UNIVERSITEIT GENT

FACULTEIT ECONOMIE
EN BEDRIJFSKUNDE

TWEEKERKENSTRAAT 2
B-9000 GENT
Tel. : 32 - (0)9 – 264.34.61
Fax. : 32 - (0)9 – 264.35.92

WORKING PAPER

An Empirical Investigation into the Design of an EU Apportionment Formula Related to Profit Generating Factors

Annelies Roggeman[*]

Isabelle Verleyen*

Philippe Van Cauwenberge[†]

Carine Coppens[*]

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[*] Faculty of Business and Information Management, University College Ghent, Henleykaai 84, B-9000 Ghent, Belgium
[†] Department of Accountancy and Corporate Finance, Ghent University, Kuiperskaai 55[E], B-9000 Ghent,Belgium

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Abstract

The European Commission (EC) has the intention to establish a Common Consolidated Corporate Tax Base, which requires an allocation formula to fairly distribute the consolidated tax base among all group entities. A fair distribution would mean that the allocation is closely related to the profit generating factors of the underlying entities. The EC supposes that fixed tangible assets, sales and labour are the dominant factors in the generation of profit. This paper analyses the profit generating capacity of these factors and of the alternative factor intangible assets. The results show that the proposed factors only explain 28% of the variation in profit. Moreover, the results indicate that recognized intangibles do not increase R^2 significantly. However, for R&D intensive companies, adding the market less book value to proxy for unrecognized intangibles, increases the explanatory power with 30%. This suggests that for these companies unrecognized intangibles could be important in generating profit.

Keywords: CCCTB, apportionment formula, fairness, international corporate taxation, European Union

JEL classification: D63, F23, H25, H87