Answer-to-Question-5

The subject of inclusion of the PE losses originates both from (a) tax law (including Double Tax Treaties - if signed by Member States X and Z) and (b) ECJ case law.

In principle a permanent establishment in Member State X should be treated as a separate taxpayer and its losses should be allowed for carrying forward in the future years in that country.

It is reasonable to assume that the tax laws in State Z deal with profits and losses of the PE by resolving double taxation either by providing an exemption or a credit under its local laws and the DT convention (assuming it is signed between States X and Z).

The answer to whether State Z can refuse depends on the presence or absence of the following factors (commonly used in the EU case law).

Sometimes they could be used as a substantiation for the restriction of freedoms and discrimination namely including prohibition of taking the losses of the PE:

- double use of tax losses;
- anti-avoidance (wholly artificial arrangements);
- coherence of the tax system;
- balanced allocation of taxing rights.

Often a combination and not a single reason could have been used.

This question also touches the following freedom: freedom of establishment as stipulated by Article 49 of the TFEU whereby nationals of a Member State are free to set up branches and agencies in another member state.

Double use of Losses

The taxpayers can not use these losses for reducing profits twice: in the HQ state and at the PE state. There is a case law on this matter (ref: Marks & Spencer, Rewe, Timac Agro). In these cases, the ECJ

concluded that the double use of tax losses can be used as a substantiation for restriction.

Coherence of the tax system

This reason has also been used in the EU case law to restrict freedoms (such as use of losses). This reason refers to a direct connection between a tax deductibility and the taxation of an item. In the EU case law there cases when it was concluded that he head office and the PE are the same taxpayer and therefore, it was possible to refer to the coherence of the tax system.

Balanced Allocation of Taxing Rights.

There is a case law accouding to which the grant of a right to company to choose the jurisdiction in which it can use its tax losses undermines its balanced allocation of taxing rights (please refer to cases Marks and Spencer, Oy AA).

Conclusion

Depending on the above facts and whether it could be established that State Z could invoke any of the above justification to restrict the Company Z's right to use losses in State Z, the local tax authorities could refuse to take the PE's losses into account.

Answer-to-Question-4

It is impossible to stipulate all possible loopholes that taxpayers could explore to perform tax avoidance and BEPS.

For this purpose, the general anti-avoidance rule ("GAAR") was introduced in Article 6 of the ATAD. It stipulates a mandatory main benefit test. The GAAR applies to transactions (or arrangements) which have been put in place for the main purpose is to obtain the tax

advantage that defeats the purpose of applicable tax law based on all facts and circumstances. This GAAR principle is applied in parallel to a) other anti-avoidance measures as introduced by ATAD and ATAD 2 such as:
- interest limitation
- CFC
- exit taxation
- hybrid mismatch

and b) other measures stipulated in other directives (e.g. in the Parent-Subsidiary directive (article 1 (2-4)) and Interest-Royalth directive).

The difference with some the above measures is that the GAAR is less specific. For instance, an interest-limitation rule results in an X amount of intragroup debt being non-deductible based on the predefined formula. At the same time, the GAAR is much broader and in case this measure is invoked, it could have broader consequences for the taxpayer as the ATAD does specify concrete formula or mechanism how to adjust profits - it would be done on a case-by-case basis based on facts and circumstances and in line with the national laws.

Then the tax liability is recalculated based on the local national law.

The application of GAAR, however, can not result in any restriction of the basic freedoms established by the TFEU:
- of movement
- of employment
- of establishment
- of capital movement.

Even before the introduction of the GAAR the concept of wholly artificial arrangements was already used in the case.

There is a concept of "wholly articifical arrangements" that was used by the ECJ where the GAAR typically should be applied before the introduction of ATAD. This "wholly artificial arrangement" concept was applied namely in the following cases:
- Cadbury Schweppes
- Eqiom and Enka
- Danish "beneficiary ownerhship" cases.

Typically "wholly artificial arrangements" are the ones that deny the economic reality and have the purpose to obtain a tax advantage.

In general it is contrary to the EU law to use it for abusive actions and the EU law can not be used for it. The above-mentioned Eqiom and Enka case was ruled before GAAR/ATAD, however, any benefits (such as WHT exemption) could be denied based on the GAAR or other Directives, e.g. the anti-abuse clause in the Parent-Subsidiary Directive.

Answer-to-Question-8

The Arbitration Convention ("AC") and the EU Tax Dispute Resolution Directive ("DRD") represent different routes to resolution of double taxation as a result of tax adjustment by one of the member states.

The scope of the DRD is to resolve tax disputes between Member States on various treaty interpretation issues (not only transfer pricing) whereas the scope of the AC is to resolve double taxation resulting from the transfer pricing adjustments (although TP adjustments could also be covered by articles 7 and 9 of the model tax treaty where the DRD could be invoked).

Overall, the DRD represents an alternative route for resolving double taxation. It uses more or less commensurate (with AC) period to resolve the double taxation.

Legal nature

the AC was concluded based on the EC Treaty. It was concluded as a multilateral treaty and not as a directive that forms part of the EU primary or secondary law. It means each member state needs to ratify it in order to get access to it. Therefore, it does not automatically binds new member states.

Scope

As mentioned in the OECD Transfer Pricing Guidelines, transfer pricing is not "an exact science" and transfer pricing disputes created problems both for taxpayers and tax administrations.
Elimination of double taxation as a result of transfer pricing adjustments between EU member states that ratified it is the main requirement of the AC. In general it follows the notion of an "arm's length principle" and starts to be applied by a taxpayer or by a local tax administration. The AC only covers direct taxes.

Such a double taxation could take place, inter alia, in the case of:

- TP adjustment between 2 legal entities located in different member states; OR
- between the head office and a permanent establishment in 2 different member states.

For years (if not decades) it represented a mandatory mechanism to resolve double taxation as a result of transfer pricing adjustments (it was binding on the parties that ratified it).

It represented additonal - to tax treaties - mechanism for the prevention of double taxation.
It was concluded prior to the BEPS project and imposition of minimal standard to the double tax treaties and therefore it could be argued that its role has somewhat recently diminished.

Mechanics

The sequence of steps is the following:

1) The application starts with a TP adjustment: Each taxpayer who does not agree with a transfer pricing adjustment has 3 years to bring the matter to its competent authority. The competent authories should notify the authorities of other states;
2) In case the competent authority finds the case well grounded it would try to resolve the issue directly with the taxpayer concerned and resolve it. If not, it would have to involve tax authorities of another state concerned and initiate a mutual agreement;
3) Then the tax authorities have 2 years to initiate the mutual agreement procedure or to deny the access to it. This is complex process involving exchange of view of tax authorities on the merits of the case

and their views and the proposal to resolve it.
4) Then it goes to the arbitration procedure and member states concerned have to resolve double taxation.
Member states concerned based on their decision should find the way to resolve the double taxation. It should be done with 6 months.

Answer-to-Question-2

1) The following basic freedoms may apply in the given case:

- freedom of establishment (article 49 of the TFEU);
- freedom of capital movement (article 63).

Normally freedom of establishment does not apply to transactions between the EU member states and non-EU states. Freedom of capital is the exception and it would apply in this case.

The ECJ would assess whether a discrimination took place and whether the basic freedom of capital movement has been restricted using such tools as comparability and analyzing whether a restriction took place.
It order to assess a purely domestic and a cross-border situation should meet the criteria of comparability.

2)

Discrimination based on the nationality is covered by Article 18 of the TFEU and the restrictions (as for capital movement as in the case at hand) are covered by Article 63 of the TFEU.

Overall, I do not find the argument that Company T is discriminated or there is a restriction. There is no restriction on basic freedom such as movement of capital and neither discrimination as it is treated in State S is not worse than resident taxpayers (even based on the DTA a 10% WHT rate is applied).

Theoretically it should be clarified whether local shareholders of subsidiaries in State S would be allowed a refund in such a case. However, there are two issues with that:

- a comparability analysis should be performed between the local shareholder and the one in the Third Country (there is a case law from the ECJ that in principle residents of member states and non-member states are in comparable situation let alone other comparability criteria);
- regardless of that Third State formed its basis for taxation in the DTA with State S and therefore effectively relinquished its entitlement to reimbursement of tax refund (assuming that the DTA follows the model tax treaty, which it should as otherwise the Euro Commission could have requested the alignment).

3) Theoretically State S could apply the following justifications to deny the WHT reimbursement:

- Coherence of the tax system

Such a justification creates a match (symmetry) that links tax deduction and taxation of a certain item. Typically Third State would not be taxing income of its subsidiary in State S and therefore it is not entitled to a deduction (refund).

There is also a double tax treaty that creates the coherence (as both states agreed to use the treaty as the basis).

There is a case law in the EU according to which the link (mentioned above) can only exist if relates to the same taxpayer (or a family). The case law relevant: Baars Case, Bosal Holding. However, Company T and its subsidiary are two separate taxpayers.

- Tax avoidance

Typically this justification is applied in case of "wholly artificial arrangements". Nothing in the fact pattern indicates such an arrangement though.

- Safe-guarding allocation of taxing rights between member states

State S would argue that the WHT is local tax applied by its state and it has the right to collect it (as ratified by the DTA between 2 states). Therefore, Company T should have no right to claim this tax from it as therefore could be a valid argument for the restriction. There is a case law (X Holding, Oy, Marks and Spencer) that supports this claim and this justification may be accepted as State S effectively losing its taxing rights.

- Compensation of unfavorable tax treatment with another benefit

State S could argue that based on the DTA it provides a lower WHT rate and this balances out an unfavourable decision on the WHT reimbursement denial.

4) In principle the prohibition on discrimination based on nationality (article 18 of the TFEU) does not cover domestic situations compared to cross-border ones. Therefore, local nationals could be treated worse than nationals of other state. This is labelled as a "reverse discrimination".

Therefore, the double tax treaty should not have an impact here. Theoretically a "state aid" argument could be invoked or the local laws of each state that prohibit such a treatment of local nationals but it would be likely fall outside of the scope of tax legislation. Plus, European Commission is tasked with checking that all double tax treaties do not contain provisions that could be viewed as a state aid.

Answer-to-Question-1

1) In principle State A could request the banking information on the following bases:

- The double tax treaty (between State A and B). Based on the model tax convention states are allowed to make such a request if it is well substantiated. In the case at hand it is mentioned that State A suspects Taxpayer Z of hiding income received in State B. Therefore, such a request is substantiated. Moreover, this request was addressed by State A not to the Bank BB directly but to State B. Therefore, the formal procedure was respected.

- Directive on Administrative Cooperation ("DAC") signed by EU member states in 2011. This directive provides minimum standard. It went through a number of updates. Specifically DAC2 (2014 update) refers to the common CRS common reporting standard whereby the financial information - including bank account detailes - is exchanged automatically.

Bank BB could argue that this request is excessive based on the mandatory automatic exchange of information and that State A should have already received this information.

2) In principle the DAC obliges to inform the addressee in the request. The addressee is Bank BB and not Taxpayer Z per se. Therefore, the claim is not valid.

3)

According to Article 8(1) of the Charter of Fundamental Rights of the EU ("CFR"), everyone has the right to his private and family life. However, article 8(2) also acknowledges that there are exceptions that the interference by the public authority is made in accordance with the law and is necessary in the interest of national securitym public safety or the economic well-being of the country, for the prevention of disorder and crime.

To the extent that the authorities could not demonstrated that the above-mentioned exception is legitimately invoked the claim of Taxpayer Z could be considered substantiated.