9 November 2012
Taxand

European Commission
Directorate-General for Taxation and Customs Union
Unit D2 – Direct Tax Policy and Cooperation
Rue de Spa 3
B-1049 Brussels
Belgium

Dear Sir / Madam,

Email: TAXUD-D2-Consultation@ec.europa.eu

Re: Taxand Responds to the European Commission's Public Consultation on Problems that Arise in the Direct Tax Field when Venture Capital is Invested Across Borders

Further to the publication of the European Commission's Public Consultation on Problems that Arise in the Direct Tax Field when Venture Capital is Invested Across Borders, Taxand is pleased to provide feedback.

Taxand welcomes this initiative. Our summary comments and observations are as follows:

II. Problems Encountered in Practice

1. General

Have you experienced direct tax obstacles in connection with your cross-border venture capital investment? If so, please provide details of:
a) The tax obstacles and the reasons why they occurred

Permanent establishment

b) The countries involved

Finland, Luxembourg.

c) The result for these obstacles (e.g. double taxation, tax treatment uncertainties, administrative obstacles, additional costs, etc.).

Investors refrain from investing in the VC structure.

2. Permanent establishment issues

If a permanent establishment has been deemed to exist in the country of the target company, please provide details about:

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a) The reasons for the deemed existence of the permanent establishment

The reasons for a deemed permanent establishment vary across Europe. For example, based on Finnish legislation, an investor of a tax-resident feeder fund making an investment in Finnish LP would be deemed to have a permanent establishment in Finland.

However, as far as Luxembourg is concerned, so far, based on the so-called "Geprägetheorie", where the GP of a Luxembourg partnership was a Luxembourg joint-stock company (which is per se commercial by reason of its legal form), the whole activity of the Luxembourg partnership was deemed to be commercial. The quality and status of the GP commercially tainted all the activities and revenues of the partnership, resulting in the LP becoming subject to Luxembourg Municipal Business Tax, and the partners to Corporate Income Tax and Net Wealth Tax in Luxembourg due to the presence of a Luxembourg PE.

Luxembourg has recently taken some measures in order to face this issue and has relaxed the conditions for the application of the Geprägetheorie. A draft law now provides that the income realised by partnerships will be considered as commercial income only to the extent the General Partner is a joint-stock company, which holds at least a 5% interest in the Luxembourg partnership. In the future, as long as the GP holds less than 5% interest in the partnership - which is generally the case in hedge funds or PE/PERE structures - the Geprägetheorie will not apply, so no taxation will arise in Luxembourg.

Some years ago, Luxembourg also implemented a vehicle dedicated to the venture capital sector (the SICAR) for which the law specifies that SICARs set up in the form of a partnership will never be considered as performing a commercial activity. There is therefore no risk of a Luxembourg PE when SICARs are set up in Luxembourg to invest in the venture capital sector.

b) Whether the permanent establishment is in respect of the income of the venture capital fund manager himself or of the venture capital fund or of the investors

The investors in a fund of fund.

c) Which Member State has deemed the permanent establishment to exist

Finland, Luxembourg.

d) What percentage/part of total profits have been attributed to that permanent establishment

N/A (theoretical question, as these kinds of structures are avoided due to the evident risk).

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e) What method was used for the profit attribution

See answer above

f) Whether the profits attributed to the permanent establishment have suffered unrelieved double taxation as a result and if so, why double taxation was not relieved

See answer above

g) The amount of the unrelieved double taxation

See answer above

3. Entitlement under double taxation conventions

Have you suffered unrelieved double taxation due to the fact that the tax classification and tax treatment of venture capital funds varies from one country to another? If so, please specify:

A very extensive tax harmonisation would be required to solve at global level the issue of mismatch of tax classification of venture capital funds. Given the existing alternatives that are used already since decades by the venture capital sector in order to face these issues, we do not consider that it is necessary to harmonise at global level.

The Luxembourg tax authorities will generally adopt a pragmatic approach and will thus, as far as possible, try to follow the tax classification given in the foreign country.

a) The exact reasons for the double taxation

N/A

b) The countries involved

N/A

c) The amount of unrelieved double taxation

N/A

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d) Whether the OECD Partnership Report1 and the Commentary to the OECD Model2 have provided guidance/assistance in resolving the issue (the Partnership Report and the Commentary to the OECD Model suggest generally that the classification of a partnership as transparent or non-transparent applied by an investor's country of residence should be the decisive one as far as the taxation and double taxation relief of the investor are concerned).

N/A

e) How often the mutual agreement procedure provided for in double tax conventions based on the OECD Model has been applied in practice and whether it was efficient

N/A

4. Avoiding the risk of double taxation

If there was a risk of double taxation of your investment returns, which you managed to avoid in practice, please specify:
a) How you managed to avoid the risk and the extra costs and complexities involved

N/A

b) The EU and non-EU countries involved

N/A

5. Risks of double non-taxation/ tax avoidance and evasion

Are you aware of any cases in which mismatches between Member States' domestic tax rules might lead to double non-taxation or tax planning?
If so please provide:
a) Details, including the jurisdictions involved

The possible mismatches of planned Finnish regulation, for example, limiting intra-group interest payments shall be ascertained when the final form of the regulation will be presented.

b) An estimation of the amounts of lost tax revenue

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[1] http://www.oecd-ilibrary.org/docserver/download/fulltext/2399521e.pdf?expires=1340028069&id=id&accname=ocid194935&checksum=934A17F5F9BED80F33551A78F2B1551D

[2] http://www.oecd.org/document/37/0,3746,en_2649_33747_1913957_1_1_1_1,00.html

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N/A

6. Tax burden and additional costs for venture capital investors investing across borders

a) Are your proceeds from cross-border venture capital investment taxed in the country of the target company?

As far as Luxembourg is concerned, for example, where Luxembourg is the source country, taxation may arise at source but since this taxation occurs only in case the investment is sold within a limited time frame (6 months), it is relatively easy to make sure that the capital gain is not taxable. In addition, as far as venture capital funds like SICARs are concerned, the Luxembourg law excludes the taxation at source, even in case of speculative (short term) gains.

b) Are your proceeds from cross-border venture capital investment taxed in the country where the fund is established?
If so, please indicate how they are taxed; please specify the type of proceeds (e.g. capital gains, dividends) and the tax rate applied, whilst mentioning any special tax incentives/ tax regimes applicable

If not, please specify why not – e.g. because the fund is a tax exempt entity or transparent for tax purposes, etc.

N/A

c) Are your proceeds from cross-border venture capital investment taxed in your state of residence?
If so, please indicate how they are taxed; please specify the type of proceeds (e.g. capital gains, dividends) and the tax rate applied, whilst mentioning any special tax incentives/ tax regimes applicable

If not, please specify why not – e.g. because your state of residence does not tax capital gains, dividends; because you are a tax exempt entity, etc.

N/A

d) What is the effective tax burden on your cross-border venture capital investment?

N/A

e) Have you suffered any additional costs due to your cross-border investment in venture capital?
If so, what are the annual additional costs related to your cross-border venture capital investment? Please specify per category, e.g. for advisory fees, unrelieved double taxation, foregone tax relief, administrative costs, etc.

N/A

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7. Possible discrimination of cross-border venture capital investment compared to domestic venture capital investment

a) Does the country where the target company is established tax proceeds from venture capital investment differently depending on whether the investors are resident or non-resident? For example, are there specific VC benefits, such as exemption, deferral/investment reserves, lower tax rates, relief from economic double taxation, etc available only to domestic fund and investors? Or is capital gains tax applicable only on (some or all) sales of shares of non-resident investors? Please provide details about any differences in treatment and the countries in which these occur.

N/A

b) Does the country where the fund is established tax receipts of the venture capital fund differently depending on whether these arise from domestic or foreign sources? Does the country where the fund is established tax differently dividends paid to non-resident investors compared to dividends paid to resident investors? Please provide details about any such differences in treatment and the countries in which these occur.

N/A

c) Does your country of residence tax the income and gains you receive from a non-resident venture capital fund or non-resident target company differently to income and gains you receive from a domestic VC fund or target company? Please provide details about any such differences in treatment and the countries in which these occur.

N/A

III. Possible solutions to the tax obstacles encountered when venture capital is invested across borders

a) What are your proposals for possible solutions to the tax obstacles you encounter?

N/A

b) Why do you prefer this solution/ these solutions? Please outline the advantages and disadvantages of your suggestion.

N/A

c) How should your suggested solution(s) be implemented e.g. by EU legislation or by changes in different national laws?

N/A

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d) How would your suggested solution(s) impact on the investors' return of investment and governments' tax revenues?

N/A

e) How would your suggested solution(s) impact on Member States' tax legislation, their double taxation conventions and existing EU law, e.g. on direct taxation, State Aid, etc.?

N/A

f) What would the advantages be for Member States in adopting the proposed solution? Would there be winning and losing Member States and if so how could the losing Member States be persuaded to agree to the solution?

N/A

g) If you are a fund or fund manager and are currently established outside the EU, would your suggested solution make it more attractive for you to move into the EU?

N/A

h) Can you recommend any best practices in any EU Member States or third countries in the area of taxation of venture capital?

N/A

i) Are you aware of any statistics or legal or economic studies which could further contribute to the analysis of the costs and benefits of implementing the solution(s) you suggest?

N/A

Do you have any other comment or thoughts to share as regards cross-border taxation of venture capital?

Ideally, VC-structures within EU-countries should be mutually recognized and accepted. Tax consequences should be predictable and symmetrical. However, as mentioned above, given the extensive harmonisation which would be required and the alternatives that exist in practice to face the related tax issues, we do not consider that this harmonisation as really necessary.

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We appreciate this opportunity to provide our feedback to the European Commission and would be pleased to discuss this further and/or to participate in any additional discussions on these matters.

More information on how to contact us, our stakeholder identification and about Taxand is provided in Appendix I. Taxand is wholly committed to supporting the European Commission's work and we look forward to contributing to further debate.

Yours faithfully,
Taxand

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APPENDIX I

CONTACT DETAILS

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ABOUT TAXAND

Taxand provides high quality, integrated tax advice worldwide. Our tax professionals, nearly 400 tax partners and over 2,000 tax advisors in nearly 50 countries - grasp both the fine points of tax and the broader strategic implications, helping you mitigate risk, manage your tax burden and drive the performance of your business.

We're passionate about tax. We collaborate and share knowledge, capitalising on our collective expertise to provide you with high quality, tailored advice that helps relieve the pressures associated with making complex tax decisions.

We're also independent—ensuring that you adhere both to best practice and to tax law and that we remain free from time-consuming audit-based conflict checks. This enables us to deliver practical advice, responsively.

Taxand has achieved worldwide market recognition. In the International Tax Review's (ITR) World Tax 2012, over 95% of Taxand locations are ranked top. 35 countries were voted top in the ITR Transaction Tax Survey 2012 and in the ITR Tax Planning Survey 2012. Taxand has received 49 national awards and 10 regional awards in the ITR European, Americas and Asia Tax Awards since 2009. These include European Private Equity Tax Firm of the Year, European Indirect Tax Firm of the Year, European Tax Policy Firm of the Year, Asia Transfer Pricing Firm of the Year, Asia Tax Policy Firm of the Year and Latin America Tax Disputes Firm of the Year. Full details of awards can be viewed at www.taxand.com/media/factsheet. www.taxand.com

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