Company taxation: Commission proposes improvements to Mergers Directive

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The European Commission has made a proposal to update, clarify and broaden the scope of the European Community's Directive that provides for tax deferral in the case of cross-border mergers and divisions of companies, transfers of assets and exchanges of shares (90/434/EEC). In particular, the Commission proposes to broaden the Directive's scope to cover a larger range of companies including the European Company (see IP/01/1376) and the European Co-operative Society (see IP/03/1071); to provide for a new tax neutral regime for the transfer of the registered office of a European Company or of a European Cooperative Society between Member States; to clarify that the Directive applies in the case of the conversion of branches into subsidiaries; and to introduce rules to prevent double taxation due to different valuations of shares and assets by different Member States.

"This proposal is an important element of our strategy to remove all forms of double taxation and other tax obstacles currently encountered by companies exercising their freedom to operate across borders within the Internal Market" commented Taxation Commissioner Frits Bolkestein. "This proposal, combined with the forthcoming proposal for a Tenth Company Law Directive facilitating mergers between companies from different Member States, would increase the efficiency of business and support the objective of making the EU the most competitive economy in the world by 2010".

The proposal is an element of the Commission's company tax strategy presented in 2001 (see IP/01/1468) in which the Commission identified a number of tax obstacles to cross-border economic activity in the Internal Market, such as high compliance costs and international double taxation, and announced its plans for short- and long-term Community action to remove them.

The proposal

The main elements of the Commission proposal to improve the operation of the "Mergers" Directive are as follows:

First, the proposal would update the list of companies to which the Directive applies to cover new, specified, legal entities, including certain co-operatives and non-capital based companies, mutual companies, savings banks, funds and associations with commercial activity. The new list would include the European Company and the European Co-operative Society that can be created from 2004 and 2006, respectively, with the result that companies and co-operatives operating in more than one Member State will have the option of establishing themselves as single entities under Community law.

Second, the proposal would ensure that the transfer of the registered office of a European Company or of a European Co-operative Society from one Member State to another would not result directly in taxation of capital gains. The intention is that the facility to make such a transfer, which is specifically provided for in the Statutes governing those entities, would not be hampered by discriminatory tax rules or by restrictions or distortions that would violate the EC Treaty.

Third, the proposal would clarify that the tax deferral regime in the Directive can apply where a company decides to convert its foreign branch into a subsidiary.

Fourth, the proposal would ensure that the values of securities and assets exchanged in cross-border mergers and divisions are calculated the same way for tax purposes in different Member States when they are ultimately subjected to tax.
The proposal replaces a previous 1993 proposal to amend the Mergers Directive (see IP/93/637) and the Commission has, consequently, now withdrawn the previous proposal. Member States could not agree to the wide scope of the earlier proposal because of the asymmetries in their commercial laws governing the types of legal entities and in the tax arrangements applicable to these entities.

**Background**

Directive 90/434/EEC of 23 July 1990 provides for the deferred taxation of capital gains arising from cross-frontier company restructuring carried out in the form of mergers, divisions, transfers of assets or exchanges of shares. Taxation of the capital gain is deferred until a later disposal of the assets.

The adoption of proposals to update and expand the scope of the Parent-Subsidiary Directive (90/435/EEC) and the Mergers Directive were among the short-term targets that the European Commission set itself in October 2001 when it presented its strategy for company taxation in the EU. The Commission presented a proposal to update the Parent-subsidiary Directive in July this year (see IP/03/1214). The Commission believes that, in the longer term, companies should be allowed a single consolidated corporate tax base for all their EU-wide activities to avoid the current costly inefficiencies of fifteen separate sets of tax rules.