

THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

December 2025

MODULE 3.01 – EU DIRECT TAX OPTION

SUGGESTED SOLUTIONS

PART A

Question 1

Part 1

Member State A can request this information from Member State on grounds of the so called 'DAC 1' directive (Directive 2011/16/EU) and specifically under the Exchange of Information on request provisions (Articles 5-7). Students may also mention that information may be exchanged also on grounds of the DTC (if one exists) between the two states, but what is of relevance here is DAC 1. The information requested must be foreseeably relevant for the purpose they aim to serve. The bank may not refuse to provide certain information if it deems that the information is not foreseeably relevant, this is a task for the tax authorities of the requested state, to ensure that the requesting state is not engaging in a fishing expedition and is not asking for any information "devoid" of any foreseeable relevance (extra points if the students mention that the standard of foreseeable relevance applied by the Court is similar to the one in the commentary of Article 26 OECD MC). None of the Article 17 limitations of the DAC 1 seems to apply here: The provision of information may be refused where it would lead to the disclosure of a commercial, industrial or professional secret or of a commercial process, or of information whose disclosure would be contrary to public policy. However, as per the Berlioz judgment and later on the Luxembourg vs. B and others, the information holder (bank) may appeal the information order before the competent domestic courts (as part of its right to an effective remedy, Article 47 of the Charter).

Part 2

The question asks the rights of the taxpayer in the exchange of information between Member States stage. DAC 1 does not give any rights to the taxpayers in this process and this was confirmed in the Sabou (C-276/12) and Luxembourg vs. B and others case (C-245/19 and C-246/19). In Sabou, the Court held that EU law does not give the taxpayer a right to be informed that their tax authority has sent an information request to another Member State, a right to participate in formulating that request, or a right to take part (or be heard) in investigative steps in the requested state (e.g., witness examinations). This approach was later confirmed in the Luxembourg vs. B and Others case where the Court confirmed that the taxpayer does not have any rights in this procedure – they cannot even appeal the information order, but they must wait for any adjustment decision by the tax authorities, which they can appeal.

Part 3

The students should first confirm that the Charter of Fundamental rights is applicable in this case. Indeed, if we assume that the relevant domestic law is implementing DAC 1 then the Charter comes into play, as per Article 51(1) of the Charter. On the basis of this, the taxpayer is indeed entitled to the right to privacy [Article 7 Charter] and the right to the protection of personal data [Article 8(1)] which is closely linked, as far as natural persons are concerned, to their right to respect for private life. The communication of information relating to an identified or identifiable natural person to a third party, including a public authority, and the measure which requires or permits that communication, are, without prejudice to any justification for them, constituting an interference with that person's right to respect for his private life and his right to the protection of personal data concerning him, regardless of whether or not the information is of a sensitive nature and irrespective of its subsequent use, unless the communication is made in compliance with the provisions of Union law and, where applicable, the provisions of national law. While there is indeed an interference, the students should be able to identify that according to Article 52(1) Charter, those rights may be limited if the limitation is provided for by law, respects the essence of the rights, and, subject to proportionality, be necessary and genuinely meet objectives of general interest recognized by the EU (or protect the rights/freedoms of others).

Question 2

Part 1

In order to identify which freedom(s) may apply, the nature of the situation has to be assessed. In this case, the issue at stake is a dividend payment from a company which is a resident of an EU Member State (S) and is paid to its parent, which is a company resident in a third country. The dividend payment is subject to withholding tax in the source state.

The payment of dividends constitutes capital movements covered by the free movement of capital but can also be covered by the freedom of establishment. In accordance with settled case-law, national provisions which apply to holdings by nationals of the Member State concerned in the capital of another company giving them definite influence on the company's decisions and allowing them to determine its activities come within the substantive scope of the provisions of the Treaty on freedom of establishment (Case C-251/98 Baars, para. 22, Case C-436/00 X and Y, para. 37, and Case C-196/04, Cadbury Schweppes, para. 31). In the latter case, the only freedom applicable would be the freedom of establishment.

In this case there is no information about a substantial shareholding that would give rise to such control from the shareholder; therefore, this is a portfolio/financial investment situation, and the case should be analysed only under the light of Article 63 TFEU and the free movement of capital.

The answer to this question therefore is that the applicable freedom is only the free movement of capital (Art 63 TFEU). If Company T had a controlling holding in its subsidiary, giving it definite influence on the subsidiary's decisions, the case would fall under the freedom of establishment, and it would be analysed under that freedom only.

Part 2

According to the case-law of the Court, the measures prohibited by Article 63(1) TFEU, as restrictions on the movement of capital, include those which are such as to discourage non-residents from making investments in a Member State or to discourage that Member State's residents from doing so in other States (see Sofina and Others, C 575/17, paragraph 23 and the case-law cited).

Specifically, the less favourable treatment by a Member State of dividends paid to non-resident companies, compared to the treatment of dividends paid to resident companies, is liable to deter companies established in a Member State other than that first Member State from undertaking investments in that same first Member State and, consequently, amounts to a restriction of the free movement of capital, prohibited, in principle, under Article 63 TFEU (Sofina and Others, C 575/17, paragraph 24 and the case-law cited).

The exclusion of an advantage in a cross-border situation whereas it is conferred in an equivalent situation in national territory constitutes a restriction on the free movement of capital (see Credit Suisse Securities (Europe) Ltd, C-601/23, para. 37).

Therefore, the answer to this question is that Company T's discrimination claim is plausible. There is a restriction on the free movement of capital because non-resident shareholders bear a final tax burden that resident shareholders may neutralize.

Part 3

By virtue of Article 65(1)(a) TFEU, Article 63 TFEU is without prejudice to the right of Member States to apply the relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their residence or the place where their capital is invested.

That provision, in so far as it constitutes a derogation from the fundamental principle of the free movement of capital, must be interpreted strictly. Therefore, it cannot be interpreted as meaning that any tax legislation which draws a distinction between taxpayers on the basis of their place of residence or of the Member State in which they invest their capital is automatically compatible with the FEU Treaty. The derogation provided for in Article 65(1)(a) TFEU is itself restricted by Article 65(3) TFEU, which provides that the national provisions referred to in Article 65(1) 'shall not constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments as defined in Article 63 [TFEU]' (Credit Suisse Securities (Europe) Ltd., C-601/23, paras. 50-51, Sofina and Others, C 575/17, para. 45 and the case-law cited).

A distinction must therefore be made between the differences in treatment authorised by Article 65(1)(a) TFEU and discrimination prohibited by Article 65(3) TFEU. It is clear from the Court's case-law that, before national tax legislation can be regarded as compatible with the provisions of the Treaty on the free movement of capital, the difference in treatment resulting from that legislation must concern situations which are not objectively comparable

or be justified by an overriding reason in the public interest (Credit Suisse Securities (Europe) Ltd., C-601/23, para. 52).

Possible justifications that member State S may submit to the Court include the following:

Balanced allocation of taxing powers between the Member States and prevention of risk of losses being used twice

Member States may argue they must be able to tax dividends paid by companies established in their territory (C-446/03 Marks & Spencer; C-337/08 X Holding).

They tax only the dividend at source, while the residence state taxes worldwide income.

Coherence of the tax system

The denial of the reimbursement of the WHT could be justified by the need to maintain the cohesion of the system. Member State S could argue that the domestic rules serve to maintain the cohesion of the national tax system, since the fact that losses sustained outside the source Member State by a non-resident company are not taken into account in that Member State follows a logic of symmetry and is the counterpart of the fact that the economic activities from which those losses arise are not taxed in that Member State. However, in order for an argument based on the need to maintain the cohesion of the national tax system to succeed, according to settled case-law a direct link must be established between the tax advantage concerned and the offsetting of that advantage by a particular tax levy (Credit Suisse Securities (Europe) Ltd., C-601/23, para. 79; Cofidis, C 340/22, para. 55 and the case-law cited).

Administrative effectiveness – effective collection of tax

It could be argued that that the restriction on the free movement of capital is justified by the need to ensure collection of the tax. Indeed, an immediately collectable tax charge payable by a non-resident company in receipt of dividends appears to be proportionate to the aim of preserving a balanced allocation of the power of taxation between the Member States, since the risk of the tax not being paid by such a company, increases over time, in the absence of any genuine and permanent link between that company and the country where the income arises. Refund procedures for non-residents may be costly and uncertain.

According to settled case-law, the need to ensure the effective collection of tax is a legitimate objective capable of justifying a restriction on fundamental freedoms, provided, however, that that restriction is applied in such a way as to ensure achievement of the aim pursued and not go beyond what is necessary for that purpose (Sofina and Others, C 575/17, para. 67 and the case-law cited). Furthermore, the Court has held that retention at source is a legitimate and appropriate means of ensuring the tax treatment of the income of a person established outside the State of taxation (Sofina and Others, C 575/17, para. 68 and the case-law cited).

Therefore, the answer to this question is that Member State S may submit several possible justifications, but the CJEU often finds outright denial of refunds disproportionate where it results in systematically heavier taxation of non-residents.

Part 4

A DTA allocates taxing rights between the contracting states and can provide beneficial treatment for the tax residents that are covered by their provisions, by providing reduced WHT rates for passive income.

The CJEU has held that a Member State cannot rely on a tax treaty to justify discrimination that would otherwise breach EU law (C-170/05 Denkavit Internationaal; C-72/09 Établissements Rimbaud).

Indeed, applying the lower WHT (10%) to the dividend payments in question does not solve the core problem, as residents in a comparable situation may still ultimately face 0% tax in loss situations, whereas comparable non-residents face final 10%.

According to the case law of the Court, unfavourable tax treatment that is contrary to a fundamental freedom cannot be regarded as compatible with EU law because of the potential existence of other advantages (Sofina and Others, C 575/17, para. 38 and the case-law cited, Credit Suisse Securities (Europe) Ltd., C-601/23, para. 45).

Therefore, the answer to this question is that the DTA reduction is irrelevant to the EU-law assessment. Even with a reduced rate, the discriminatory final burden remains.

PART B

Question 3

Part 1

The question indicates from the beginning that the group falls within the GloBE directive (Directive 2022/2523). The first question aims to discuss the role of posterior works to the adoption of the Directive and the dangers in referring to future OECD works in the Directive. The students should first acknowledge that the directive itself makes in several parts reference to the Pillar Two OECD Model Rules, for instance when it comes to the assessment of the IIR 'equivalence' or even in a more general way: "In implementing this Directive, Member States should use the OECD Model Rules and the explanations and examples in the [Commentary] as well as the GloBE Implementation Framework, including its safe harbour rules, as a source of illustration or interpretation in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law." The students should identify that EU law takes precedence over these documents/ guidelines, which should be used only as a source of illustration or interpretation and only if they are compliant with EU law. They should also critically argue that while this helps coherence in the implementation across the EU, it may also lead to paradoxical situations whereby future non-binding works on the Model Rules, even if agreed by consensus among the members of the Inclusive Framework, will be binding upon the Member States, without formally passing the unanimity rule and Art. 115 TFEU procedure.

Part 2

The exercise aims to make the students identify two main rules in the GloBE directive. First that the IIR is the main rule, and the collection of the 'top up' tax happens at the 'top' level of the structure (UPE – unless a POPE exists in the structure) and that if a QDMTT exists (or an 'equivalent' QDMTT) then the IIR or UTPR should be neutralized for the amount covered by the QDMTT for the domestic entities. With these in mind:

- State D will collect the IIR in respect of HCo as DCo qualifies as POPE;
- State D will collect the QDMTT in respect of DCo;
- The top up tax for E Co will be collected by way of IIR by Member State A as well as 50% of the top up tax (proportion to the ownership) for F Co; and
- The top up tax for PE G will also be collected by way of IIR by Member State A.

Part 3

ATAD and the GloBE Directive share a broadly similar origin in the EU's post-BEPS anti-avoidance agenda and pursue complementary objectives. They are therefore designed to operate in parallel, rather than to replace one another. This parallel application, however, can in practice generate situations of double taxation or additional tax burdens, for example where a Member State applies its ATAD CFC rules to include low-taxed income at parent level while, at the same time, the GloBE rules would trigger a top-up tax under the IIR.

As regards priority, ATAD has the wider scope and, accordingly, the ATAD rules are intended to apply first. The Commission has confirmed this approach, noting that it is consistent with the OECD Model Rules to continue applying the ATAD CFC rule in parallel with the GloBE rules: in practice, ATAD CFC rules apply first, and any additional taxes paid by a parent company under a CFC regime in a given fiscal year must then be taken into account under the GloBE computation by attributing those taxes to the relevant low-taxed entity for the purpose of calculating the jurisdictional effective tax rate. The same logic of sequencing applies to other ATAD-based taxes as well: where they arise, they should be reflected in the GloBE calculations so that the assessment of any residual top-up tax is made on the basis of taxes already levied under ATAD.

Question 4

Students may refer to the preamble of the ATAD that explains the structure, function and aim of the GAAR.

As mentioned in the preamble of the ATAD, general anti-abuse rules (GAARs) feature in tax systems to tackle abusive tax practices that have not yet been dealt with through specifically targeted provisions. GAARs have therefore a function aimed to fill in gaps, which should not affect the applicability of specific anti-abuse rules. Within the Union, GAARs should be applied to arrangements that are not genuine; otherwise, the taxpayer should have the right to choose the most tax efficient structure for its commercial affairs. It is furthermore important to ensure that the GAARs apply in domestic situations, within the Union and vis-à-vis third countries in a uniform manner, so that their scope and results of application in domestic and cross-border situations do not differ. Member States should not be prevented from applying penalties where the GAAR is applicable. When evaluating whether an arrangement should be regarded as non-genuine, it could be possible for Member States to consider all valid economic reasons, including financial activities.

Basic elements and function of the GAAR

The ATAD includes a number of anti-tax avoidance rules with the aim to coordinate Member States' responses to aggressive tax planning. The overarching goal is to:

- combat aggressive tax planning;
- ensure taxation reflects economic reality; and
- promote a more consistent level of protection across the internal market.

Article 6 ATAD introduces a mandatory General Anti-Avoidance Rule (GAAR) applicable to corporate taxation in the EU. Its function is to allow tax authorities to disregard artificial arrangements that, while formally complying with the law, defeat its purpose and provide an undue tax advantage.

Article 6(1) is structured around two cumulative conditions (a) main purpose (or one of the main purposes) and (b) not genuine arrangements.

The arrangement (or series of arrangements) must have a main purpose of obtaining a tax advantage that defeats the object or purpose of the applicable tax law. This is a subjective/objective hybrid test: authorities look not only at explicit intent but also at how the structure operates in practice.

The arrangement is considered “not genuine” to the extent that it is not put into place for valid commercial reasons which reflect economic reality. This introduces the idea of economic substance. The more artificial the structure, the more likely Article 6 applies.

If both limbs of the test are satisfied, then tax authorities ignore the artificial arrangement and compute tax “by reference to economic reality.”

The application of the GAAR does not include the imposition of a penalty in itself. The result of the application of the GAAR is to re-characterise or disregard arrangements in order to restore taxation consistent with the law's purpose. ATAD deliberately sets a minimum standard. Provided they are at least as effective as the ATAD GAAR, Member States may:

- adopt stricter GAARs; or
- preserve national doctrines (e.g., abuse of law, sham doctrine).

Relationship with other anti-avoidance rules

The ATAD includes a number of specific anti-abuse rules (SAARs). SAARs are targeted provisions and include CFC rules, interest deduction limitation rules and hybrid mismatch rules. In addition to the ATAD, specific anti-abuse rules are also found in other directives, such as the parent-subsidiary directive and the merger directive.

The key principle is that SAARs operate first whereas the GAAR operates residually.

GAAR comes into play when aggressive planning falls outside the precise wording of SAARs but still frustrates the law's intent. The aim of the GAAR is to fill the gaps.

However, GAAR cannot be used to contradict the legislature's deliberate choices. If a SAAR clearly allows a particular outcome, it is generally inappropriate to invoke GAAR to override it (unless the arrangement is clearly abusive in the broader sense of EU law).

Many Member States already had anti-abuse doctrines. Article 6 is designed to coexist with these rules. Where national rules are stricter, they remain valid. Where national rules are weaker, they must be strengthened to match ATAD. The GAAR therefore functions as a floor, not a ceiling.

CJEU case law and the shaping of Article 6

The ATAD GAAR is heavily inspired by the CJEU's doctrine of abuse of rights. The most important cases are:

Halifax (C-255/02): birth of the general abuse doctrine

In Halifax, the Court held for the first time in a VAT case that EU law cannot be relied upon for abusive or fraudulent ends. Two key ideas emerged:

- Transactions constitute abuse when their essential aim is to obtain a tax advantage contrary to the purpose of the legislation.
- Authorities may redefine transactions to reflect economic reality.

These concepts are mirrored almost word-for-word in Article 6 ATAD.

Cadbury Schweppes (C-196/04): freedom of establishment and artificiality

After VAT and the Halifax judgment, the abuse of law doctrine was transposed in direct taxation cases, following the judgment of the court in the Cadbury Schweppes case. In the context of controlled foreign companies (CFCs), the Court distinguished between:

- genuine economic activity carried out in another Member State, which must not be penalised; and
- wholly artificial arrangements designed to circumvent national tax law.

This case influenced ATAD's emphasis on "valid commercial reasons" and "economic reality."

Eqiom (C-6/16): Member States may neither employ general presumptions of abuse nor define any tax planning or structuring as abusive in light of secondary EU law or the fundamental freedoms

In this case, which concerned the application of the parent-subsidiary directive, the Court held that

- A general presumption of abuse is not allowed; anti-abuse measures must be targeted at wholly artificial arrangements, they cannot be based on broad, automatic presumptions.
- Member States may refuse directive benefits in abusive situations, but only where authorities show objective indicators of artificiality — such as lack of economic substance, conduit structures, or purely tax-driven arrangements.
- Taxpayers can be asked to provide evidence, but Member States cannot impose overly restrictive or automatic burdens that undermine the directive's benefit.

The Danish beneficial ownership cases (C-116/16, C-117/16 etc.)

These cases stress that:

- Member States may deny directive benefits (Parent–Subsidiary, Interest–Royalties) where structures are purely artificial, and
- tax authorities must look beyond formal ownership to identify beneficial ownership and the real purpose of arrangements.

They reinforce the legitimacy of anti-abuse provisions, provided they remain proportionate and evidence based. It emerges from the case law of the Court that:

- 1) Abuse requires objective and subjective elements: both artificiality and a tax-driven aim.
- 2) Proportionality is essential: automatic denial rules are suspect if they do not allow case-by-case assessment.
- 3) Economic substance matters more than legal form.

ATAD's GAAR essentially codifies these principles into EU secondary law.

To conclude, in practice, Article 6 of the ATAD fills gaps between specific anti-avoidance measures, harmonises the concept of abuse across Member States, supports the integrity of the internal market by discouraging harmful tax competition, and gives tax authorities a legal basis to challenge sophisticated planning schemes. At the same time, it is not intended to punish legitimate tax planning or discourage cross-border structuring grounded in real economic

substance. The GAAR under Article 6 ATAD targets arrangements whose main purpose is to obtain an illegitimate tax advantage, and which lack genuine economic substance. It allows authorities to tax based on economic reality instead of legal form. Its structure and limits are deeply influenced by CJEU case law, especially Halifax, Cadbury Schweppes, Egiom, and the Danish beneficial-ownership cases.

PART C

Question 5

The students are required to analyse the CJEU case law in respect to the utilization of PE losses by the headquarters in another State. They should be able to distinguish between the parent/ subsidiary case law, although it will be useful to mention that the doctrine of 'final losses' and the need that they are taken into account 'somewhere' originates in the Marks and Spencer judgment (C-446/03). PE relevant case law begins with the Deutsche Shell (C-293/06) and Lidl Belgium (C-414/06) cases.

The students should be able to identify the particular relevance of the balanced allocation of taxing rights as a justification to the restriction imposed by the inability to utilize losses in another Member State. They should be able to justify the need for this 'symmetry' between taxing profits and deducting losses which is preserved through the allocation of taxing rights in DTCs as per the Timac Agro (C-388/14) and Nordea Bank (C-48/13) cases. Thus, if the State of the headquarters does not tax the profits of the PE, as per the DTC, it does not have to consider the losses either. Whether the 'final losses' doctrine or the 'balanced allocation of taxing rights' doctrine should take precedence was decided in the W AG judgment (C-538/20) where the Court decided that if the State of the headquarters has waived its right to tax the profits of the PE, then it should not have to deduct the losses, even if those are final.

Question 6

Withholding taxes are generally permissible, but they must comply with the fundamental freedoms; free movement of capital for portfolio holdings and establishment for controlling stakes as well as free movement of services for services providers. A withholding tax is problematic where it discriminates or restricts cross-border payments by imposing a heavier effective burden on non-residents - for instance, the most common problem being taxing them on a gross basis or denying expense deductions, as in *Gerritse* (C-234/01) and *Scorpio* (C-290/04). Expenses should be deducted (if this is allowed domestically) as long as they are linked to the business carried. Differences in collection methods can be acceptable only if they do not produce a higher overall burden for comparable situations and remain proportionate (see *Truck Center*, C-282/07).

The key point is whether resident and non-resident recipients are in objectively comparable situations for the income concerned; unequal treatment of outbound dividends has repeatedly been condemned (e.g., *Amurta*, C-379/05; *Denkavit*, C-170/05). In these cases, the Court has repeatedly ruled that once a Member State is imposing a withholding tax, it extends its taxing rights to the non-resident taxpayers in a way that the non-residents become comparable to the residents. Accordingly, the two should be granted equal treatment and the source state should eliminate the discriminatory restriction.

Restrictions may be justified by overriding reasons such as effective fiscal supervision – the most commonly used justification in that context, but only if the measure is suitable and necessary (proportionality). In *Brisal* (C-18/15), for instance the Court stated that withholding tax on non-residents may be justified by overriding reasons such as effective tax collection—but it struck down the Portuguese rule because denying non-residents any deduction of directly linked costs went beyond what was necessary.

Question 7

Direct taxation was never fully harmonised in the EU. The EU Treaties did not provide explicitly for the harmonization of direct taxes, in the same way that they provide for indirect taxation. Member States kept primary competence over direct taxes (income tax, corporate tax, capital gains, etc.). However, from early on, the Court of Justice recognised that when Member States exercise their competence to tax in a way that affects the internal market, then EU law applies.

The foundations lie in early judgments where national tax rules conflicted with the Treaties' fundamental freedoms, especially the free movement of workers, the freedom of establishment, the free movement of capital, and the freedom to provide services.

The key case is the *Avoir fiscal* case of 1986 (C-270/83). France granted tax credits only to resident shareholders of insurance companies. The Court held that this discriminated against non-resident companies that were established in France through protected by the freedom of establishment.

This judgment marked the beginning of the statement that — even without harmonisation — Member States must exercise their tax jurisdiction consistently with Community (now EU) law.

Over time, the Court repeated and refined the doctrine, consolidating the principle that direct taxation competence belongs to Member States, but they must respect EU law when exercising that power.

Important milestones in the case law of the Court include:

- The *Schumacker* case (C-279/93), where the Court held that national income tax rules are not compatible with the free movement of workers when non-resident workers face a tax disadvantage where most income earned in the source State.
- The *Bachmann* case (C-204/90), where the Court held that a possible justification of a discriminatory tax measure exists where tax cohesion is at stake.
- The *Futura Participations* case (C-250/95), where the Court clarified the impact of the principle of fiscal territoriality but also acknowledged limits to the justification it may provide.
- The *Marks & Spencer* case (C-446/03), where the Court held that even though legislation that limits the setting off of foreign losses is, in principle justified, the limitation must respect proportionality and allow deductibility of final foreign losses.
- The *Cadbury Schweppes* case (C-196/04), where the Court developed its concept of anti-avoidance and artificial arrangements in direct taxation.

In practice, competence remains national, but it is not unlimited. Member States choose the tax bases, rates, reliefs, exemptions, structures of corporate and personal tax; however, they cannot design or apply those rules in ways that discriminate on the basis of nationality or residence or restrict fundamental freedoms, unless there is a legitimate public interest objective, and the measure is suitable, necessary, and proportionate.

This approach adopted by the Court had a huge impact on the evolution of EU direct tax law.

Since legislation harmonising direct taxes is limited, the CJEU has become the main engine shaping rules through case law, through the so-called “negative harmonization”, a process of removing the barriers by encouraging coordination and minimum standards.

Case law pressure helped drive political initiatives, including the Anti-Tax Avoidance Directive (ATAD), which partly codifies principles forged by the Court.

On the other hand, the doctrine has also exposed tensions. Member States argue that judicial scrutiny narrows fiscal sovereignty. The Court has been accused of “activism”.

The Court sometimes must balance freedoms against legitimate revenue protection.

In addition, fragmentary case-driven change can create uncertainty until legislation follows.

But the central message remained stable: EU law does not replace national tax systems, it aligns them.

Question 8

Legal nature of the Arbitration Convention

The Arbitration Convention (90/436/EEC) is formally a multilateral international treaty concluded by the Member States, not a directive or regulation adopted under the Treaties; as such it is not EU legislation.

That means that it is binding on Member States because they ratified it, it operates outside the ordinary EU legislative framework, and it is not subject to the monitoring of the European Commission or the scrutiny of the Court of Justice. Concerning its primacy over national law, this depends on the constitutional provisions of each member state that regulate the relationship between national and international law; this is not the same as EU law that enjoys primacy. Its initial duration was limited and required periodic renewal, highlighting its treaty-based character.

The Convention aims to eliminate double taxation arising from transfer pricing adjustments between associated enterprises situated in different Member States. It provides for a mandatory dispute resolution mechanism.

Although not part of EU law, the Convention is linked with the EU internal market objectives, and it is interpreted with awareness of fundamental freedoms and State aid constraints.

However, because it is not “EU law” in the strict sense, individuals cannot generally rely on it with the same direct effect expectations as for EU directives or regulations.

Scope of the Arbitration Convention

The material scope of the Convention is narrow and technical: it is limited to transfer pricing and PE profit adjustments. It applies only to transfer pricing adjustments between associated enterprises, and adjustments to profits attributable to permanent establishments in cross-border situations.

As far as the personal and territorial scope is concerned, the Convention applies to enterprises resident in Member States, transactions between “associated enterprises” and cross-border adjustments within the EU.

The mechanics of the Arbitration Convention

The Arbitration Convention provides for a two-stage dispute resolution procedure.

Stage 1 consists of the traditional Mutual Agreement Procedure (MAP). When double taxation arises from the adjustment of profits, the taxpayer submits a complaint to the competent authority of its Member State. Authorities of the relevant Member States attempt to resolve the case by agreement. They have two years from the date the case is first submitted to both competent authorities. If they reach an agreement, then the case is resolved, and the result eliminates double taxation.

Stage 2 consists of mandatory binding arbitration. If MAP fails and no agreement is reached within two years, an Advisory Commission (arbitration panel) is established. It consists of representatives of competent authorities plus independent experts. The Advisory Commission issues an opinion on how to eliminate the double taxation and submits it to the Competent Authorities. The Competent Authorities then have six months to either adopt the opinion, or agree another solution eliminating double taxation. If they fail to do so, the opinion becomes binding.

Implications of the Arbitration Convention's legal nature

Because it is a treaty between Member States and not part of EU Law, there is weak institutional oversight. There is no Commission infringement mechanism in the strict sense if states delay or underperform. Compliance relies on political pressure rather than robust supranational enforcement. In addition, fragmentation risks are high. Divergent interpretations and inconsistent practice may develop between Member States. These limitations motivated later reform — in particular, the 2017 EU Dispute Resolution Directive.

Relevance after the EU Tax Dispute Resolution Directive (2017/1852)

The Directive builds on and modernises cross-border tax dispute resolution by introducing broader material scope (beyond transfer pricing) covering any double taxation disputes relating to income or capital were covered by tax treaties. The Directive provides for clearer taxpayer rights, including access, information and time limits, as well as enhanced transparency and enforceability obligations on Member States. It also provides for mandatory binding arbitration if mutual agreement fails.

It effectively dispute resolution: The Directive, being EU secondary law, is subject to supervision and judicial review by the EU Institutions. The Commission monitors the effective and uniform implementation of the Directive, and the Court ensures the uniform interpretation of the Directive.

The adoption of the Directive did not abolish the Arbitration Convention. Instead, the Convention still applies to transfer pricing and PE profit allocation disputes.

Taxpayers may, in principle, choose between mechanisms (subject to coordination rules to avoid duplication). The Directive however is the preferred dispute resolution method in the EU, as according to the Directive itself, if a taxpayer uses the mechanism of the Directive, all other procedures cease immediately and automatically.

In practice, many taxpayers might also prefer the Directive because it has a broader scope, it provides for stronger procedural guarantees, coupled with firmer enforcement and transparency.

The residual role of the Arbitration Convention means that it functions as a specialised, legacy instrument for transfer pricing disputes, providing a tested arbitration structure. Its relevance is reduced but not obsolete. It continues to matter particularly where the Directive does not apply (older disputes, procedural exclusions), or taxpayers strategically prefer its structure.