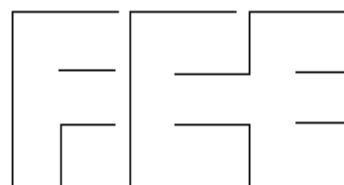


Date
11 June 2003

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Mr. Rolf Diemer
European Commission
DG Taxation and Customs Union
Office MO 59 6/17
Rue de la Loi 200
B-1049 Brussels

Dear Mr. Diemer,

Re: European Commission Consultation Document: "The experimental application of 'Home State Taxation' to Small and Medium Enterprises in the EU"

FEE (Fédération des Experts Comptables Européens, European Federation of Accountants) participated in the EC Workshop on December 17, 2002 and is submitting its comments to the Commission on the related Consultation Document.

Tax obstacles currently hamper Internal Market efficiency and transparency, and prevent Europe to be a competitive single market. Among the comprehensive solutions proposed by the EC 2001 Communication, we support Common Consolidated Base Taxation (CBT) as the most suitable approach. Currently there is already a common trend in many Member States towards broadening the tax base and lowering tax rates.

However, as CBT strategy can be achieved only in the long term, we consider that in the short term Home State Taxation (HST) applied to Small and Medium Enterprises (SMEs) might be more easily accepted across Europe. Member States will be able to acquire considerable practical experience through the pilot project, which will come in useful for the future implementation of Common Consolidated Base Taxation.

FEE therefore welcomes the initiative of the Commission to examine the experimental application of Home State Taxation to SMEs, although it is aware of the difficulties of its practical implementation.

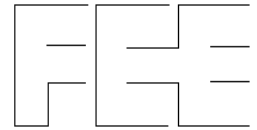
Below we provide you with answers to the specific questions raised in the document.

Responses to the Questions Raised

Question 1)

Would respondents from the business community (and notably the bodies representing SME interests) be prepared to co-operate on the design and testing of a 'pilot scheme'?

FEE believes that the business community has a supportive attitude towards the pilot scheme. We are involved in both Tax and SME areas. We endorse the launching of HST project on SMEs and are willing to help in its design and testing.



Question 2)

Do respondents think that the arrangement under negotiation between Germany and the Netherlands could be usefully extended to other regions?

We consider the arrangements between Germany and the Netherlands as too narrow in scope. A mere bilateral approach would not cover all cross border taxation issues.

Question 3)

Would moving to 'Home State Taxation' for the taxation of small and medium-sized enterprises in the Internal Market deliver real simplification benefits and efficiency gains?

SMEs are discouraged to expand internationally owing to the burden of compliance issues and costs linked to cross border operations, which they cannot overcome as easily as MNCs. The application of HST to SMEs would significantly reduce cross border costs, therefore enabling them to carry out business abroad.

Question 4)

What are respondents' views on the basic approach of the pilot scheme?

We agree with the basic approach of the pilot scheme, according to which European SMEs would be allowed to adopt the parent company tax rules for their subsidiaries and permanent establishments.

Question 5)

Is it considered necessary or suitable that in any event a SME, which fulfils its tax formalities under 'home state rules' with the tax authorities of its 'home country' only, still introduces a pro-forma tax declaration in all countries where it is active?

The compulsory introduction of a *pro forma* tax return in the countries where the SME is active would conflict with the aim of reducing administrative burden. We therefore suggest that an SME should fulfil its tax formalities only with the tax authorities of the 'home country'.

Question 6)

What are respondents' views on the possibility of a purely theoretical / hypothetical pilot scheme?

In our opinion a purely theoretical approach cannot help to advance in this field. We suggest instead a more practical approach.

Question 7)

Is it considered feasible in practice to go beyond the practical testing of the approach in selected sample firms and implement a far-reaching and broad 'pilot scheme'?

We consider a broad implementation of HST to SMEs, as the best possible solution of developing the project.

Question 8)

Would respondents consider that the SME-pilot scheme gives rise to serious discrimination and/or competition problems? If yes, could respondents indicate in which precise area/situation they see such problems?

FEE is of the opinion that the SMEs pilot scheme might give rise to discrimination issues only in the case of implementing the project merely to a selected sample of companies. We think the best solution would be a broad application of the pilot project to SMEs.

Question 9)

What are respondents' views on the potential infringement of the principle of neutrality in taxation (e.g. vis-à-vis the legal form of a business)?

We don't believe there would be any infringement of the neutrality principle. Neutrality is not currently fully in force in the EU, owing to the existing difference between partnership taxation (personal income tax) and corporate taxation (company income tax).

Question 10)

Is it considered desirable or necessary to develop a proper definition of SMEs for the purposes of the pilot scheme?

We don't consider it appropriate to develop a SME definition *ad hoc* for tax purposes, as it would increase complexity and hamper harmonization. A distortion of competition would in fact arise among SME acting in the same market, but located in different Member States

Question 11)

What are respondents' views on the idea to apply the mutual recognition principle to the definition of SMEs (in order to take country-specific conditions into account)?

FEE does not consider suitable to apply the mutual recognition principle, as it would cause Internal Market distortions.

Question 12)

Of the existing SME definitions identified, which would be the most useful for the purpose of the pilot scheme?

We believe that the current definition provided by EC Recommendation would be the most suitable for the purpose of the pilot scheme.

Question 13)

Which 'buffer rules' and transition arrangements would be desirable for dealing with borderline situations?

We consider buffer rules necessary in case businesses fall short of meeting the requirements for participating in the pilot scheme.

Question 14)

Is it considered necessary to define the scope of the pilot scheme by having recourse to additional criteria (other than size)?

We think that the recourse to additional criteria other than size might lead to discrimination issues.

Question 15)

What are respondents' views on the introduction of a time limit for businesses participating in the pilot scheme?

From our point of view, a temporal limitation in the first years of establishing an enterprise abroad would be discriminating against other businesses, which have been active for a longer period.

Question 16)

Are there any sectors, which could be usefully identified for defining the scope of the pilot scheme?

We don't think that there should be any limitation to specific sectors, as it would cause problems of discrimination to particular branches

Question 17)

What are respondents' views on the treatment of activities in third countries or income therefrom? Is it considered suitable to provide for a territorial limitation of the pilot scheme?

FEE believes that the exclusion of SMEs with activities in third countries might be discriminatory, especially under the rules of double-taxation treaties. We don't consider territorial limitations to be suitable for the pilot scheme.

Question 18)

Is it considered necessary and feasible to include partnerships in the scope of the pilot scheme?

According to FEE opinion, partnerships should be included in the scope of the pilot scheme. The main reasons for this are the relevance of partnerships in most of the Member States and HST focus only on the calculation of the tax base and its territorial allocation.

Question 19)

If partnerships would be included in the pilot scheme's scope, should this be done under a "tax treaty approach" or under a "consolidation approach"?

If partnerships were included in the pilot scheme, according to us the most suitable way would be under a consolidation approach, as it appears more consistent with HST features.

Question 20)

Are there significant tax incentives, which are relevant for SMEs, that would impact on the feasibility of the proposed pilot scheme? If yes, which and in which countries?

We believe there are some tax incentives for SMEs which could impact HST. For example, enhanced capital allowances on plant and machinery, IT equipment and research and development.

Question 21)

Is it considered necessary to provide for special rules on the treatment of tax incentives (e.g. by transforming these, within the scope of the pilot scheme, into tax credits)?

We consider it necessary to provide special rules for the treatment of tax incentives. In order to do so, we suggest a preliminary comparison of tax incentives and national accounting rules of all participating European Member States. Transforming tax incentives into tax credits may be a possible solution.

Question 22)

What are respondents' views on the proposed exclusion of VAT from the range of taxes covered by the pilot scheme?

In our opinion, VAT should be excluded from the pilot scheme, as we consider HST a system designed for company taxation only.

Question 23)

What are respondents' views on the proposed inclusion of local profit taxes in the range of taxes covered by the pilot scheme?

We believe that the pilot scheme should include local profit taxes as well, in order not to diminish the advantages of HST.

Question 24)

What are respondents' views on the proposed means for including local profit taxes into the pilot scheme? Are there country-specific aspects to be taken into account and, if so, which?

Local taxes are defined at national level. In order to include local profit taxes into the pilot scheme, we think that the starting point for the calculation of local taxes should be the taxable profit allocated to the MS under the HST. We take for granted that local taxes should continue to be calculated according national rules. Besides, considering the peculiarities of local taxes, we believe that an additional set of national rules is required in order to correctly include local taxes into the HST system.

Question 25)

If a broad scope of the pilot scheme is being decided, is it considered necessary to provide for a revenue or base allocation mechanism? If so, which would be preferable?

In our opinion, if a broad scope of the pilot scheme is decided, it would be necessary to provide a base allocation system with an apportionment formula.

Question 26)

Would there be particular difficulties in collecting the data necessary for applying an apportionment formula based on 'sales' or one based on 'payroll'?

The allocation formula should respect the balance between the need for accuracy and reliability of the allocation on one hand, and the need for simplicity on the other hand.

Such a compromise could probably be reached by taking into account the specifics of different sectors and considering elements such as payroll, sales and assets.

Question 27)

Would there be particular difficulties in collecting the data necessary for applying an apportionment formula based on 'value added'?

We do not believe the value added formula to be appropriate, as it includes the determination of purchase costs. In case of intragroup transactions, such inclusion would lead to transfer price issues, which are one of the main cross border problems that HST is trying to overcome.

Question 28)

What are respondents' views on a direct revenue compensation mechanism between Member States?

Direct revenue compensation would imply that tax revenues are collected by one country only and then redistributed to the other MS. Probably such compensation mechanism is too complex to be implemented in the short term.

Question 29)

What are respondents' views on the proposed intensification of mutual assistance and information exchange between tax administrations as well as the increase of joint audits?

We are in favour of an increase in mutual assistance and information exchange between tax administrations of MS, as well as of joint audits. Co-operation between MS is gradually becoming a general trend across Europe.

Question 30)

Is it considered valuable to launch the pilot scheme even if it was not introduced in all Member States?

FEE believes it is worth launching the pilot scheme, even for a small group of Member States.

Question 31)

Is it considered necessary to provide a coherent EU wide framework for the pilot scheme which would set out the rules for all Member States, regardless of whether or not they implement the scheme in practice?

We are in favour of a EU legal framework to ensure uniformity of implementation of the HST system, and to avoid distortions arising from different regional agreements.

Question 32)

If an EU legal framework for the pilot scheme is being favoured, is it considered necessary to provide a legally binding instrument (which would fall under the control of the European Court of Justice)?

We think it is necessary to provide a EU legal framework in the form of EC Recommendations. A Directive would not be politically accepted in the short term.

Question 33)

Are there any other issues which respondents wish to raise or comment on? If so, which?

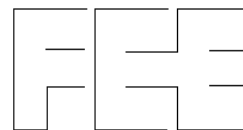
We have several remarks.

Firstly, it should be considered that national tax law is drafted taking civil, commercial and administrative law into account. According to HST, only one tax code would be used for group activities, i.e. the one of the parent company. The adoption of only one tax system could create some problems. More specifically, there may be some contracts or transactions peculiar only to the 'host country' or the 'home country'. This is often the case, among 'common law countries' and 'civil law countries'. Some issues could also arise between countries belonging to the same system (common law/ civil law) but following different approaches in commercial law.

However, it must be pointed out that limiting the implementation of HST only to SMEs reduces such a risk, as SMEs might typically engage in common commercial transactions for which tax rules are roughly aligned in all MS.

Secondly, according to HST, different companies located in the same country are taxed in different ways, depending on the nationality of the parent company. Such a situation is clearly against the principle of 'capital import neutrality' and could hamper Internal Market transparency.

Finally, HST requires very close co-operation among tax administrations and an efficient system to settle disputes arising in the assessment procedure and in the implementation of a decision of Tax Courts.



FEE is confident that the launch of the pilot project would provide practical experience and solutions to the above mentioned issues.

We would be pleased to discuss any aspect of this letter you may wish to raise with us.

Yours sincerely,

David Devlin
President