Why Europe needs 3CTB to get ahead

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On 17 June 2015, the Commission adopted a plan to relaunch the 3CTB (Common Consolidated Corporate Tax Base), a common system for calculating the tax base of businesses operating in the EU. Except, it did not, it announced that it would start with a modified 2CTB (Common ~~Consolidated~~ Corporate Tax Base) instead.
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BEPS is old news. The EU "BEPS" plan, called the "Action Plan on Corporate Taxation" of 17 June 2015, is newer. The plan has been welcomed by the OECD Secretary-General with the words, "The European Commission's initiative is another major step towards international co-operation in the fight against tax evasion and avoidance." The question is why?

If the EU could, in one single step, eliminate virtually all the issues addressed under the BEPS action points, but deliberately chooses not to do so, why congratulate them? Is it because 3CTB looks too much like global formulary apportionment, and the EU has chosen not to go there yet?

Another theme, both for BEPS and the EU, is transparency. For BEPS it is focussed under Actions 5 and 12; for the EU the news is the Transparency package of 18 March 2015. Again the OECD Secretary-General congratulated the EU with the words, "The European Commission's initiative is another major step to tackle corporate tax avoidance." The question is why?

If the EU could, in one single step, eliminate virtually all the issues addressed under BEPS regarding transparency, but deliberately chooses not to do so, why congratulate them?

I was at public hearing of the European Parliament's TAXE committee. Following the LuxLeaks revelations, this committee was launched in February 2015 to see if some member states use special tax regimes that favour large MNE's. The questions from the committee members illustrated at least three things:

1. A real concern about fair taxation;
2. An honest belief that they were doing a good thing; and
3. A clear display that most had no idea what the difference is between a 2CTB and a 3CTB.
   This is so crucial.

Under 2CTB:

MNE's can within the EU: do most of the things the BEPS digital economy report warns against; have CFC's; erode tax bases through interest deductions; benefit from harmful tax practices; abuse tax treaties; avoid PE's; do all the TP things BEPS actions 8, 9, 10 and 13 warn against; use aggressive tax structures; and will still need a lot of dispute resolution.

Under 3CTB:

MNE's cannot do any of the above within the EU.

Like the proverbial Samson's strength was in his hair and he lost all of it when he lost his hair; 3CTB's strength is in consolidation, and you lose all of it when you lose consolidation; you don't get to keep 66%, just because you kept 2C's.

The reason is simple. Under consolidation profits will be allocated on the basis of wages, assets and destination of sales. Consequently, an EU finance company with little personnel; little physical assets and even less destination of sales will get little income no matter how large its capital is, or what its intercompany agreements entail; a non-EU finance company can be dealt with by 3CTB CFC rules.

So why does the EU not embrace 3CTB? Clearly part of the reason is that the TAXE members do not appreciate this difference. If they did, one would assume that they would push for 3CTB with the same fervour as with which they demand tax transparency.

However, a lack of technical understanding should not be the case with the technicians at the Commission, at DG TAXUD, Unit 1, dealing with Company Taxation Initiatives. So what is keeping them back? I think it is the national counterparts of the European Parliament: time and again one hears that member states do not want to give up their tax sovereignty (but will settle for a compulsory 2CTB?). So, rather than have an EU wide system that works, each country wants to keep their sovereignty to make their own tax rules, wants to keep the right to fight BEPS (or not?) their own way, wants to keep a broken system in place and wants to blame business instead. This is such a pity. What it means is that when these national administrations tell their political leaders to tell the G-20 that they have done their best to fight BEPS – as their leaders committed to – then these administrations are telling their leaders to tell the G-20 a partial truth.

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A person that knows far more about tax than I, Prof. Dr. Kees van Raad – Academic Director of the International Tax Centre Leiden in Holland, thinks that a harmonised global tax system is the only sustainable solution for BEPS (https://www.youtube.com/watch?v=M6sSJc6V3sg around the 7th minute). In other words, a 3CTB for the world: if it can work for the EU, it might work for the world (IF the world can agree on 1 tax base and 1 set of allocation keys).

Though I do believe that the current volume of OECD and EU rules and attacks may grind the global corporate tax system to a halt and slowly sink it into a vast ocean of disputes, I do not know if Kees' vision will come true. However if it would, the faster implementation of 3CTB would give the EU a strategic advantage: the EU can either be in the lead, as the ones with practical experience of making a formulary system work; or the EU can be followers, as the ones who choose national hobbyism over the greater good.

Another reason why the 2CTB:3CTB stepped approach is such a pity, is the waste of resources:

- instead of spending all its resources on developing a workable 3CTB, the Commission and member states will now work on a 2CTB (plus the national implementation thereof), then a 3CTB (if ever); plus an interim host of antiabuse measures on a per country basis; an interim cross border loss transfer system (which would have been dealt with 3CTB in any case); more work on tax transparency on a per country basis (not needed under a consolidation system); and a number of EU coordination tools (already arranged under 3CTB). Surely, a concerted BEPS-like effort would have gotten a 3CTB system in place much faster, much more focussed and with far fewer resources from the Commission, the member states and taxpayers;

- instead of one transition, we will have to deal with at least 2 transitions: from separate country systems to a 2CTB system, and from a 2CTB system to a 3CTB system. Each system will generate its own grandfathering issues and its own tax disputes. As for the latter, companies and authorities will have to currently administer one system, while still fighting battles from a previous system (and eventually battles from a previous-previous system). A nightmare for all, but highly paid advisers.

I know 3CTB has many critics and sceptics. I am not one of them. In fact, I think it is the only way for the EU to get ahead in the global tax competition. It will give us a more robust, stable system which treats Europe like the internal market we are supposed to be. Robust because it eliminates BEPS within the EU; stable because it removes corporate tax legislation from small country local specialists and hobbyists to an EU wide pool of experts and opinions (governments consistently underestimate the value business puts on legal stability when making their investment decisions).