European Union

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International Tax Consolidation in the European Union: Evidence of Heterogeneity

With regard to this topic, the authors first consider the concept of tax neutrality and its domestic and international implications. They next focus on the rules that each Member State has for a corporate group to adopt group taxation. As a result of the diversity of the national group taxation regimes within the European Union, the authors then suggest a typology for these systems as well as examining the intrinsic features of tax consolidation systems.

1. The Background to the Topic

The notion of a "corporate group" is deeply embedded in the existing economic framework of the European Union, especially as international mergers and acquisitions are a current phenomenon. This concept is, however, not uniformly integrated into fiscal legislation and the taxation of intra-group operations depends significantly on their legal form, their location in time and space and the economic entity in which they occur. Inevitably, this gives rise to tax planning opportunities, which affect EU market efficiency and the international circulation of goods, services and capital between group entities in different Member States. The decision of the European Court of Justice (ECJ) in *Marks & Spencer*[1] also identified an urgent need for multinational groups to be able to offset tax losses on an EU-wide basis.

In its efforts to overcome these tax obstacles to cross-border transactions, the Commission has expressed the need for a consolidated corporate tax base.[2] Specifically, the Commission recently communicated its option for a Common Consolidated Corporate Tax Base (CCCTB) to be the group taxation regime at an EU level. The CCCTB would permit international consolidation between group companies. A common consolidation system would also uniformly integrate the "corporate group" concept into tax legislation and would answer the question of the offsetting of international tax losses. The acceptance and implementation of this new strategy by the Member States will take time. Some Member States have, however – possibly encouraged by *Marks & Spencer* – already attempted to satisfy this need and have integrated an international consolidation system into their tax legislation.[3]

In order to highlight the need for a common EU consolidation system, this article provides a general survey of the (international) tax consolidation systems currently existing in the European Union. The starting point is the criterion of tax neutrality, which, in part, motivates the Member States to implement group taxation systems. The concept of tax neutrality and its implications, both in a domestic and in an international environment, are, therefore, considered in Section 3. Section 4. focuses on the requirements that each Member State has established for a corporate group to adopt group taxation. The heterogeneity of these national requirements is also considered. As a result of the diversity amongst the national group taxation regimes in the European Union, a typology of these systems is suggested in Section 5. In addition, the intrinsic features of tax consolidation systems are examined. Section 6., which sets out the authors' conclusions, completes the article.

The scope of the analysis is limited to corporate income tax, as set out in the tax legislation of the Member States at 1 January 2007. Throughout the paper, "entity" is a general term that refers to both subsidiaries and permanent establishments (PEs). The concepts of "tax group" and "group taxation regime", which are frequently used in this article, are defined in the relevant sections.

2. Tax Neutrality

According to economic tax theory, an efficient tax design should be neutral, by which is meant that economic choices should not be affected by taxation. From a group taxation perspective, neutrality requires that decisions regarding, for example, the geographical distribution of entities (the international context) or the organization of the group (the national context), should not be influenced by taxation. As such, international tax neutrality requires both the tax base and the tax rate to be unified. For this reason, the CCCTB would only create partial international tax neutrality, as each Member State would retain the right to decide on its corporate income tax rate according to budgetary needs.

In a national context, tax neutrality is achieved when a company doing business by way of divisions (a single

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1. ECJ, 13 December 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*.
2. European Commission, "Towards an Internal Market without tax obstacles. A strategy for providing companies with a consolidated corporate tax base for their EU-wide activities", Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee, 23 October 2001, COM(2001) 582, p. 15.
3. Italy (2004) and Austria (2005) have recently introduced international tax consolidation.

company) has the same tax burden as a company undertaking a similar activity by way of subsidiaries (a corporate group). Under a tax-neutral system, the choice of the taxpayer for a given organizational form is not influenced by tax issues because a business activity is taxed regardless of its organizational form as a single company or a corporate group. In principle, this view of tax neutrality stimulates tax legislators to introduce group taxation regimes that permit the similar taxation of corporate groups and single companies. Through the typology of the various group taxation regimes, it is, however, clear that this objective has not been realized. This is due to the fact that the tax neutrality criterion[4] can only be verified if the Member States assume that both organizational forms are totally identical in economic terms. As no Member State fully adheres to this assumption, biases are inevitable. Accordingly, national as much as international tax neutrality remains utopian in an EU context.

3. Recognition and Definition of a Tax Group

3.1. Introductory remarks

So far, the authors have set out the reasons for establishing group taxation regimes. It is now necessary to examine the requirements for a corporate group to benefit from such a regime. This section, therefore, focuses on the conditions that each Member State has established for a corporate group to adopt group taxation.

Before proceeding further, it should be noted that a corporate group is characterized differently for civil and tax law purposes. In most Member States, the concept of a corporate group has a specific definition according to the scope of application. In a civil law context, a corporate group can generally be defined as a group of business organizations connected through common control by way of shareholdings and/or other financial and managerial relationships. From a fiscal point of view, a corporate group is usually characterized by stricter conditions and little flexibility is possible.

3.2. The concept of a tax group

Group taxation is based on the principle of equal taxation of identical economic situations (tax neutrality). To ascertain that corporate groups, which request the application of group taxation, are in the same economic situation as a single company, the Member States apply a set of requirements to benefit from group taxation. A corporate group meeting such a set of conditions is commonly referred to as a "tax group". It is important not to confuse the tax group with the specific group taxation regime to which the tax group may be subject.

If no specific group taxation regime applies, a tax group would exhibit tax properties[5] that are primarily tax disadvantages. In contrast, as a result of a specific group taxation regime, a common taxable income can be determined in respect of which one corporate income tax liability can be paid for the entire group and the tax group can be treated as a single taxpayer. This is, of course, another extreme situation and there are intermediary tax regimes, which are reviewed in this article. As such, a group taxation regime has a determinant role, as it completes or adjusts the tax properties of a tax group. It is also the group taxation regime that makes a tax group more or less desirable for tax planning purposes.

As each Member State has fiscal sovereignty under EC law and can freely define, to date, the concept of a tax group and the group taxation regime that applies, there is considerable heterogeneity in this respect in the European Union. This, in turn, provides corporate groups with the opportunity to choose the most convenient regime and locate their main company in the Member State that offers the most attractive regime.

3.3. Heterogeneity under domestic laws

3.3.1. No tax group recognition

Two of the "old" (Belgium and Greece) and some of the "new" (Bulgaria, the Czech Republic, Estonia, Hungary, Lithuania, Romania and the Slovak Republic) Member States completely ignore the tax group concept and, consequently, do not provide for a group taxation regime. The domestic tax laws of these Member States do not distinguish between an isolated company and a company that is part of a national or international corporate group. Accordingly, no specific group taxation regime is provided for and taxable income is determined for each legal entity separately. Each entity is taxed as if it were an independent company. It should, however, be noted that, notwithstanding the absence of a tax group, Belgian tax law included a favourable tax regime for resident companies and the PEs of non-resident companies pursuing activities as a coordination centre.[6]

3.3.2. Tax group recognition

3.3.2.1. Initial comments

Most Member States recognize the interdependence of companies for tax purposes and have introduced the tax group concept into their tax legislation. These Member States acknowledge the existence and legitimacy of tax groups so as to create a legal order that better agrees with economic reality. In this respect, either the legal or the economic aspect of a tax group can be privileged.

A legal approach is based on a legal (direct or indirect) ownership threshold. A subsidiary is considered to be part of its parent tax group if a certain amount of its shares or voting rights is owned by the parent company. In contrast, an economic approach relies on ownership control and the operational or economic interdepend-

4. Y. Masui, "General Report", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), pp. 34-35.
5. P. van Ommeslaghe, "La notion de 'groupe de sociétés' en droit des sociétés et en droit fiscal", in H. Biron and C. Dauw (eds.), *La reconnaissance des groupes de sociétés en droit fiscal* (Antwerpen: Kluwer Rechtswetenschappen, 1989), pp. 23-24.
6. Id.

ence between the group companies.[7] In practice, most Member States base their tax group definition on a combination of both the legal and the economic approach. Legal and economic conditions vary widely from one Member State to another and primarily concern requirements regarding shareholdings, company form, interdependence and accounting. An overview of the legal and economic conditions for tax group recognition is set out in Table 1.

3.3.2.2. Legal conditions

As noted in 3.3.2.1., legal ownership criteria refer to the amount of shares or voting rights that a parent company holds in its subsidiaries. These are generally expressed as a percentage of the total amount of shares or voting rights of these subsidiaries. Polish tax legislation, for instance, requires a parent company to hold 95% of the shares of its subsidiary for the latter to be part of the parent's tax group. With regard to tax group definition, all Member States have strict ownership requirements, which, however, vary considerably from one Member State to another. The reason for these strict thresholds is often to ensure that the group members form a single economic entity.[8]

Legal ownership requirements can be based on shareholding (Finland and Sweden), voting power (Cyprus, Germany and Italy) or on both (Austria and Portugal). The assessment of these requirements can also differ from one Member State to another. Netherlands tax legislation, for example, stipulates that, if the subsidiary has issued different types of shares, the ownership requirement must be met for each type.[9] In Cyprus,[10] Malta and the United Kingdom,[11] the requirement not only applies to shareholding and voting rights but must also be met with regard to the profits available for distribution to the parent company.

Unfortunately, due to these strict conditions, only a relatively small number of corporate groups can benefit from the tax group status. Accordingly, some Member States have introduced specific regimes to extend this status to companies not meeting the legal ownership requirement. Sweden, for example, exempts from the ownership requirement companies that can prove that the transfer of losses is vital for their activity.[12] Austria also recently allowed participation pools (see 3.3.2.3.) to act as the parent company of a tax group, provided that all the pool members hold at least 15% of the nominal capital and the voting rights of the group member and that one pool member holds at least 40%.[13]

3.3.2.3. Economic conditions

In addition to the legal conditions, most Member States also have economic conditions for tax group recognition. These primarily relate to the economic characteristics of the company, the degree of interdependence or integration within the group and a series of other requirements, including in terms of accounting.

Some characteristics of a company may exclude it from participating in a tax group, such as inactivity (for example, in Finland,[16] Portugal[17] and Spain)[18] or their exemption from the normal taxation regime (for example, in Sweden).[19] In almost all Member States, tax group participation is also restricted to certain organizational forms. In particular, the form required to be regarded as part of a tax group often differs according to the role of the company in the tax group (parent company or group entity). Both alternatives are explored in the following paragraphs.

Most Member States require parent companies to be domestic joint stock companies, limited liability companies or cooperatives. Some, however, accept a non-company as heading the tax group. German tax legislation, for instance, permits individuals pursuing a commercial activity and tax-transparent entities, such as partnerships, to act as group head,[20] provided that there is sufficient substance to their activities[21] (pure holding activities do not, however, satisfy this requirement).[22] In Austria, a participation pool (a transparent entity),[23] which consists of entities that separately do not have sufficient financial control to form a tax group can qualify as the parent company of a tax group.[24] Portugal has extended the parent company status to partnerships and public business entities. Some Member States, such as

7. European Commission, Common Consolidated Corporate Tax Base Working Group (CCCTB WG), "Issues related to group taxation", Working Document, 5 May 2006.
8. M. Dos Prazeres Lousa, "Portugal", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 552.
9. R.J. de Vries, "Netherlands", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), pp. 470-471.
10. A. Athinodorou, "Cyprus", *International Tax Review,* World Tax, 2006, Vol. 16, p. 124.
11. Y. Rupal, "United Kingdom", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 689.
12. B. Wiman, "Sweden, in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 638.
13. G. Gahleitner and S. Ratzinger, "International Group Taxation: An Overview of Austria's New Tax Incentive", *European Taxation* 11 (2005), p. 511.
14. European Commission, "Tax Treatment of Losses in Cross-Border Situations", Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee, 19 December 2006, COM(2006) 824 final, annex VIII.
15. N. Josephsen, "Denmark", *International Tax Review*, World Tax, 2006, Vol. 16, p. 137.
16. H. Ranta-Lassila, "Finland", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 260.
17. Dos Prazeres Lousa, note 8, p. 551.
18. M. Amparo Grau Ruiz, "Spain", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), 2004, p. 615.
19. Wiman, note 12, p. 770.
20. A. Rädler, "Tax consolidation in the Federal Republic of Germany", in H. Biron and C. Dauw (eds.), *La reconnaissance des groupes de sociétés en droit fiscal* (Antwerpen: Kluwer Rechtswetenschappen, 1989), p. 100.
21. S. Ditsch, "Germany", *International Tax Review;* World Tax, 2006, Vol. 16, p. 182.
22. M. Lenz, "Draft guidance proposed on tax consolidation rules", *International Tax Review*, April 2005, Vol. 16, Issue 4, p. 72.
23. Sec. 9(3) *Körperschaftsteuergesetz* (KStG).
24. Gahleitner and Ratzinger, note 13.

Table 1: Legal and economic conditions for tax group recognition

Criteria	Legal shareholding (%)[14]	Economic			
		Company form		Group entities' interdependence	Accounting requirements
		Parent company	Eligible entities		
Austria	>50	(1) or (5)	(6) or (11)	(14) and (15)	–
Cyprus	≥75	(1)	(6)	(14)	–
Denmark	>50	(1)[15]	(6) or (9) or (13)	(14) and (15)	(16)
Finland	≥90	(1)	(6)	(14) and (15)	(16)
France	≥95	(1)	(6) or (10)	(14)	(16)
Germany	>50	(2) or (5)	(6)	(14) and (15)	–
Ireland	≥75	(1)	(6)	–	–
Italy	>50	(1) or (5)	(6) or (9)	(14)	(16)
Latvia	≥90	(2)	(7)	(14)	–
Luxembourg	≥95	(3)	(8)	–	(16)
Malta	≥51	(1)	(6)	(14)	(16)
The Netherlands	≥95	(3)	(6)	(14)	(16)
Poland	≥95	(1)	(6)	–	–
Portugal	≥90	(1)	(6)	(14)	(16)
Slovenia	≥90	(1)	–	–	–
Spain	≥75	(1)	(6) or (10)	(14)	(16)
Sweden	≥90	(1) or (4)	(6) or (12)	(14)	–
United Kingdom	≥75	(2)	(6)	–	–

Company form:
(1) Domestic company.
(2) Domestic taxpaying company.
(3) Domestic fully taxpaying company.
(4) Foreign EU/European Economic Area (EEA) company, taxpaying in the Member State in question.
(5) Foreign company, resident in a treaty state with a PE in the Member State in question (only for domestic consolidation).
(6) Domestic subsidiary.
(7) Domestic taxpaying subsidiary.
(8) Domestic admitted subsidiary.
(9) Foreign subsidiary.
(10) Foreign admitted subsidiary.
(11) Foreign EU subsidiary.
(12) Foreign EU/EEA subsidiary, taxpaying in the Member State in question.
(13) Foreign PE.

Group entities' interdependence:
(14) Existing for the entire taxable year.
(15) Agreement.

Accounting requirements:
(16) Same accounting periods.

Portugal[25] and Italy,[26] also require the dominant company to be the highest level group member (for international tax group purposes only).

As stated previously, in most Member States, only resident taxpaying companies, created under domestic company law, can qualify as parent companies. Sometimes, however, as in the Netherlands,[27] entities established under the company law of certain foreign countries are also allowed to act as a parent company, provided that they are similar in nature to a qualifying Netherlands entity.[28] For Austrian, German and Italian tax purposes, a parent company can be a non-resident company as long as it is a resident in a treaty state and it has a registered PE in Austria,[29] Germany[30] or Italy,[31] respectively. In Denmark[32] and in the United Kingdom,[33] two resident subsidiaries of a non-resident parent company can form a Danish or UK tax group without having a resident parent company.

In general, resident subsidiaries, meeting the shareholding requirements, qualify as group members. Company form requirements for group entities are less strict than for parent companies. In most Member States, only first-tier subsidiaries, created under resident law, are permitted to belong to a taxable group. In some Member States, however, such as the Netherlands[34] or Sweden,[35] subsidiaries at any level are eligible for group membership. Austria, Denmark, France and Italy have all widened their definition of a tax group to include non-resident EU group entities. Under Austrian law, however, lower-tier subsidiaries are only included in the tax group if they are controlled by an Austrian group member or parent company.[36]

25. Dos Prazeres Lousa, note 8, p. 551.
26. R. Murphy and G. Moretti, "Aggregation features in new Italian group consolidation rules", *International Tax Review*, September 2004 Industry Guide: Energy, p. 31.
27. Entities established under company laws of Aruba, the Netherlands Antilles, the Member States and treaty states prohibiting discrimination on the grounds of nationality.
28. De Vries, note 9, p. 469.
29. C. Hoeing and N. Schmidt, "Government tries for more investments with corporate tax changes", *International Tax Review*, October 2004, Vol. 15, Issue 9, p. 21.
30. M. Lenz, "Tax authorities reject cross-border consolidation", *International Tax Review*, February 2005, Vol. 16, Issue 2, p. 46.
31. M. Giacionia, "Italy", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol.89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 379.
32. Josephsen, note 15.
33. Rupal, note 11, p. 701.
34. Art. 15(2) Corporate Income Tax Act (CITA).
35. Wiman, note 12, p. 637.
36. Gahleitner and Ratzinger, note 13.

Table 2: Group taxation regimes

Group taxation regimes	Member States
1. Tax relief	
	Not used in Member States
2. Transfer	
– Group contribution	Finland and Sweden
– Group relief	Cyprus, Ireland, Latvia, Malta and the United Kingdom
3. Consolidation	
– Partial tax consolidation	Austria, Denmark, France, Germany (*Organschaft*), Italy, Luxembourg, Poland, Portugal, Slovenia and Spain
– Full tax consolidation	The Netherlands

In addition to conditions listed so far, the corporate tax legislation of several Member States requires the group relationship to exist during the entire taxable year for which the tax group status is applied. These Member States include Austria, Cyprus, Denmark, Finland, France, Germany, Italy, Latvia, Malta, the Netherlands, Portugal, Spain and Sweden.

In some Member States, such as Denmark, Germany, Finland and Spain, national tax legislation requires the group relationship to be stated in an agreement. Specifically, the German *Organschaft* requires a profit and loss pooling agreement to be concluded between the group members[37] for a five-year period.[38] Group members surrendering their profits and losses must register this contract with the Commercial Register and the German tax authorities control its application.[39] In Denmark, a joint taxation arrangement must be established to benefit from the international joint taxation regime.[40] In Finland, the contributing and the receiving companies must provide a statement regarding contribution modalities.[41] In Spain, group members have to establish a group agreement to be treated as a tax group.[42]

In order to be recognized as a tax group many of the Member States require that the accounting periods of all the group members coincide. This requirement is primarily explained by the need to treat the information relating to the tax group in a uniform manner.

In some Member States, a request must be submitted for a corporate group to be considered to form a tax group (Austria, Italy (for worldwide consolidation only), Luxembourg and the Netherlands). In other Member States, such as, Portugal[43] and Spain,[44] group members must inform the local tax authorities of the constitution of a tax group. These Member States often require a minimum duration in respect of the group interdependence.

In some cases, the constitution of a tax group is a right. In Denmark, for instance, group members applying to form a Danish tax group have a legal claim in respect of this status if the relevant legal conditions are met.[45]

Some Member States restrict the eligibility for a tax group status to companies meeting certain additional conditions. For Danish domestic and cross-border joint taxation, for instance, an administration company must be appointed, which is liable for the payment of corporate income tax. In general, the taxpaying parent company acts as the administration company.[46]

Some Member States, such as France and Poland, require a certain level of profitability from companies claiming a tax group status. Specifically, to form a Polish "tax capital group", the taxable income of the group companies must be at least 3% of the gross taxable revenues of the group companies.[47] Due to this stringent condition, the Polish tax group regime is inflexible and tax groups are rare in Poland.[48] A French corporate group that wishes to be considered as an international tax group must disclose its growth forecasts to the local tax authorities and demonstrate that its foreign industrial investments are important for its business activities.[49]

The result of all these requirements, especially taken together, is that there could be insufficient scope for tax groups. Consequently, many companies, even if they are related through strong economic control relationships, fall outside the scope of a tax group.

4. Group Taxation Regimes

4.1. Introductory remarks

The concept of "group taxation regime" refers to the rules that enables a tax group to compute its tax liability on a combined basis[50] and, therefore, to benefit from being considered as a single taxpayer. This section examines the group taxation regimes in the European Union (see Table 2).

37. European Commission, Common Consolidated Corporate Tax Base Working Group (CCCTB WG) Issues related to group taxation, Working Document, 5 May 2006, p. 7.
38. Sec. 14(1), No 3 KStG.
39. H-M Eckstein, "Germany", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 303.
40. Josephsen, note 15, p. 138.
41. Ranta-Lassila, note 16, p. 261.
42. Amparo Grau Ruiz, note 18, p. 616.
43. Dos Prazeres Lousa, note 8.
44. Amparo Grau Ruiz, note 18, p. 616.
45. C. Amby, "Denmark", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 237.
46. Josephsen, note 15, p. 138.
47. J. Kozinski, "Poland", *International Tax Review*, 2007 World Tax Supplement, p. 350.
48. R. Czarnecki, M. Grzymala and J. Galeza, "Older system requires creative approach", *International Tax Review*, April 2007, Mergers & Acquisitions, p. 53.
49. J.A. Borrat and A Bassière, "France", in IFA, "Group Taxation", *Cahiers de droit fiscal international*, Vol. 89b (Amersfoort: Sdu fiscale en financiële uitgevers, 2004), p. 279.
50. Masui, note 4, p. 25.

According to the degree of tax neutrality sought, group taxation regimes can be classified into three categories. The first category, referred to as tax relief regimes, offers limited tax neutrality by only granting tax relief to the parent company for the corporate taxes paid by the various group entities. This type of group taxation regime, which has not been adopted in the European Union, is typically applied in the United States. The second category, referred to as transfer regimes, goes further and permits certain amounts to be transferred from one group entity to another. This category includes the group contribution (see 4.2.2.) and group relief systems (see 4.2.3.). The third category recognizes a tax group as a single tax unit and, therefore, consolidates the revenues of the group members.[51] The German *Organschaft* and the consolidation systems fall into this category.

4.2. Transfer regimes

4.2.1. Initial comments

In order to highlight the differences between the various regimes, Example 1 has been created, which makes it possible to measure the effect of the regime on the tax basis and the amount of tax levied.

Example 1

A parent company (P) and its fully owned resident subsidiary (S) are both part of the same domestic tax group. Suppose that P receives 20 (i.e. 30) from S in payment of some intermediate product or intra-group service. Moreover, the revenues of S amount to 170, whilst P supports costs, which are estimated at 90. Consequently, P generates a result of 20 – 90 = –70 so that it realizes a loss (i.e. 30 – 90 = –60), though the taxable profit of S is positive, being 170 – 20 = 150 (i.e. 170 – 30 = 140). The corporate income tax rate in the Member State in question is 30% for S and 25% for P, assuming that the rate depends on the size of the taxable income or the region in which the entities are located. This is a simple way to anticipate on international tax design, though the example is entirely domestic. Alternatively, assume that S is a division or a branch of P recreated as unitary company (C) and take this case as a benchmark. The taxable profit of C is, then, 170 – 90 = 80, subject to a tax rate of 25%.

Without group taxation, each company is taxed separately. As loss-making companies are not subject to tax, P is not liable to pay taxes while S pays a tax amount of 45, i.e. 30% of 150 (i.e. 42, i.e. 30% of 140) (see Table 3). Obviously, the taxes due by the group, and, therefore, its after-tax value, depends on the distribution of the aggregate gross operating profit of 170 – 90 = 80 between the two entities, including the pricing of intra-group services or product transfers. Clearly, domestically, there is no tax neutrality.

Table 3: No group taxation regime

	Intra-group income	Other income	Total income	Tax base	Tax levied
Parent (P)	20	(90)	(70)	0	0
	30	*(90)*	*(60)*	*0*	*0*
Subsidiary (S)	(20)	170	150	150	45
	(30)	*170*	*140*	*140*	*42*
Unitary (C)	–	–	80	80	20
	–	–	*80*	*80*	*20*

4.2.2. Group contributions

The Swedish and Finnish group taxation regimes are commonly referred to as "group contribution" systems, as each group entity may, under certain conditions, contribute its profits to another group member,[52] according to the tax group's needs. The group contribution systems in Sweden and Finland are very similar.

According to these systems, each group entity is treated as a separate taxpayer, with its own accounts and its taxable income determined separately. A group company, however, has the opportunity to transfer ("contribute") some of its wealth (but not losses) to another group member. Through this contribution, a loss-making company can offset its losses against the profits contributed by a profit-making member of the group. Contributions are considered to be deductible expenses for the contributing entity and taxable revenue for the receiving company. In practice, contributions are primarily used by profit-making companies to reduce their tax liability. Loss-making group entities can, however, also use them.[53]

The Swedish and Finnish tax authorities require that wealth, i.e. profits, are effectively transferred from one group member to another. The corresponding liability and receivable must be booked in the accounts of the receiving and contributing companies.[54] In Finland, in contrast to Sweden,[55] the tax authorities also require the relevant revenue and expense to be recorded in the profit and loss account.[56] Each group member is liable for the taxes computed on its taxable income.

Group contributions can, in principle, only apply between resident entities. The contributing and the receiving entities have to be Swedish or Finnish companies, respectively. In order to conform to the decision of the ECJ in *X AB and Y AB*,[57] both Member States had, however, to amend their group taxation systems. In Sweden, group contribution is available for residents of the EEA from January 2001 onwards. To benefit from the group taxation regime, group entities must have a juridical form similar to Swedish companies and the receiving entity must be liable to Swedish taxation.[58] In practice, this means that contributions to a PE in Sweden from a non-Swedish but similar EEA company are deductible. In Finland, an identical situation was allowed by the Finnish Central Tax Board in one of its advance rulings. To date, Finnish corporate tax law has, however, not been amended.[59]

51. Van Ommeslaghe, note 5, pp. 25-26.
52. In Sweden, the "*Koncernbidrag*", is regulated by Chapter 35 *Inkomstskattelagen* and in Finland by the Group Contribution Act 1987.
53. S. Douma and C. Naumburg, "*Marks & Spencer*: Are National Tax Systems *Eclairé*?", *European Taxation* 9 (2006), p. 434.
54. Wiman, note 12, p. 636 and Ranta-Lassila, note 16, p. 259.
55. Wiman, note 12, p. 636.
56. Ranta-Lassila, note 16, p. 261.
57. ECJ, 18 November 1999, Case C-200/98, *X AB, Y AB v. Riksskatteverket*.
58. Wiman, note 12, pp. 645-646 and Douma and Naumburg, note 53, p. 433.
59. Ranta-Lassila, note 16, p. 265.

The group taxation rules did not, however, provide for the deduction of contributions to non-Swedish EEA subsidiaries. Following the ECJ decision in *Marks & Spencer*, some Swedish advance rulings[60] did, in certain conditions, disregard the juridical form of the receiving entity and extended the possibility for profit contributions to non-Swedish EEA subsidiaries. This possibility was, however, denied for non-Swedish EEA parent companies receiving contributions from a Swedish subsidiary. In Finland, a similar situation was subject to the ECJ decision in *Oy AA*,[61] in which a Finnish subsidiary claimed the deductibility of the contributions made to its UK parent company. In this case, the ECJ considered the Finnish group contribution regime to be in line with EC law. Accordingly, contributions to a foreign parent company are not permitted in Sweden or in Finland.

With reference to Example 1 and assuming that the Member State of the parent company and the subsidiary uses a group contribution regime, the tax situation is as follows:

Example 1 – continued

Table 4: Group contribution regime

	Intra-group income	Other income	Total income	Tax base	Tax levied
Parent (P)	20	(90)	(70)	0	0
	30	*(90)*	*(60)*	*0*	*0*
Subsidiary (S)	(20)	170	150	80	24
	(30)	*170*	*140*	*80*	*24*
Unitary (C)	–	–	80	80	20
	–	–	*80*	*80*	*20*

Companies benefiting from a group contribution regime can transfer their profit to a loss-making group member. Accordingly, S can contribute 70 (i.e. 60) of its profits to P, thereby reducing its taxable income to 80. As each group member is liable for the taxes computed on its taxable income, P is free of tax and S is charged a tax amount of 24. Consequently, the group's overall tax liabilities are reduced and the after-tax value of the group is increased. Nevertheless, tax neutrality is not attained, as the amount of tax levied is greater for S than in C.

4.2.3. Group relief

As with the Swedish and Finnish group contribution systems, group relief rules provide for some tax adjustments in order to take into account the economic unity of the corporate group. Group relief systems are primarily adopted in the Member States with a common law tradition, i.e. Cyprus, Ireland, Malta and the United Kingdom, as well as Latvia.

There are various tax relief rules. One tax relief relates to the transfer of losses within a tax group. Under this relief, a group member (the surrendering company) can, in specific conditions, transfer (surrender) certain amounts, such as trading losses, to another entity in the tax group (the claimant company).[62] In contrast to Sweden and Finland, the UK corporate tax legislation permits losses, but not profits, to be allocated to other group entities. As such, amounts do not have to be transferred and losses can virtually be attributed to another group member.[63] Due to such transfers, profit-making group members can offset their taxable incomes and reduce or eliminate their tax payments. As with the group contribution system, every group entity must compute its tax bases and is taxed on it separately.

The UK group relief regime has been questioned via the ECJ in *Marks & Spencer*. The UK company, Marks & Spencer plc, having tax losses in its non-resident EU subsidiaries, wanted to offset these tax losses against its UK profits. As the UK tax authorities ruled that this was not possible, the company appealed, claiming that the group relief system was not in line with EC law. In its decision, the ECJ considered the UK's objectives (i.e. a balanced allocation of taxing powers between the Member States, the prevention of the double use of losses and the restriction of tax avoidance) to be legitimate but held that, in some situations, they did not respect the principle of proportionality as they could be attained by less restrictive measures. The situations in which the UK tax regime constituted an infringement of the EC law were clarified in the ruling i.e. when:

> the non-resident subsidiary has exhausted the possibilities available in its State of residence of having the losses taken into account for the accounting period concerned by the claim for relief and also for previous accounting periods ... and there is no possibility for the foreign subsidiary's losses to be taken into account in its State of residence for future periods either by the subsidiary itself or by a third party ...[64]

Example 1 – continued

The application of a group relief regime to Example 1 results in similar tax bases and tax liabilities as under a group contribution regime, although the underlying mechanisms differ. This time P surrenders its losses, whilst previously S contributed its profits. As under a group contribution regime, each group member is liable for the taxes computed on its taxable income. Again, tax neutrality is not realized.

Table 5: Group relief regime

	Intra-group income	Other income	Total income	Tax base	Tax levied
Parent (P)	20	(90)	(70)	0	0
	30	*(90)*	*(60)*	*0*	
Subsidiary (S)	(20)	170	150	80	24
	(30)	*170*	*140*	*80*	*24*
Unitary (C)	–	–	80	80	20
	–	–	*80*	*80*	*20*

60. Dnr 206-04/D and Dnr 193-04/D, 29 September 2006.
61. ECJ, 18 July 2007, Case C-231/05, *Oy AA*.
62. Rupal, note 11, p. 688.
63. H.J. Ault and B.J. Arnold, *Comparative Income Taxation, A Structural Analysis* (The Hague: Kluwer Law International, 2004), p. 322.
64. ECJ, 13 December 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, Para. 55.

Table 6: Overview of tax consolidation regimes				
	Legal personality	**Reach**	**Obligation to use**	**Degree**
Austria	No	Cross-border	Optional	Domestic: total cross-border: proportional
Denmark	No	Cross-border	Domestic: compulsory cross-border: optional	Domestic: total Cross-border: proportional
France	No	Cross-border	Domestic: optional cross-border: compulsory	Total
Italy	No	Cross-border	Domestic: optional cross-border: compulsory	Domestic: total cross-border: proportional
Luxembourg	No	Domestic	Optional	Total
The Netherlands	Yes	Domestic	Optional	Total
Poland	No	Domestic	Optional	Total
Portugal	No	Domestic	Optional	Total
Slovenia	No	Domestic	Optional	Total
Spain	No	Domestic	Optional	Total

4.3. Consolidation regimes

4.3.1. Initial comments

Tax consolidation enables the overall income of the various group members to be allocated to the sole parent company and allows the taxation of the corporate group only once. This category of group taxation systems (see Table 2) also reflects the reality of a single economic unit and ensures tax neutrality. Tax consolidation systems can, however, be differentiated according to various criteria, i.e. the existence of legal personality, the reach and degree of consolidation and the obligation of using the consolidation system.

4.3.2. Legal personality and partial or full consolidation

4.3.2.1. Key distinguishing factors

A key distinction must be made between methods that refrain from assigning legal personality to the tax group (the pooling of taxable incomes or partial tax consolidation) and those that assign such personality to the tax group (full tax consolidation) – see Example 2.

Example 2

To appreciate the difference between the two methods, consider a parent company (P) with a fully owned resident (domestic) subsidiary (S), which is part of the same domestic tax group. Suppose P has an extra-group operating income of 400 and extra-group operating charges of 100. S only sells its services to P, generating an operating income of 150 and charges of 80. P has also sold shares and fixed assets to S that give rise to a capital gain of 20 for the share sale and a capital gain of 15 for the fixed asset sale. The corporate income tax rate in the Member State in question is 30%.

In the absence of group taxation, each company is taxed separately. P is taxed on its operating profit, 400 – 150 – 100, as well as on the capital gains, 20 + 15, i.e. on 185, and is required to pay tax amounting to 55.5, i.e. 30% of 185. Based on a taxable income of 150 – 80 = 70, S pays tax of 21, i.e. 30% of 70. Again, the unitary case, operating through divisions or branches, is tentatively used as a benchmark. In that case, the taxable income is 400 – 100 – 80 = 220. This benchmark reveals the lack of tax neutrality if there is no group taxation regime.

Table 7: No group taxation regime				
	Income	**Taxable income**	**Tax rate**	**Tax levied**
Parent (P)	185	185	30	55.5
Subsidiary (S)	70	70	30	21.0
Tax group				76.5
Unitary (C)	220	220	30	66.0

4.3.2.2. Partial tax consolidation

The primary consolidation technique used in the European Union is a pooling system. Under this system, the tax bases of the separate group members are aggregated and jointly taxed. This group taxation regime takes into account the legal personality of each group entity and, therefore, the tax group is not assigned a fiscal personality. Moreover, the tax bases are not necessarily adjusted for intra-group transactions. The taxable incomes and losses are first calculated for each group member separately, i.e. on a company-by-company basis. Then, the common taxable income is computed by aggregating taxable incomes and tax losses.

Subsequently, this common tax income is attributed to the parent company, which is responsible for paying tax for the tax group. In contrast to group contributions (see 4.2.2.) and group relief (see 4.3.3.), the parent company is the only beneficiary of the profit allocations, other group members being excluded from any wealth transfer. As the parent company is taxed by its local tax authorities, only the tax rate of the parent's Member State applies. All group members are, however, jointly liable for the tax payment toward the Member State. Some Member States, such as Denmark, do even provide for special rules regarding the distribution of the corporate income tax amongst the group members.[65] It should be noted that the consolidated taxable income is determined independently of the consolidated profit of the

65. Amby, note 45, p. 241.

corporate group computed for accounting purposes. No accounting consolidation is, therefore, required to apply tax consolidation.

Member States using a group taxation regime based on these principles include Austria, Denmark, France, Italy, Luxembourg, Poland, Portugal, Slovenia and Spain. The French[66] and the Spanish tax legislation require the elimination of intra-group transactions, but the tax legislation of other Member States does not. The Member States permitting international tax consolidation, such as Denmark and France, often use the same rules for domestic and cross-border consolidation.

In Germany, a specific type of partial tax consolidation applies, i.e. the *Organschaft*[67] or integration. Under this system, group entities are considered to be "inner organs", strongly integrated in the economic activity of the parent company.[68] By way of a pooling agreement, concluded with the parent company (the *Organträger*), group entities (*Organgesellschaften*) are committed to assigning their entire profits and losses to the parent company,[69] both for tax and commercial purposes. Group entities are considered to be doing business for the profit of the parent company and, as such, are considered to be PEs of the parent company.[70] The tax profits and losses of the separate group entities are computed on an individual basis and are then attributed to the parent company.[71] As such, the group entities are considered to have neither profits nor losses.[72] The primary consequence of a profit and loss agreement is that it makes parent company and group entities liable for each another.

Since the corporate tax reform of 2005, the *Organschaft* no longer applies in Austria. Specifically, the Austrian tax authorities abolished it and introduced a tax consolidation system, thereby reducing the restrictions on the offset of losses of one group member against the profits of another member.[73]

Example 2 – continued

Suppose that the tax legislation of P's Member State provides for a consolidation adjustment for capital gains on share sales, but not for capital gains on fixed assets. The tax bases of the separate group members are first computed and the adjustment for the capital gains on share sales is only made when both tax bases have been aggregated. The tax bases of P and S are identical to those observed in the absence of a group taxation regime. Once they are pooled, however, the adjustment of 20 is made and there is a tax base of 185 + 70 – 20 = 235.

Table 8: Partial tax consolidation regime without elimination of all intra-group incomes

	Income	Taxable income	Tax rate	Tax levied
Parent (P)	185	165		
Subsidiary (S)	70	70		
Tax group		235	30	70.5
Unitary (C)	220	220	30	66.0

4.3.2.3. *Full tax consolidation*

The Netherlands are the only Member State using a tax consolidation regime (*fiscale eenheid*), in which the legal personality of each group entity is completely disregarded for tax purposes.[74] No distinction is made between the result of the group members and that of the parent company. A corporate group is considered having a proper legal personality from a tax point of view. From a technical viewpoint, the taxable income of the different group entities is first computed separately and then the income from intra-group transactions is neutralized.

The sum of these adjusted incomes is attributed to the parent company and the tax group is considered to be a fiscal unity with one set of accounts aggregating the results as well as all assets and liabilities of the entities.[75] The parent company files one corporate income tax return for the entire group[76] and is taxed in its resident Member State as if there was a single taxpayer.[77] As under pooling consolidation, the liability to pay the levied tax is jointly assigned to all subsidiaries.[78]

The full tax consolidation system has the particularity of allowing the elimination of all income related to intra-group transactions. Accordingly, the tax base of the parent company, which absorbs all profits and losses of the tax group, is limited to 220, i.e. 400 –100 – 80. A total tax of 66 is levied at the level of the parent company. This constitutes the lowest tax charge observed in the case in hand. A comparison of the penultimate and last lines of Table 9 reveals that eventually domestic tax neutrality has been achieved.

Table 9: Full tax consolidation regime

	Income	Taxable income	Tax rate	Tax levied
Parent (P)	185			
Subsidiary (S)	70			
Tax group		220	30	66.0
Unitary (C)	220	220	30	66.0

66. Ault and Arnold, note 63, p. 323.
67. European Commission, Common Consolidated Corporate Tax Base Working Group (CCCTB WG) Issues related to group taxation, Working Document, 5 May 2006.
68. Masui, note 4, p. 770.
69. Sec. 291 *Aktiengesetz* and D. Endres, C. Schreiber and P. Dorfmueller, "Holding companies prove worth", *International Tax Review*, December 2006/January 2007, Vol. 18, Issue 1, pp. 43-46.
70. Douma and Naumburg, note 53, pp. 436-437.
71. Eckstein, note 39, p. 305.
72. Ault and Arnold, note 63, p. 324.
73. Hoeing and Schmidt, note 29.
74. European Commission, "Tax Treatment of Losses in Cross-Border Situations", Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee, 19 December 2006, COM(2006) 824 final, Technical Annexes, p. 5.
75. Art. 15(1) CITA.
76. Douma and Naumburg, note 53, p. 439.
77. S. Douma,, "*Marks & Spencer* and the tax consolidation regime", *International Tax Review*, September 2006, Vol. 17, Issue 8, pp. 72-73.
78. De Vries, note 9, p. 468.

Example 1 – continued

Finally, reconsider Example 1 and Tables 3 and 4. Now, the consolidated tax base is attributed to the parent entity and taxed at that company tax rate, i.e. 25%. Accordingly, tax neutrality is achieved domestically.

Table 10: Full tax consolidation regime - continued

	Intra-group income	Other income	Total income	Tax base	Tax levied
Parent (P)	20	(90)	(70)	80	20
	30	*(90)*	*(60)*	*80*	*20*
Subsidiary (S)	(20)	170	150	0	0
	(30)	*170*	*140*	*0*	*0*
Unitary (C)	–	–	80	80	20
	–	*–*	*80*	*80*	*20*

4.3.3. Domestic versus cross-border consolidation

4.3.3.1. National or domestic consolidation

National consolidation consists of consolidating the taxable incomes of the sole resident or domestic group members. Such a pure national tax consolidation system exists in Luxembourg, the Netherlands, Poland, Portugal, Slovenia and Spain.

In principle, entities willing to belong to a tax group of one of these Member States should have their fiscal residence in that Member State. There are, however, several exceptions to this principle. Since the Netherlands tax reform (1 January 2003), for instance, various provisions have been inserted into Netherlands tax law to permit some foreign entities with their fiscal residence outside the Netherlands and some Netherlands entities with their effective management abroad to apply the tax consolidation rules, provided that certain specific requirements are met. One of the main requirements is the existence of a PE in the Netherlands whose profit is subject to Netherlands tax.[79] The same tax rules must also apply to the other group members.[80]

4.3.3.2. International or cross-border consolidation

International consolidation consists in consolidating the taxable incomes of all group companies, regardless of whether these companies are residents or non-residents of the parent's Member State. According to the type of consolidation system, the common taxable income is computed on the basis of the previously noted consolidation rules. Such international tax consolidation has already existed for some time in Denmark (1960, amended in 2004, i.e. international joint taxation) and France (1966, *régime du bénéfice consolidé*) and was recently introduced in Austria (2005) and Italy (2004, worldwide consolidation) and, therefore, permits greater tax neutrality in these Member States.

As noted in the previous paragraph, Austria, Denmark, France and Italy all apply a pooling consolidation system for resident group companies. Except in Austria, the same pooling rules are used for international tax groups. Some special provisions were, however, introduced to deal with non-resident group entities. The main adjustments required relate to the computation of the taxable income.

As each company computes its financial accounts according to local rules and in its local currency, some recomputations and conversions must be made to include a non-resident entity in a tax group. In Denmark, a non-resident subsidiary must calculate its taxable income in its local currency, but according to Danish rules. Once the tax basis has been computed, it is translated into Danish currency.[81]

The double taxation of the common income is eliminated by granting tax relief to the parent company for the foreign taxes paid by the non-resident group members. In Italy, the use of the foreign tax relief is limited to the amount of the Italian tax incurred on these incomes.[82] Tax relief is also restricted in Denmark.[83]

In order to avoid tax losses to be offset twice, the Danish tax legislation states that, if the loss of a non-resident group member is offset against profits of third companies, it cannot be offset against the joint taxable income (an anti-"double dip" provision).[84] Under Austrian tax law, the offset of foreign losses generated before the constitution of the tax group is only possible against the profits of the group member that generated the losses.[85]

When introducing an international group taxation regime, the Austrian legislator decided not to apply the same type of regime to domestic and foreign group members. In contrast to resident members who benefit from a tax-pooling regime, a form of group relief system applies to foreign group members. Under Austrian international group consolidation, only losses, and not profits, can be transferred from a non-resident group member to a resident one.[86]

Following the ECJ decision in *Marks & Spencer* regarding the UK group taxation system, the Netherlands considered introducing an international consolidation regime. The Advocate General in *Marks & Spencer* opined that, if losses in an EU subsidiary could benefit from a tax loss transfer in its resident Member State, it should be able to benefit from the same treatment when inserted into the group taxation system of its parent company located in another Member State. Following the Advocate General's opinion, the Netherlands proposed proactively to change its full tax consolidation system to permit non-resident subsidiaries to be included in the Netherlands corporate group. On 29 April 2005, the Netherlands government published a

79. Id., p. 475.
80. Ault and Arnold, note 63, p. 323.
81. Amby, note 45, p. 244.
82. G. Marino and A. Ballancin, "The Italian Corporate Tax Reform: U.S. Outbound Update", *International Tax Journal,* Spring 2004, Vol. 30, Issue 2, p. 36.
83. Amby, note 45, p. 246.
84. Id.
85. Sec. 9(6), No. 6 KStG.
86. Gahleitner and Ratzinger, note 13.

memorandum outlining the changes required to transform the domestic tax consolidation regime into an international one (mainly foreign loss compensation for non-resident entities).[87] As the ECJ's decision in *Marks & Spencer* did not completely follow the Advocate General's opinion and did not create an obligation to insert an international consolidation system, the Netherlands did not implement the contemplated changes.

Example 2 – continued

Example 2 and Tables 7 to 9 should, therefore, be reconsidered, but in an international context with the subsidiary and the PE assumed to be located abroad. In this context, it should be noted that, for a PE, no shares are supposed to be traded with the parent company. It is also assumed that the tax rate is 25% in the parent Member State and 30% abroad, with the tax paid abroad credited against the consolidated tax liabilities in the parent Member State.

It can be observed that, in the example, partial consolidation ensures tax neutrality with regard to the organizational form or "domestic" neutrality. In addition, full consolidation introduces a form of "international" tax neutrality. As long as the tax rate in the parent Member State is not less than that in the subsidiary or branch Member State, capital export neutrality applies, by which is meant that the income of the subsidiary, respectively the branch, is taxed identically wherever it is located, at the tax rate of the parent entity. Full consolidation does not, however, imply the other aspect of "international" tax neutrality, i.e. capital import neutrality. Indeed, the location of the parent entity determines the size of the tax liabilities. Clearly, full tax neutrality requires not only full tax consolidation but also cross-border equalization of the tax rates.

4.3.4. Optional versus compulsory consolidation

In almost all Member States, the application of the tax consolidation regime is optional, i.e. multinational companies must request the application of the tax consolidation system. In all Member States, except for Denmark, France and Italy, companies can choose which group members to include in the tax group ("cherry-picking"), provided that the electing entities qualify. In Denmark, some companies, such as non-resident parent companies, must join the consolidation regime.[88] Optional consolidation allows the development of strategic behaviour by multinational companies.[89]

The only compulsory consolidation systems in the European Union are the Danish domestic joint taxation regime[90] and the French[91] and Italian[92] international consolidation systems. In order to reduce tax avoidance possibilities, the Danish parliament decided to limit the free choice of participating entities. Accordingly, all related Danish companies and PEs in Denmark of non-resident companies must be included in the tax group and are subject to the group taxation regime.[93] In Italy, the corporate group can decide whether or not to include non-resident entities within the tax group. Once it has opted for a worldwide consolidation system, however, the tax group must include all non-resident companies (the "all-in or all-out" option).[94]

In most Member States, the election for group taxation is binding for a certain period. This varies greatly from one Member State to another, i.e. in Denmark the period is ten years,[95] in Portugal, five years,[96] and, in Austria, three years.[97] There is no time requirement in the Netherlands.[98]

4.3.5. Proportional versus total consolidation

Some Member States apply a proportional consolidation system, i.e. partial consolidation of the profit or losses of the group entity according to the effective shareholding

87. A. Van der Smeede and A. Sibarani, "Tax changes aimed at attracting international business", *International Tax Review*, September 2005, Vol. 16, Issue 8, p. 48.
88. Josephsen, note 15.
89. See the examples in M. Gerard, "Reforming the taxation of multijurisdictional enterprises in Europe: a tentative appraisal", *European Economy*, Economic Papers of the DG Economy and Finance, EU Commission, 2006, p. 47 and "Reforming the Taxation of Multijurisdictional Enterprises in Europe", *CESifo Economic Studies*, 2007, pp. 329-361.
90. Josephsen, note 15.
91. Borrat and Bassière, note 49.
92. Marino and Ballancin, note 82.
93. Josephsen, note 15, p. 138.
94. Marino and Ballancin, note 82.
95. Josephsen, note 15, p. 138.
96. Dos Prazeres Lousa, note 8.
97. C. Hasenauer and J. Prinz, "What the 2005 reforms will mean", *International Tax Review*, March 2005, Vol. 16, Issue 3, p. 54.
98. De Vries, note 9, p. 473.

Table 11: Steps towards cross-border consolidation

	No consolidation+		Partial consolidation		Full consolidation	
	Taxable Income	Tax levied	Taxable income	Tax levied	Taxable Income	Tax levied
Parent (P)	185	46.25	165		150	
Subsidiary (S)	70	21	70	21	70	21
Tax group		67.25++	235	58.75*	220	55**
Parent (P)	165	41.25	165		150	
Branch (C)	70	21	70	21	70	21
Tax group		62.25+++	235	58.75*	220	55**

+ The tax paid abroad may be credited against tax liabilities in the parent Member State (tax relief mechanism).
++ 67.25 – 21 = 46.25 to be paid to the tax authorities of the parent Member State and 21 to be paid to the tax authorities of the subsidiary Member State.
+++ 62.25 – 21 = 41.25 to be paid to the tax authorities of the parent Member State and 21 to be paid to the tax authorities of the subsidiary or branch Member State.
* 58.75 – 21 = 37.75 to be paid to the tax authorities of the parent Member State and 21 to be paid to the tax authorities of the branch Member State.
** 55 – 21 = 34 to be paid to the tax authorities of the parent Member State and 21 to be paid to the tax authorities of the subsidiary or branch Member State.

of the parent company into this entity. The use of such proportional system is proper to the international consolidation regimes in Austria, Denmark and Italy. In Austria, it is also used in domestic situations if a participation pool acts as parent company of the tax group.[99]

Other Member States have opted for a total consolidation system, which means that all the profits or losses of the group entity are consolidated, regardless of the effective shareholding of the parent company in that group entity.[100] Specifically, Austria,[101] Denmark[102] and Italy[103] have opted for a 100% attribution of profits and losses with regard to their domestic consolidation regime.

5. Conclusions

There is no doubt that heterogeneity is a primary characteristic of the taxation of corporate groups in the European Union. There is also no doubt that some entities can profit from this heterogeneity and exhibit strategic behaviour selected accordingly. It is, however, clear that the related opacity and the requirement to be aware of so many different tax systems create obstacles for other companies wishing to develop EU-wide activities and to operate in the Single Market.

As responsible for the operation of the Single Market, the Commission has decided to remove the tax obstacles to the operation of the Single Market and to eliminate the discriminations amongst companies in terms of the need to be aware of as many tax systems as there are Member States.[104] Accordingly, there are now discussions in progress concerning the CCCTB. This project has two pillars, i.e. a common way to define and compute a consolidated tax base, on the one hand, and formulary apportionment of the common consolidated tax base, on the other.

Clearly, as illustrated by Examples 1 and 2, consolidation negates many profitable strategies, characterized by "paper profits". If, however, there is no room for these paper profits, tax competition between the Member States could increase. In other words, if small tax reductions are no longer an efficient way of attracting mobile tax bases at little cost, large tax reductions will remain the efficient tool for attracting mobile investments, but at a high cost.

Whether consolidation will increase or reduce tax competition and its negative consequences for public expenditure and distribution, will greatly depend on the apportionment formula adopted. In particular, if the distribution of the consolidated tax base depends on factors that, for a large part, are outside an entity's control, such as the location of demand and sales,[105] tax competition is likely to be reduced by the CCCTB. In contrast, if the distribution of the consolidated tax base depends on factors that an entity can manipulate, such as the location of plant and employment, tax competition is likely to be increased by the CCCTB. The choice of the formula is, therefore, of primary relevance and useful lessons can be drawn from the experience of countries, such as Canada and the United States, in this respect.[106]

Eventually, tax neutrality can only be achieved if the governments of the Member States not only decide on a common consolidated corporate tax base, but also on a common tax rate. Unfortunately, the compatibility of such a programme with the principle of subsidiary is questionable.

99. Gahleitner and Ratzinger, note 13, p. 512.
100. European Commission, Common Consolidated Corporate Tax Base Working Group (CCCTB WG) Issues related to group taxation, Working Document, 5 May 2006, p. 7.
101. M. Tas, M., "Oostenrijk: ingrijpende belastinghervorming ingevolge EU-uitbreiding", *Intern. Fisc. Act* (2004), No. 8, p. 5.
102. Josephsen, note 15.
103. Giaconia, note 31, p. 386.
104. European Commission, "Towards an Internal Market without tax obstacles. A strategy for providing companies with a consolidated corporate tax base for their EU-wide activities", Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee, 23 October 2001, COM(2001) 582.
105. Gerard, *European Economy*, note 89 and *CESifo Economic Studies*, note 89.
106. J. Martens-Weiner, *Company Tax Reform in the European Union: Guidance from the United States and Canada on Implementing Formulary Apportionment in the EU* (New York: Springer Science+Business Media, 2006).