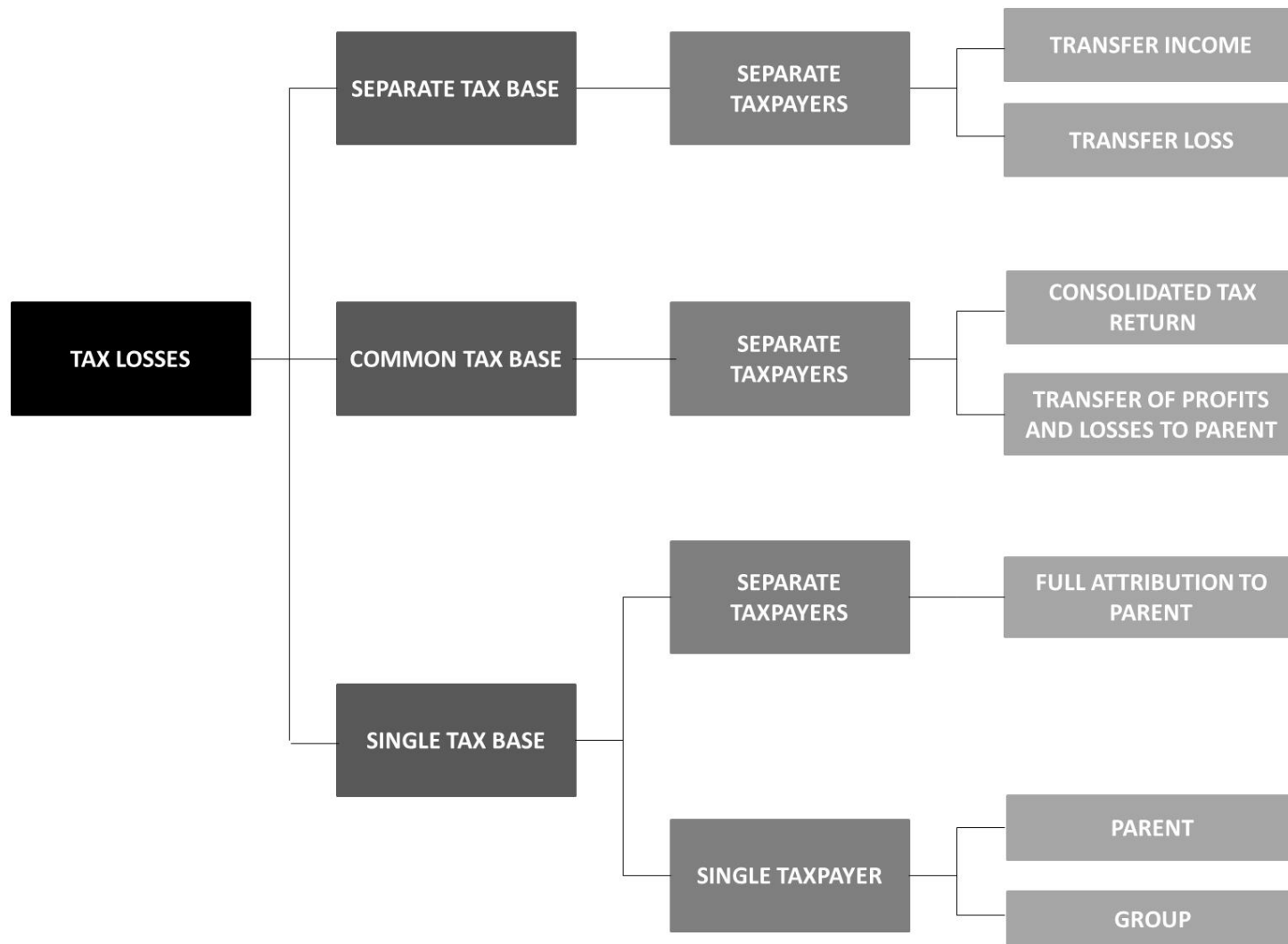
GROUP TAXATION MODELS **(Traditional Taxonomy):**

1. *Organschaft* (ex: Germany and Austria)
2. Group contribution (ex: Norway, Sweeden and Finland)
3. Group relief (ex: United Kingdom, New Zealand and Singapore)
4. Consolidation model (ex: United States, France, Italy, Australia, Portugal, etc)

The Core Blocks of Tax Integration Solutions



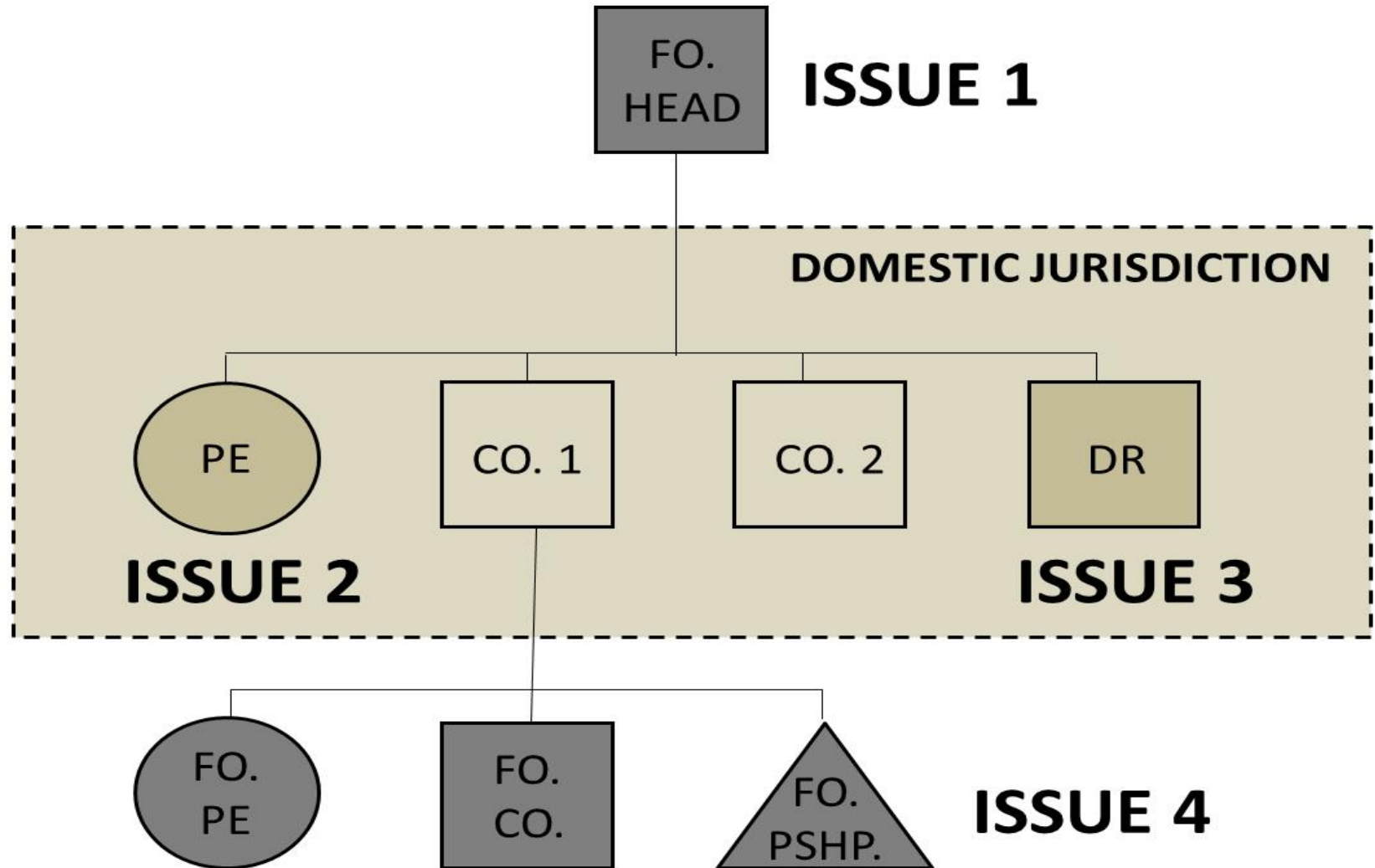
TAX INTEGRATION SOLUTIONS| Intra-Group Loss Transfers



Should jurisdictions adopt Group Taxation regimes?

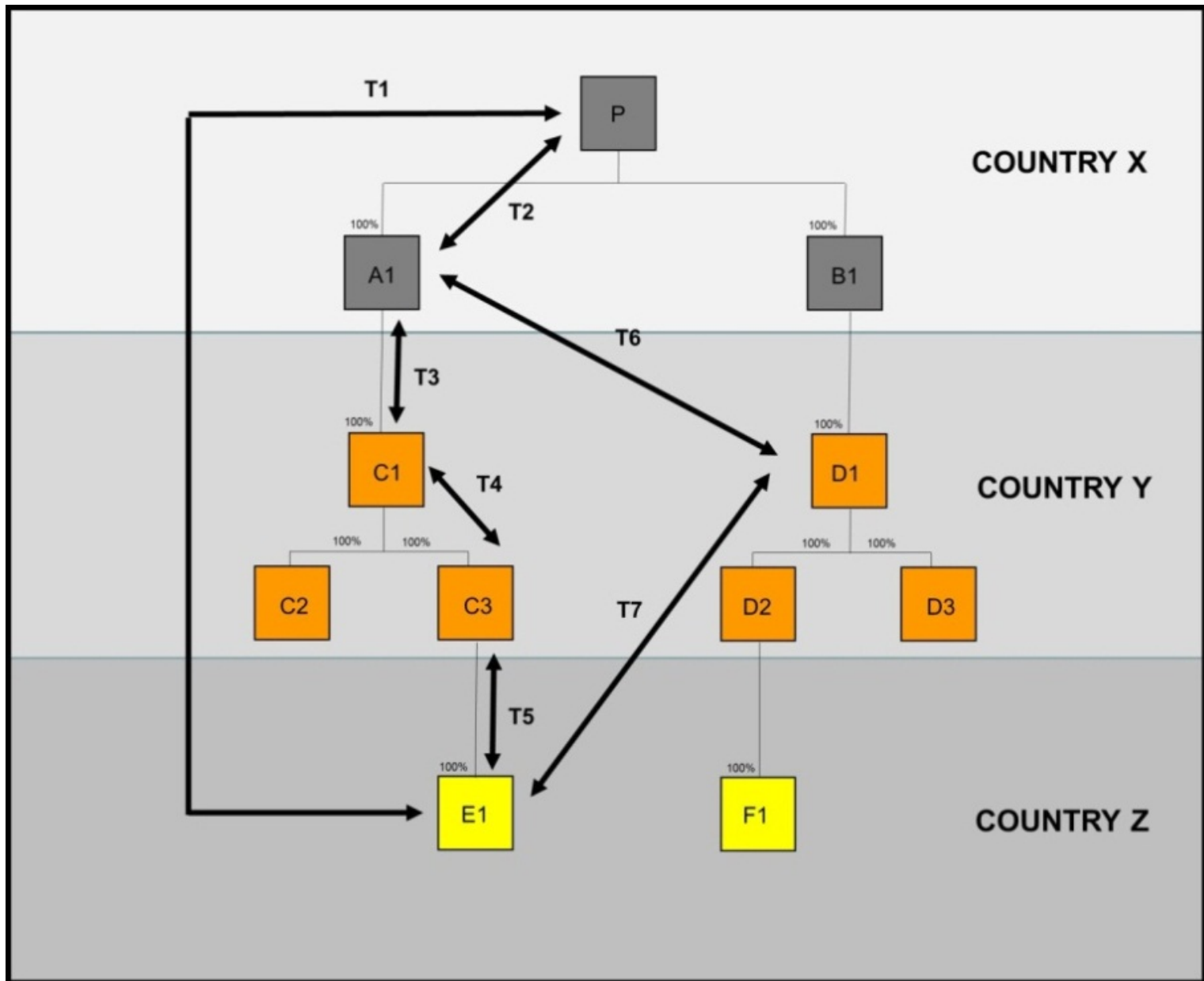
- Based on efficiency criteria, jurisdictions **SHOULD** generally adopt Group Taxation Regimes.
- The selection of the different models available for tax integration will depend of **political decision-making** as much as of **degree of sophistication of local businesses and tax authorities**.
- Comprehensive tax integration solution that covers loss, asset and income transfers, should be preferable. However, risks involved must be adequately tackled.

OPEN SETTING FRAMEWORK



Substitution on an Open Setting Framework:

- Location (tax base and tax rate + exemptions, credits and other tax benefits + tax treaties + anti-abuse arsenal of all jurisdictions involved)
- Direction of transactional flow (entity and country)
- Characterization of legal instrument(s) used to implement transaction (by all countries involved)
- Characterization of entities involved in transaction (by all countries involved)



TRANSACTIONAL FLOWCHART | OPEN SETTING FRAMEWORK

Policy Guidelines (Open Setting)

- High-potential for international substitutive behavior due to asymmetries and mismatches of current international tax system.
- Efficiency very difficult to define on an Open Setting.
- Development of OPEN SETTING FRAMEWORK for tax integration solutions must be very carefully pondered.
Not necessarily recommended in all situations.

LATEST LEGISLATIVE DEVELOPMENTS (EU LEVEL | INTERNATIONAL LEVEL)

- 1. CCCTB**
- 2. COMMISSION ACTION PLAN TO FIGHT FRAUD AND EVASION**
 - RECOMMENDATIONS ON AGGRESSIVE TAX PLANNING AND GOOD TAX GOVERNANCE
 - REVISION OF ANTI-ABUSE RULES OF PARENT/SUB; INTEREST AND ROYALTIES; AND MERGER DIRECTIVES
- 3. EUROPEAN SEMESTER – COUNTRY SPECIFIC RECOMMENDATIONS**
 - CURB DEBT-TO-EQUITY BIAS
 - TRANSFER OF TAX BASE AWAY FROM CIT TO OTHER TAX BASES
- 4. HYBRIDS – WORK OF SUBGROUP OF CODE OF CONDUCT**
- 5. TAXATION OF INTRA-GROUP FINANCING UNDER FTT**
- 6. COUNTRY-BY-COUNTRY TAX REPORTING FOR LARGE CORPORATE GROUPS**
- 7. BEPS (INTL)**
- 8. MOVE TO AUTOMATIC EXCHANGE OF INFORMATION AS NEW GLOBAL STANDARD (FATCA / OECD GLOBAL MODEL / REVISION OF EU DIRECTIVES) (INTL)**

Now it's time to read the book...

Thank you for your attention!

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