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A NEW APPROACH TO COMPANY TAXATION

"Company taxation should not place businesses operating in more than one member state at a disadvantage compared with those pursuing purely national activities," commented EC Tax Commissioner Christiane Scrivener as she recently introduced a new package of company taxation legislation for Council consideration. Her chief goal is to abolish all forms of double taxation in the Community by January 1,1993.

The package, which includes three directives, covers the following areas: the tax treatment of mergers, splits, asset contributions and share swaps; the taxation of dividends distributed by subsidiaries to parent companies established in different member states; and an arbitration procedure in the event of disputes on double taxation and transfer pricing between EC countries.

The directive on mergers would remove the capital gains tax that can arise on cross-frontier mergers as long as the acquired company continues to be a tax paying entity in its home member state. In the parent-subsidiary directive, the withholding tax on dividend payments from subsidiaries in one EC country paid to parent companies in another would be abolished.

Although these draft directives have existed for some time, European business believes more than ever that their passage is essential for doing business across the EC. Most important, however, is the change in the Commission's approach. Rather than attempt to harmonize corporate tax rates throughout the EC, the Commission is giving priority to the approximation of national tax laws and to mutual recognition in order to assist companies as the single market further develops. Accordingly, and in light of tax reforms in the 1980s, the Commission has withdrawn its 1975 proposal on harmonizing systems of company taxation and withholding taxes on dividends.

Commissioner Scrivener also announced that another "new" proposal would be forthcoming, allowing businesses or subsidiaries permanently established in an EC country to deduct losses from their foreign establishments for tax purposes. (This provision currently exists as Article 133 of the European Company Statute proposal.)

NEW VAT PLAN AIMS TO SCRAP TAX BORDERS

The EC Commission has released a proposal to eliminate border checks for value added tax (VAT) purposes as of January 1, 1993. Building on the guidelines set by the EC finance ministers last fall (see EURECOM, November 1989), the Commission's plan includes a new system of VAT payment that will be easier for businesses, strengthened cooperation among member state tax authorities and new methods to collect tax statistics.

Under the proposal, which must be passed by the Council of Ministers, VAT would still be charged on goods at the point of consumption (i.e. the "destination principle") rather than at the good's origin, as the Commission would prefer in the long-term. However, instead of routine border checks and the accompanying Single Administrative Document (SAD), the proposed system would rely on periodic VAT declaration forms and invoices provided by companies. Except for trade with non-EC countries, the SAD would be abolished.

After 1992, only some 20% of the Community's largest traders would have to complete a periodic form requiring 10 pieces of statistical information (versus around 50 in the SAD). The vast majority of companies would have only to supply monthly information on their total intra-Community imports and exports.

To guard against fraud, the Commission aims to establish an improved system of cooperation between EC tax authorities, ensuring the rapid and compulsory exchange of VAT information between member states.

On the consumer side, individuals would be able to buy goods in the EC country of their choice after 1992 — paying that member state's VAT rate — without any controls or tax payments at borders. There are, however, two important exemptions: passenger vehicles (cars and motorcycles) and mail-order sales. These would be taxed at the purchaser's home country rate.

EC Tax Commissioner Christiane Scrivener emphasized that the proposed system is an interim solution which would expire after a four-year transition period (until December 31, 1996 at the latest). Before this deadline, the member states would evaluate the functioning of the system and decide on the Commission's goal of changing VAT to a country-of-origin basis.

CAPITAL ADEQUACY RULES FOR INVESTMENT SERVICES

In a significant step toward achieving a single European financial services market, the Commission has proposed a directive on the minimum capital requirements of investment firms wanting to operate throughout the EC. The new Capital Adequacy Directive — a technical complement to the Investment Services Directive — would apply to all firms that carry out financial investments on the behalf of clients, including banks or specialized securities houses, dealers, brokers or investment managers.

Commenting on the proposal, Financial Services Commissioner Sir Leon Brittan said that it is the key that will unlock the Investment Services Directive. "Agreement on these directives will provide the common passport to securities firms to operate throughout the common market and will open up Europe's stock exchanges."

As promised earlier this year by Sir Leon, the Capital Adequacy Directive sets the level of capital an investment firm must maintain according to the risk it runs. The directive calls for a basic capital requirement of at least 500,000 ecu (ecu1=$1.24) for investment institutions. For firms which act as agents or portfolio managers, but which do not hold trading positions of their own, member states could reduce the requirement to 100,000 ecu. For institutions which are not authorized to hold customers' money or securities (nor to act as a market maker), the requirement could be reduced to 50,000 ecu. Investment advisors are not treated as investment firms for the purposes of this directive.

The directive ensures a high level of consumer protection by requiring all investment service businesses to maintain a safety net of "own funds" equal to one quarter of their previous year's overhead.

Banks present a special case. Although banking rules vis-a-vis capital adequacy have already been set in other directives, many EC banks are also engaged in the securities business. To solve this potential conflict, bank supervisors would be able to apply the existing 8% solvency ratio to all the bank's activities, or they could separate their investment trading book from other activities and subject it to the investment services' capital adequacy provisions.

CLEANER DIESELS IN SIGHT

New heavy diesel trucks sold in the EC will have to be 60% cleaner by 1997 under a two-stage plan recently announced by EC Environment Commissioner Carlo Ripa di Meana. According to the Commissioner, diesel trucks emit 10 times more pollution than other forms of transport. If passed, the EC's diesel truck emission standards will be the world's toughest.

The directive, which still needs Council approval, would reduce harmful diesel emissions in two stages (first by 40%, then by 60%) from the maximum permitted levels that were set in 1988. First-stage reductions would enter into force for new models on July 1, 1992, and for all new trucks on December 31, 1992. Second-phase cuts would take effect on October 31, 1996, and a year later for all new trucks.

Following consultations with the industry, the Commission believes that diesel manufacturers have the necessary technology to meet the new standards, and that the two-step approach is appropriate.

Commissioner di Meana also hopes that the proposed standards, along with a forthcoming directive on truck noise, will solve a conflict over truck traffic between the EC and neighbors Switzerland and Austria.

EUROPEAN PORTABLE PHONES

As part of a broader plan to create a single market in telecommunications, the Commission has proposed common frequencies for cordless telephones, which would enable EC citizens to use these phones in any member state.

Further, it urged the Twelve to adopt a European norm for portable phones that was recently developed by the European Telecommunications Norms Institute. This would come into effect in 1993.

Already several leading European telecommunications companies are developing a new generation of portable phones using the new standard.

EC SEEKS POWERS AGAINST AIRLINES' "PREDATION"

Responding to a Council request, the Commission is seeking powers to act faster against airlines engaged in anti-competitive activities. The proposed amendment to the 1987 air transport package would allow the Commission to order airlines to suspend "predatory" fares or other unfair practices, pending a subsequent review by Commission experts. At present, it takes the Commission an average of three months to act in such cases.

This speed of action is essential to protect smaller airlines that are attempting to establish themselves on certain routes (either through lower prices or new schedules) from the larger, established airlines. The amendment would advance the Commission's goal of a liberalized, single market in air transport in which competition is maintained and the consumer benefits.

The Commission has identified four "predatory practices" of airlines that have recently drawn fire: providing excessive capacity or frequency on a given route to keep other airlines out of the market; charging fares considerably lower than the airline's costs; granting "override" commissions to travel agents; and granting excessive loyalty benefits (e.g. frequent flyer points) to passengers.

"POISON PILL" LIMITATIONS PROPOSED

Spearheaded by Internal Market Commissioner Martin Bangemann, the Commission has endorsed a plan to limit "poison pill" takeover defenses, asserting the rights of individual shareholders. It intends to facilitate cross-border takeovers, thereby helping European companies attain the economies of scale necessary to compete globally.

Commissioner Bangemann's three-prong attack plan amends existing and draft EC legislation: the draft 13th Company Law Directive would be amended to limit the power of directors in a target company to buy their own stocks; the 5th Company Law Directive -- which already limits the cases in which large companies can issue non-voting shares — would be strengthened; and the 2nd Company Law Directive would be changed to restrict the ability of a subsidiary to buy shares in its parent as a defensive tactic.

Given the widely divergent national attitudes on hostile takeovers, the proposal will no doubt generate vigorous debate.

QUOTES

*"Economic strength is increasingly determining the real balance of power in the world. Economic integration and the economic strength it provides must have a commensurate political component. In my view, the time is not very far off when the economic identity of the European Community will have to be translated into political terms; this is a prerequisite for a foreign policy on a Community basis." EC Commissioner **Frans Andriessen**.*

*"As the wider Europe of which we are a part begins to stretch and stir, the Community is already a living force within it. Britain today is committed to the further development of the Community as a living force." British Foreign Secretary **Douglas Hurd.***

*"I often have the impression that what we've done over the past 40 years, and especially the last five, because it concentrates on the economic, is rather elitist and distant from our people. One of the ways of involving people is democratization." EC President **Jacques Delors** commenting on the need to "democratize" EC institutions as the EC approaches political union.*

*"The US and Japan have one important advantage which Europe does not yet have: a common currency. Only when we have the benefits of a single currency area will businesses be able to take full advantage of the single market." EC Commissioner **Sir Leon Brittan**.*

*"Companies from our region must rework their European marketing strategies. We have to become one of those concentric circles." New York Governor **Mario Cuomo** commenting on the idea of a greater Europe built in "concentric circles", with the European Community as the core.*

FIRST US-EC MINISTERIAL MEETING IN THE US

Top EC Commission officials and members of the US Administration recently met for the first time in Washington DC as part of the new twice-yearly talks to intensify their political and economic relationship.

Commission President Jacques Delors and US Secretary of State James Baker headed their respective delegations during the talks, which centered on recent political developments in Europe, the Uruguay Round of GATT negotiations and the EC-US relationship.

President Delors, who also met with President Bush, described the meetings as particularly important because they have taken place "at a crossroads in Atlantic history, at a time when several different political processes are experiencing a sharp acceleration, lending new significance to the partnership between the Community and the United States." He pointed to the 1992 single market program and events in Eastern Europe, including German unification and strengthened links with the other Eastern bloc countries, as just some of the political processes affecting the EC-US relationship.

Delors also mentioned that new areas of common interest were discussed, i.e. cooperation in the fields of science and technology, drugs and vocational training.

COMMISSION TO INVESTIGATE INTERNATIONAL PHONE RATES

Responding to allegations that a world-wide cartel of telephone operators massively overcharges consumers on international calls, the Commission has launched its own investigation into the arrangements governing international phone charges to determine whether they are compatible with EC competition rules.

"We have to ensure that consumers benefit from an international telephone charging system which allows genuine competition between the telecommunications operators," said EC Competition Commissioner Sir Leon Brittan.

COMPARATIVE ADVERTISING IN THE CARDS

Building on a recent European Court of Justice decision in favor of cross-border price comparisons (EURECOM, May 1990), EC Consumer Affairs Commissioner Karel Van Miert is planning new legislation allowing companies to use advertising which directly compares their products with rival goods.

"The principle is that comparative publicity should be possible throughout the Community," said Van Miert.

At present, most EC countries forbid advertisements that make direct comparisons between, for example, the performance of two different makes of automobiles or the nutritional content of different food brands.

...IN BRIEF

...A new EC-sponsored Gallup Poll finds US citizens generally positive about the EC and 1992. Most impressive, however, is the upsurge in EC awareness. Forty-seven percent of US adults say they have "heard or read about" the European Community compared with 29% of the population in a

1987 poll. Further, 84% of the respondents said that they were interested in receiving more information about EC developments via the media.

The poll revealed that Americans regard Western Europe's trade policies as basically "fair", and those who are aware of the single market see it as good (50%) rather than bad (18%) for US consumers. A large majority (73%) express either strong (37%) or moderate (36%) support for the Community's efforts to integrate Western Europe.

For copies of the survey, call or write to: Press and Public Affairs, EC Commission Delegation, 2100 M Street, NW, Suite 707, Washington DC, 20037, tel. (202) 862-9554.

...The EC's 1992 program is having an impact on Europe's financial markets. According to the Bank of England's latest quarterly bulletin, business between European-based banks in the first nine months of last year was more than double the activity for the whole of 1988. In the Bank's opinion, this was "almost certainly stimulated by the plans for a single European market by the end of 1992."

...Italy recently removed its remaining exchange controls, well in advance of the July 1, 1990 deadline. Controls on Italians opening bank accounts abroad or holding foreign currency in domestic accounts were eliminated as of May 14. This marks, according to EC Commissioner Henning Christopherson, "an important step in the process of the creation of a European financial area which is increasingly gathering momentum and credibility."

Italy is the last of the eight most prosperous EC member states to lift all restrictions on capital flows. Spain, Greece, Ireland and Portugal have until the end of 1992 to abolish all controls.

...Hefty price increases in Greece, the UK and Portugal drove up EC inflation by 0.5% in March to an annual rate of 5.3%, according to Eurostat. Not surprisingly, Greece had the highest annual inflation rate at 17.8%, followed by Portugal (12.8%) and the UK (8.1%). The Netherlands had the lowest rate at 2.1%, followed closely by the Federal Republic of Germany at 2.7%.

...The American Bar Association Section of Antitrust Law is sponsoring a seminar — "Competition Law and Practice in the European Community" — on June 20-22 in Luxembourg and Brussels. For more information please call (312) 988-5609.

... Spicers Centre for Europe (a subsidiary of Spicer and Oppenheim) has developed a computerized European information service to assist companies in addressing their information needs vis-a-vis the EC and 1992. For more information please call Kathy Edersheim at (212) 422-1000.

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Commission of the European Communities
3 Dag Hammarskjold Plaza, 305 East 47th St., New York, NY 10017
Telephone (212) 371-3804

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