COUNCIL OF THE EUROPEAN UNION

Brussels, 27 May 2005

9427/05

LIMITE

FISC 55

REPORT

From :	Code of Conduct Group (Business Taxation)
to :	the ECOFIN Council
on:	7 June 2005
Subject :	Code of Conduct (Business Taxation) - Report to the ECOFIN Council

INTRODUCTION

1. The Council and the Representatives of the Governments of Member States, meeting within the Council, adopted on 1 December 1997 a Resolution on a Code of Conduct for business taxation which provides for the establishment of a Group within the framework of the Council to assess tax measures that may fall within the Code. In its report to the Feira European Council on 19 and 20 June 2000, the ECOFIN Council agreed that work should be pursued with a view to reaching agreement on the tax package as a whole, according to a parallel timetable for the key parts of the package (Taxation of savings, Code of Conduct (Business Taxation) and Interest and Royalties).

2. On 9 March 1998, the Council confirmed the establishment of the Code of Conduct Group. The Group has reported regularly on the measures assessed and these reports have been forwarded to the Council for deliberation.

3. Two interim reports of the Code of Conduct Group were presented to the ECOFIN Council on 1 December 1998 and 25 May 1999 respectively (12530/98 FISC 164 and 8231/99 FISC 119). Subsequently, the Group reported to ECOFIN on 29 November 1999 setting out the results of the Group's work (SN 4901/99) on the assessment of 271 tax measures under the Code where 66 measures were considered harmful by the Group.

4. On 13 October 2003, the Council welcomed a report by the Working Party on Enlargement (Tax Experts) (13213/03 ELARG 94 FISC 138) establishing a list of 30 measures in the acceding States found harmful under the Code. The Council also agreed on the adequacy of the rollback measures envisaged or already undertaken for 27 of these measures.

5. On 26-27 November 2000, the Code Group presented a progress report on its work to the ECOFIN Council (13563/00 FISC 193). Further progress reports on the Code Group's work were presented to the ECOFIN Council on 5 June 2001 under the Swedish Presidency, on 4 December 2001 under the Belgian Presidency, on 4 June 2002 under the Spanish Presidency, on 3 December 2002 under the Danish Presidency, on 7 March 2003 under the Greek Presidency, on 25 November 2003 under the Italian Presidency and on 7 December 2004 under the Netherlands Presidency (8789/01 FISC 83, 14467/01 FISC 249, 8848/02 FISC 129, 14812/02 FISC 299, 7018/1/03 FISC 31 REV 1, 14361/03 FISC 173 and 15317/04, FISC 249).

6. This latest report from the Code Group to the ECOFIN Council encompasses the work of the Code Group in 2005 under the Luxembourg Presidency.

7. As required by the ECOFIN conclusions of 9 March 1998, the Group's report to the 29 November 1999 ECOFIN Council reflected either the unanimous opinion of the members of the Group or the various opinions expressed in the course of discussion. References to 'the Group' in that report reflected the broad consensus where unanimity was not achieved and alternative views were shown in the notes as appropriate. Consistent with the Group's report to the 29 November 1999 ECOFIN, references to 'the Group' in this and other reports should be construed in the same way.

PROGRESS OF WORK

8. Since the ECOFIN Council meeting on 7 December 2004, the Code of Conduct Group has met on 24 February 2005 and 24 May 2005 under the Luxembourg Presidency.

9. Under paragraph 8 of the ECOFIN conclusions of 9 March 1998, if the Member State which holds the Chair also holds the Presidency of the Council, that Member State is excluded from holding the Vice-Chair for the six-month period of its Presidency and the preceding six months. As the UK holds the Presidency in the second half of 2005, there is only one Vice-Chair of the Code Group in 2005. Therefore, at the Code meeting on 24 February, Mr Gaston Reinesch, Director General of the Ministry of Finance in Luxembourg was confirmed as the sole Vice-Chair for the period up to the end of the Luxembourg Presidency.

10. The Group confirmed its programme of work for the period to June 2005 under the Luxembourg Presidency. The Group's work focused on the following two areas:

- implementation of rollback
- standstill.

(a) Implementation of rollback

11. Members of the Group were asked to provide information on any developments since the Group's December 2004 report (15317/04 FISC 249) on the implementation of rollback of measures on the list in Annex C of SN 4901/99 and the measures included in the report of the Working Party on Enlargement (Tax Experts) (13213/03 ELARG 94 FISC 138).

12. The Group noted that measure SL2 (Slovenia- Foreign Income) had been rolled back. The new foreign income measure and respective anti-abuse measure came into force on 1 May 2004.

13. The Code Group's report dated 26 November 2002 (14812/02) set out the British Virgin Islands intention to abolish measure F056 (International Business Companies) by amalgamating the local Companies Act with the International Business Companies Act into a single statute. The Group was informed that the legislation to put this into effect is now in force. The Group invited the UK to provide a report on the recent changes to the structure of the tax system in BVI in time for its next meeting.

14. The group was also informed that the provisions of the Republic of Lithuania "Law on Tax on Profit" and "Law on the Fundamental of Free Economic Zones stipulating the taxation of business entities established in free economic zones in the Republic of Lithuania" have been amended and potentially discriminatory benefits for non-resident companies and the possibility of applying tax benefits to banking and insurance activities in free economic zones in the Republic of Lithuania have been abolished. The latter amendments to Lithuanian legislation removing harmful tax measures were enacted on 1 of May 2004.

15. The Group was also notified that the law making the modifications to achieve the rollback of Luxembourg 1929 holding companies (A0013) was passed by the Luxembourg Parliament on 19 April 2005. The Group noted the rollback of this measure but also noted that Luxembourg had not complied with the original rollback proposal, because the regime, which should have been closed to new entrants from 2001, will not be closed to new entrants until 1 July 2005.

16. The Group considered a document agreed by Malta and the Commission explaining the rollback proposal provided by Malta in respect of the measures International Trading Companies (ML4) and Dividends from (other) Maltese Companies with Foreign Income (ML5). However, the Group's decision on whether the rollback proposals were acceptable was deferred to the first meeting of the Group under the UK presidency.

17. The Group considered the rollback proposal provided by the Czech Republic in respect of the measure Czech Republic: Investment Incentives (CZ1). With the benefit of a document from the Czech Republic explaining the measures, the Group agreed that the rollback measure was adequate. It was agreed that a formal evaluation of the measure was not necessary.

18. As reflected in the Group's report to ECOFIN in December 2004, B013 (UK: Gibraltar – Qualifying (offshore) Companies and Captive Insurance) has already been abolished and A017 (UK: Gibraltar – 1992 Holding Companies) is, in practice, ineffective but has not yet been rolled back. The Group was informed of a Commission decision under State aid rules, formally accepted by the UK and the Government of Gibraltar, according to which the Government of Gibraltar is committed to the phased abolition of B012 (UK: Gibraltar – Exempt (offshore) Companies and Captive Insurance), with a reducing number of new entrants until June 2006 and existing beneficiaries able to continue to benefit from the regime until the end of 2010.

19. The Code Group asked the UK for a new proposal in accordance with the ECOFIN of 7 December 2004. The Group therefore urged the UK: Gibraltar to look for an urgent rollback solution in relation to measure B012, in particular relating to not having new entrants in 2005, noting that the measure should have been closed to new entrants in 2001[1].

(b) Standstill

20. Member States are committed not to introduce new tax measures which are harmful within the meaning of the Code.

21. In view of this ongoing commitment, at the Code meeting on 24 February, Member States were invited – in accordance with the Code Group's established practice - to assist the Group in its work by notifying to the Commission services any new measures which potentially fall within the scope of the Code of Conduct and which have been enacted in the twelve months to end-January 2005. Two Member States notified measures to the Group (Slovenia – various measures; Ireland – Holding Company Measure) and one matter was held over from the December 2004 report to ECOFIN (Greece: replacement measure for Tax Incentives for Investment).

[1] Referring to its footnote in the Group's previous report (15317/04) the UK noted that, in these circumstances, the acceptance of the State aid decision constituted the best possible, most practical and legally binding, rollback proposal, stressing that, notwithstanding the absence of certainty about the future tax provisions in Gibraltar, measure B012 was nonetheless now being rolled back.

22. The Group considered these notifications and concluded that:

- Slovenia's measures relating to participation exemption of revenues from profit participation, exempt entities, investment incentives allowance, taxation of interest and royalties, and implementation of the Parent-Subsidiary, Interest and Royalties and Mergers Directives; and
- Ireland's Holding Company measure did not require assessment under the Code.

23. Greece Tax Incentives for Investment **-** The December 2004 report to ECOFIN had required the replacement measure for Greece's Tax Incentives for Investment to be notified to the Code of Conduct Group in the 2005 round of work on standstill. The Group agreed that the new law which has replaced the previous measure and which was notified to the Group does not require assessment under the Code.

24. Netherlands – New Fiscal Framework in Aruba: As agreed at the Group's meeting in November 2004, the Netherlands delegation reported back to the meeting of the Group on 24 February 2005, following discussion with Aruba, on the rollback proposal for this measure. The Group's work on the evaluation of rollback was informed by an explanatory document from the Netherlands and by revised assessments which had been prepared by the Commission services, in discussion with the Chair, against criteria 1 to 5 of paragraph B of the Code. As a result, the Group accepted that the replacement regime was not harmful under the Code criteria and that the harmful aspects of this measure had been adequately rolled back.

25. The Group considered the standstill description provided by Hungary in respect of the measures: Revenue from Stock Exchange Operations, Interest from affiliated companies and Royalty Income. With the benefit of a document agreed by Hungary and the Commission explaining the measures and of initial assessments which had been prepared by the Commission services, in discussion with the Chair, against criteria 1 to 5 of paragraph B of the Code. The Group concluded that the Revenue from Stock Exchange Operations measure was not harmful under the Code criteria. The Group noted that the Interest from Affiliated Companies measure raised important issues of principle. The Group therefore agreed to defer its final assessment of this measure until the first meeting under the UK Presidency. The Group also deferred the final assessment of the Royalty Income measure until the first meeting under the UK Presidency.

26. Extension of benefits beyond the end of 2005 - The Group agreed that outstanding requests for an extension of benefits for certain measures beyond the end of 2005 for the following two measures in Malta:

- **Malta: International Trading Companies (ML4)** – extension of benefits up to 31 December 2015 in respect of those companies which qualified as International Trading Companies on the day immediately before the measure is effectively rolled back;
- **Malta: Dividends from (other) Maltese companies with foreign income (ML5)** – extension of benefits up to 31 December 2015 in respect of those companies which could allocate profits to the Foreign Income Account on the day immediately before the measure is effectively rolled back.

Should be deferred to the first meeting under the UK presidency.