International Chamber of Commerce
The world business organization

Policy Statement

Prepared by the ICC Commission on

Taxation

Tax treatment of international takeovers/mergers

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ICC policy statement
on tax treatment of international takeovers/mergers

Introduction

As the world business organization, and a representative body that speaks on behalf of enterprises from all sectors in every part of the world, the International Chamber of Commerce ("ICC") has noted with concern a recent trend in some jurisdictions towards the taxation of international takeovers and mergers.

In particular, a number of jurisdictions have asserted that they may impose capital gains taxes and withholding tax obligations in circumstances in which some portion of the transactional value derives from underlying assets in its jurisdiction even though the transaction has taken place entirely outside that jurisdiction. For example if a company in Country A takes over a company in Country B, which directly or indirectly owns a subsidiary in Country C, or indeed in Country D, E or F, Country C, D E or F may seek to impose such taxes.

Separately, ICC notes that such recent changes are introduced by means of retrospective changes in law or policies. Such retroactivity undermines the stability of the tax regime of a country.

ICC is concerned that this approach extends the scope of taxation outside commonly applied international taxation principles, and can create a significant barrier to international trade and investment.

ICC recommends that governments:

- ***Review their tax policies to ensure that the tax treatment of global acquisitions is consistent with generally applied principles of territorial taxation;***
- ***Avoid retrospective changes in tax laws or policy; and***
- ***Develop tax regimes that are supportive of other policies to promote business investment, noting that this will result in increased employment and tax revenues in the long term***.

Background

Over the past few years, a number of states have put forward the view that they are entitled to capital gains tax on mergers and acquisitions taking place outside their jurisdictions, involving transfers of shares in overseas companies that have no personal or proprietary link with that state. Further, in some cases, it may be suggested that the buyer is subject to obligations for deducting withholding tax from the seller's proceeds, even if the buyer and seller have no connection with that particular jurisdiction.

As a logical consequence of this position, the sale and acquisition of a global corporation with significant international operations could be subject to capital gains taxes and withholding tax obligations in numerous jurisdictions beyond those with which the parties to the transaction and the assets or shares directly transferred had any material direct connection. Such a situation would create a significant barrier to international trade, merger and acquisition activity and foreign direct investment flows— thereby undermining the efforts of many governments to attract businesses by expanding investment opportunities.

International taxation and extra-territoriality

Whilst ICC fully recognises that countries may need provisions in their tax law to prevent conduct involving artificial arrangements—designed to circumvent a country's tax laws—ICC is concerned that this treatment of international takeovers and mergers, imposing taxation based on the location of underlying assets, is not in conformity with generally accepted international tax practices. The tax treaty network has been established on the basis of these international tax practices.

In this connection, it is a widely accepted general principle of international tax law that a state may exercise its fiscal jurisdiction with respect to persons who have a personal link with that state, or to assets with which it has a real or proprietary link. The basis of tax jurisdiction linked to residence or "local source" also underlies numerous tax treaties, the vast majority of which are concluded on the basis of models published by the Organisation for Economic Co-operation and Development or the United Nations. These models proceed on the assumption that states will exercise their jurisdiction in accordance with the general principles of international tax law and will either tax persons who are residents of that state, or income having its source in that state.

Applying these concepts to capital gains on the sale of corporate shares, such a capital gain may be taxed either in the state of residence of the person disposing of the asset on which the gain arose, or in the state where the asset is situated. The only exception to this principle that is often accepted in tax treaties is where there is a disposal of shares in a company and the value of those shares is substantially derived from the ownership, directly or indirectly, of immovable property situated in a state. In those circumstances the state where the immovable property is situated may choose to preserve its jurisdiction to tax the gain, even though that gain is realised by a person who is not resident in that state on the disposal of shares not situated in that state.

The approach to the taxation of mergers and takeovers outlined above—that capital gains taxes and withholding tax obligations may be imposed by a state on transactions which have no direct link with that state—creates considerable uncertainty and indeed real costs to international businesses, many of which are ultimately born by consumers (through higher prices), workers (through reduced employment opportunities and lower wages), and governments (through decreased tax revenues in the long-run).

Retrospective amendments to tax law and regulations

ICC is particularly concerned to note the use of retrospective changes in law. Moreover, we also note a development regarding the reinterpretation of long established existing laws and tax treaty provisions to justify these changes to the tax treatment of international transactions. The legal and commercial aspects of such exercise of extra-territorial jurisdiction create additional uncertainty.

From a business perspective, such an approach is liable to expose many previous buyers and sellers of shares in global corporations to significant tax liabilities, and create further uncertainty for such transactions going forward. This position greatly amplifies the likely adverse impact of these measures on international trade and investment.

The use of retrospective amendments to tax laws and regulations by jurisdictions is a deterrent for businesses which consider future investments in those jurisdictions.

Recommendations to policy-makers

In light of the potential impact on international trade and investment, ICC stresses the need for governments to undertake a review of their approach to the taxation of international takeovers and mergers.

As a guiding principle, this should seek to ensure that domestic policies and administrative practices are aligned with reasonable and generally accepted international tax principles as described above. This is particularly true in an ever accelerating globalised world where differences in tax regimes create barriers to the efficient conduct of a business operation. The use of retrospective changes in law creates great uncertainty and concern for investors and should be avoided.

The International Chamber of Commerce (ICC)

ICC is the world business organization, a representative body that speaks with authority on behalf of enterprises from all sectors in every part of the world.

The fundamental mission of ICC is to promote trade and investment across frontiers and help business corporations meet the challenges and opportunities of globalization. Its conviction that trade is a powerful force for peace and prosperity dates from the organization's origins early in the last century. The small group of far-sighted business leaders who founded ICC called themselves "the merchants of peace".

ICC has three main activities: rules-setting, dispute resolution and policy. Because its member companies and associations are themselves engaged in international business, ICC has unrivalled authority in making rules that govern the conduct of business across borders. Although these rules are voluntary, they are observed in countless thousands of transactions every day and have become part of the fabric of international trade.

ICC also provides essential services, foremost among them the ICC International Court of Arbitration, the world's leading arbitral institution. Another service is the World Chambers Federation, ICC's worldwide network of chambers of commerce, fostering interaction and exchange of chamber best practice.

Business leaders and experts drawn from the ICC membership establish the business stance on broad issues of trade and investment policy as well as on vital technical and sectoral subjects. These include financial services, information technologies, telecommunications, marketing ethics, the environment, transportation, competition law and intellectual property, among others.

ICC enjoys a close working relationship with the United Nations and other intergovernmental organizations, including the World Trade Organization and the G8.

ICC was founded in 1919. Today it groups hundreds of thousands of member companies and associations from over 130 countries. National committees work with their members to address the concerns of business in their countries and convey to their governments the business views formulated by ICC.

ICC

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Policy and Business Practices

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