THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

December 2023

MODULE 3.01 – EU DIRECT TAX OPTION

SUGGESTED SOLUTIONS

PART A

Question 1

The question draws a lot from the ‘funds-specific’ EU tax law. The facts resemble (with modifications) the Emerging Markets case (C-190/12), but the students could solve the case even if they are not aware of this case/case law. The candidates are expected to identify the following.

Part 1

Discussion whether free movement of capital applies because of the involvement of a third country. Reference to the definite influence test and identification that the holding does not appear to have any relevance here, thus free movement of capital applies. Bonus if they mention that EU law should prevail over the DTC.

Identification of a restriction in that domestically, distributions are not subject to a WHT but cross border they are. The difference in treatment lies on the fact that a higher tax burden is imposed on the basis of the ‘seat’ of the fund (one of the requirements for exemption from WHT is that the fund’s registered office is in Member State Q). Comparability: the resident / non-resident investors become comparable in so far as, in each case the state of the fund (Q) has extended its tax jurisdiction to the ‘foreign taxpayer’ through the imposition of the WHT (as it happens in the present case).

Additional credit if the candidates referred to the ‘distinguishing criterion approach’ as this was first discussed in the Santander case (C-338/11) – the ‘source’ of the different treatment/ the ‘distinguishing’ criterion is the ‘seat of the fund’ that does not reflect an objectively different situation.

Possible justifications: here, the candidates could discuss a series of justifications with the most prominent one being the effectiveness of fiscal supervision.

Part 2

The second part of the question is partly discussed in Fidelity Funds (C-480/16) – whether taxation could be moved from the vehicle to the shareholder. However, the candidates could solve the case without prior knowledge of this case.

Under the facts of part (2), the national law appears to allow for an exemption from WHT on condition that the dividend is taxed in the hands of the recipient. Thus, the purpose of the law appears to ensure taxation at least once. That would seem to be justified both on grounds of combatting tax avoidance but also on ground of the coherence principle equalling exemption from WHT because of taxability in the hands of the investor. For this last condition to be valid, however, it would have to be assumed that the same requirement applies also to domestic investors/taxpayers.

Part 3

The existence or inexistence of a DTC between the two states would play a role in what regards possible grounds for exchange of information (EoI, Art. 26 OECD MC). If a DTC existed with an EOI clause, then it could be assumed that the justification based on the effectiveness of fiscal supervision would be more easily satisfied. Having to deal with a third state, the EU law framework on EoI (DACs) does not apply, hence only a DTC could provide for such a safety net.

Question 2

Short description of the issue

Mr X, a resident of EU Member State A, has received an offer to work as an employee of Company Y, which is established and has its only premises in EU Member State B. Mr X lives with his family, close to the border with Member State B, and Company Y's premises are located a few kilometres away across the border.

According to the double tax treaty between Member State A and Member State B, income from employment is exclusively taxable in the source state. Therefore, if Mr X continues to be a resident in Member State A, his worldwide income will be taxable only in Member State B and he will have no taxable income in his state of residence. However, Mr X is entitled to certain personal tax benefits as a resident in Member State A that he risks losing, if he has no taxable income there. At the same time Member State B only grants similar personal tax benefits to persons who are residents in Member State B.

Mr X asks what, if any, protection he has under the EU fundamental freedoms.

On whether EU law and the fundamental freedoms applies in this situation

As the Court has repeatedly stated, although, as EU law stands at present, direct taxation does not as such fall within the purview of the EU, the powers retained by the Member States must nevertheless be exercised consistently with EU law (see for example Schumacker, C-279/93, paragraph 21). As far as the free movement of workers is concerned, Article 45(2) TFEU provides that such freedom of movement shall entail the abolition of any discrimination based on nationality between workers of the Member States as regards employment, remuneration and other conditions of work and employment.

On whether cross-border workers can enjoy tax benefits in the source state

In that connection, the Court held in Case C-175/88 Biehl (paragraph 12) that the principle of equal treatment with regard to remuneration would be rendered ineffective if it could be undermined by discriminatory national provisions on income tax. That is why the Council laid down the requirement in Article 7 of Regulation (EEC) No 1612/68 of 15 October 1968 on the free movement of workers within the Com¬ munity (OJ, English Special Edition 1968 (II) p. 475) that workers who are nationals of a Member State are to enjoy, in the territory of another Member State, the same tax benefits as nationals working there (Schumacker, C-279/93, paragraph 23). The Court has also consistently held that the rules regarding equal treatment forbid not only overt discrimination by reason of nationality but also all covert forms of dis¬ crimination which, by the application of other criteria of differentiation, lead in fact to the same result (Case 153/73 Sotgiu, paragraph 11). National rules under which a distinction is drawn on the basis of residence in that non-residents are denied certain benefits which are, conversely, granted to persons residing within national territory, are liable to operate mainly to the detriment of nationals of other Member States. Non-residents are in the majority of cases foreigners. In those circumstances, tax benefits granted only to residents of a Member State may constitute indirect discrimination by reason of nationality (Schumacker, C-279/93, paragraph 28-29). The case of residents and non-residents are not as a rule comparable in relation to direct taxes.

It is incompatible in principle with the rules on freedom of movement for a worker who has made use of that right to be the subject of less favourable treatment in the Member State of which he is a national than he would receive if he had not made use of the opportunities offered by those rules. However, it must be remembered that discrimination can arise only through the application of different rules to comparable situations or the application of the same rule to different situations (see, inter alia, Schumacker, C-279/93, paragraph 30; Gschwind, C-391/97, paragraph 21; and Case C-383/05, Talotta, paragraph 18).

Income received in the territory of a Member State by a non-resident is in most cases only a part of his total income, which is concentrated at his place of residence. Moreover, a non-resident's personal ability to pay tax, determined by reference to his aggregate income and his personal and family circumstances, is more easy to assess at the place where his personal and financial interests are centred. In general, that is the place where he has his usual abode. Accordingly, international tax law, and in particular the Model Double Taxation Treaty of the Organization for Economic Cooperation and Development (OECD), recognises that in principle the overall taxation of taxpayers, taking account of their personal and family circumstances, is a matter for the State of residence.

The situation of a resident is different in so far as the major part of his income is normally concentrated in the State of residence. Moreover, that State generally has available all the information needed to assess the taxpayer's overall ability to pay, taking account of his personal and family circumstances. Consequently, the fact that a Member State does not grant to a non-resident certain tax benefits which it grants to a resident is not, as a rule, discriminatory since those two categories of taxpayer are not in a comparable situation (Schumacker, C-279/93, paragraph 32-34). The position is different, however, in a case where the non¬ resident receives no significant income in the State of his residence and obtains the major part of his taxable income from an activity performed in the State of employment, with the result that the State of his residence is not in a position to grant him the benefits resulting from the taking into account of his personal and family circumstances.

In the case of a non-resident who receives the major part of his income and almost all his family income in a Member State other than that of his residence, discrimination arises from the fact that his personal and family circumstances are taken into account neither in the State of residence nor in the State of employment (Schumacker, C-279/93, paragraph 38).

The findings of the Court in the Schumacker case were confirmed subsequently in the Case C-169/03, Wallentin. Persons who receive only a small part of their income in the Member State of residence are, from the point of view of their tax treatment, in a comparable position to persons who reside in the Member State in which they receive their income. Where a person’s income is subject to little or no tax in his Member State of residence, that State cannot ensure that the tax paid on income received in another Member State is deducted from the taxable amount.

The Court has also held that, in a situation in which there is no taxable income in the Member State of residence under the tax legislation of that State discrimination could arise if the personal and family circumstances of a person were taken into account neither in the Member State of residence nor in the Member State of employment (Wallentin, C-169/03, paragraphs 17-18; Commission v Estonia, C-39/10, paragraph 53).

Similarly in the Gschwind case (C-391/97) the Court also held that where a Member State grants an allowance for income below certain amounts in order to ensure taxpayers a minimum subsistence amount, that benefit should also be granted to non-residents, since it is granted in accordance with the personal situation of the taxpayer.

<u>On whether there is a justification</u>

Once the Court has established comparability of residents and non-resident workers, as is the case when a non-resident worker acquires almost all or most of his income in the source state as is the case with Mr X, no justification has been accepted by the Court that would allow the source state to discriminate and not grant to Mr X the personal tax benefits that the source state provides for its own resident taxpayers.

It has been suggested that different treatment is justified by the need for consistent application of tax regimes to non-residents. That justification, based on the need for cohesion of the tax system, was upheld by the Court in Case C-204/90 Bachmann. According to that argument, there is a link between the taking into account of personal and family circumstances and the right to tax worldwide income. Since the taking into account of those circumstances is a matter for the Member State of residence, which is alone entitled to tax worldwide income, it is argued that the State on whose territory the non-resident works does not have to take account of his personal and family circumstances since otherwise the personal and family circumstances of the non-resident would be taken into account twice and he would enjoy the corresponding tax benefits in both States (see also Commission v Estonia, C-39/10, paragraph 57). That argument however was rejected in Schumacker and in later also in Commission v Estonia, since the State of residence could not take account of the taxpayer' s personal and family circumstances because the tax payable there was insufficient to enable it to do so. The Court concluded in Schumacker that where that is the case, the EU principle of equal treatment requires that, in the State of employment, the personal and family circumstances of a foreign non-resident be taken into account in the same way as those of resident nationals and that the same tax benefits should be granted to him (Schumacker, para. 41).

Similarly, the argument that administrative difficulties prevent the State of employment from ascertaining the income which non-residents working in its territory receive in their State of residence was also rejected. The Court pointed out to the administrative assistance directive as an effective tool that provides for ways of obtaining information comparable to those existing between tax authorities at national level. There is thus no administrative obstacle to account being taken in the State of employment of a non-resident' s personal and family circumstances (Schumacker, para. 45).

<u>Conclusion</u>

According to the established case law of the Court, Mr X enjoys the protection of the TFEU, once he has exercised his freedom to move and undertake employment in a Member State other than the state of his residence. The fact that he will receive the total of his worldwide income in Member State B, which is the state of his employment, even if he still remains a resident of Member State A, puts him in a comparable situation with tax residents of Member State B (source state; state of employment). Therefore Member State B is obliged to grant to Mr X all the personal tax benefits that it provides for its own tax residents. If Member State B does not comply with this obligation, MR X can make a complaint to the Commission or pursue any available domestic legal remedies to challenge the refusal of Member State B to treat him in the same way as resident taxpayers, relying directly on Article 45 TFEU.

PART B

Question 3

The present question draws from the Hervis (C-385/12), Tesco (C-323/18) and Vodafone (C-75/18) line of case law. The candidates could approach the question posed both from a fundamental freedoms' perspective and a state aid aspect.

With regard to fundamental freedoms, the candidates should identify that the turnover tax is, at first place, an acceptable from of taxation, compatible with the ability to pay principle, and the applicable case law (and principles) to income taxes, should apply in the present case too. The candidates should elaborate mainly on whether discrimination exists at first place here. Does the turnover tax allow for covert/indirect discrimination in the present case? As provided in settled case law, not only overt discrimination based on the location of the seat of companies, but also all covert forms of discrimination which, by the application of other criteria of differentiation, lead in fact to the same result are, in that regard, prohibited. As the turnover tax in the present case makes no distinction between undertakings according to where they have their registered office, the candidates should consider whether the steep progressivity of the tax could lead to indirect discrimination (to the disadvantage of companies owned by 'foreign' corporations). At this stage, they could pursue their own analysis or follow AG Kokott's/CJEU's judgment in Vodafone (and other judgments) that suggest that de facto discrimination is not a problem for the fundamental freedoms to resolve.

In terms of state aid analysis, the candidates would be expected to conduct an analysis similar to the one the CJEU followed in Vodafone, notably that for taxes to fall within the scope of the state aid provisions, they should form an integral part of the aid measure. For a tax to be regarded as forming an integral part of an aid measure, it must be hypothecated to the aid measure under the relevant national rules, in the sense that the revenue from the tax is necessarily allocated for the financing of the aid and has a direct impact on the amount of that aid. It would be left to the candidates to decide from the given facts of the case whether this is the case here. If so, then a brief analysis of the elements of Art. 107 TFEU would be expected, especially advantage and selectivity.

Question 4

Short description of the issue

Under the domestic legislation of Member State D, investment vehicles can be established under a variety of types, such as investment funds of various legal forms. The Government considers the possibility of granting a tax exemption to certain investment vehicles that invest in real estate, limiting the tax exemption to only one type of investment fund, which can only be constituted under the domestic legislation of Member State D. I was asked to provide an assessment of whether such legislation would be compatible with the EU Fundamental freedoms.

Application of the EU Fundamental Freedoms in direct tax matters

First of all it must be observed that according to the established case law of the Court, although direct taxation falls within the competence of the Member States, they must nevertheless exercise their direct taxation powers in accordance with European Union law, especially the fundamental freedoms (see for example Schumacker, C-279/93; de Groot, C-385/00; Santander, C-338-347/11; Itelcar, C-282/12). The fundamental freedoms that are mainly relevant for direct taxation issues are: the free movement of workers (Article 45 TFEU); the freedom of establishment (Article 49 TFEU); the freedom to provide services (Article 56 TFEU); the free movement of capital (Article 63 TFEU) and the freedom to move and reside freely within the territory of the EU (Article 21 TFEU). The first four relate to economically active operators whereas the fifth one applies to non economically active persons (such as pensioners).

On which freedom(s) may be affected by the proposed measure

A specific direct tax measure may come within the scope of more than one fundamental freedoms. However the Court has repeatedly held that in order to ascertain whether national legislation falls within one or the other of the freedoms of movement, the purpose of the legislation at issue must be taken into consideration (C-196/04 Cadbury Schweppes and Cadbury Schweppes Overseas, paragraphs 31 to 33; Case C-452/04 Fidium Finanz, paragraphs 34 and 44 to 49; Case C-374/04 ACT Group Litigation, paragraphs 37 and 38; Case C 446/04 FII, paragraph 36; and Case C-524/04 Thin Cap Group Litigation, paragraphs 26 to 34). Accordingly, national provisions relating to holdings giving the holder a definite influence on the decisions of the company concerned and allowing him to determine its activities come within the material scope of the Treaty provisions on freedom of establishment (C-251/98 Baars, paragraph 22; Cadbury Schweppes and Cadbury Schweppes Overseas, paragraph 31; and Thin Cap Group Litigation, paragraph 27).

Investment in real estate can fall both under the freedom of establishment and the free movement of capital. Indeed, as regards property investments, in accordance with settled case-law, national measures which govern transactions by which non-residents make such investments on the territory of a Member State may come within the scope of both Article 49 TFEU, relating to freedom of establishment, and Article 63 TFEU, relating to the free movement of capital (UBS Real Estate, C 478/19 and C 479/19, paragraph 29).

Where it is not clear from the subject matter of that legislation whether it falls predominantly under the freedom of establishment (Article 49 TFEU) or the free movement of capital (Article 63 TFEU), the Court takes account of the facts of the case in point in order to determine whether the situation to which the dispute in the main proceedings relates comes within the scope of one or other of those provisions (KOB, C 206/19, paragraph 25). In addition, where a national measure relates to the freedom of establishment and the free movement of capital at the same time, the Court will in principle examine the measure in dispute in relation to only one of those two freedoms if it appears, in the circumstances of the case in the main proceedings, that one of them is entirely secondary in relation to the other and may be considered together with it.

The currently proposed legislation concerns the tax treatment of income from real estate investments carried out by certain investment vehicles. Although it does not exclude from its scope situations coming within the scope of the freedom of establishment, the proposed legislation concerns investments carried out with a view to making a financial investment, without any intention to influence the management and control of the undertaking. It is therefore liable predominantly to affect the free movement of capital. Any restrictions on freedom of establishment resulting from that legislation are an inevitable consequence of the restriction of the free movement of capital and do not, therefore, justify an independent examination of that legislation in the light of Article 49 TFEU (UBS Real Estate, C 478/19 and C 479/19, paragraph 33; C-342/20, A SCPI, paragraph 47).

Consequently, the proposed national measure should be examined exclusively in the light of the free movement of capital (Articles 63 and 65 TFEU).

On whether the proposed legislation constitutes discrimination or restriction

The Government considers the possibility of granting a tax exemption to certain investment vehicles that invest in real estate, limiting the tax exemption to only one type of investment fund, which can only be constituted under the domestic legislation of Member State D.

It follows from settled case-law that the measures prohibited by Article 63(1) TFEU, as restrictions on the movement of capital, include those that 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 (Société Générale, C 565/18, paragraph 22; UBS Real Estate, C 478/19 and C 479/19, paragraph 36). Specifically, the less favourable treatment by a Member State of income paid to non-resident collective investment undertakings, compared with the treatment of income paid to resident collective investment undertakings, is liable to deter undertakings established in a State other than that Member State from pursuing investments in that same Member State and, consequently, amounts to a restriction of the free movement of capital, prohibited, in principle, under Article 63 TFEU (College Pension Plan of British Columbia, C 641/17, paragraph 49).

It has been decided by the Court that the exemption of income received by a resident collective investment undertaking, whereas income received by a non-resident collective investment undertaking is subject to tax, constitutes such less favourable treatment (College Pension Plan of British Columbia, C 641/17, paragraph 50; A SCPI, C-342/20, paragraph 51).

The proposed legislation introduces a difference in treatment that is based not on the State of residence of the investment vehicle, but on the legal form taken by that vehicle. Only investment vehicles constituted under the particular law of Member State D may be eligible for the tax exemption. This feature will inevitably result in a situation where investment vehicles established according to the law in Member State D may enjoy the exemption but investment vehicles established under the law of other member states will not be eligible for the exemption because they will not be the investment vehicle type that can be constituted only according to the legislation of Member State D. Although it appears that the criterion for granting the exemption (legal form) is neutral, in fact it is mainly resident companies that may satisfy that criterion.

In that regard, it must be stated that national legislation which applies without distinction to resident and non-resident operators may constitute a restriction on the free movement of capital. It follows from the Court's case-law that even a differentiation based on objective criteria may de facto place cross-border situations at a disadvantage (Köln-Aktienfonds Deka, C 156/17, paragraph 55; UBS Real Estate, C 478/19 and C 479/19, paragraph 39; A SCPI, C-342/20, paragraph 54). That is, inter alia, the case where national legislation which applies without distinction to resident and non-resident operators reserves a tax advantage in situations in which an operator complies with conditions or obligations which are, by their nature or in fact, specific to the national market, in such a way that only operators present on the national market are capable of complying with those conditions or obligations, and non-resident operators which are comparable do not generally comply with those conditions or obligations (Köln-Aktienfonds Deka, C 156/17, paragraph 56; UBS Real Estate, C 478/19 and C 479/19, paragraph 40; A SCPI, C-342/20, paragraph 55). Where a Member State provides for a tax advantage in favour of certain investment vehicles, the conditions under which that advantage is granted must not constitute a restriction on the free movement of capital (Köln-Aktienfonds Deka, C 156/17, paragraph 46).

The free movement of capital would be rendered ineffective if a non-resident investment undertaking, constituted according to the legal form authorised or required by the legislation of the Member State in which it is established and which operates in accordance with that legislation, were to be deprived of a tax advantage in another Member State in which it invests solely on the ground that its legal form does not correspond to the legal form required for investment undertakings in that latter Member State (A SCPI, C-342/20, paragraph 61).

Consequently, the proposed legislation is liable to deter non-resident investment vehicles from investing in immovable property in Finland and therefore constitutes a restriction on the free movement of capital prohibited, in principle, by Article 63 TFEU.

<u>On whether the restriction can be justified</u>

Pursuant to Article 65(1)(a) TFEU, Article 63 TFEU is to be 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 place of residence or with regard to the place where their capital is invested. Article 65(1)(a) TFEU, in so far as it is a derogation from the fundamental principle of the free movement of capital, must be interpreted strictly. That provision cannot therefore be interpreted as meaning that all tax legislation which draws a distinction between taxpayers based on their place of residence or the State in which they invest their capital is automatically compatible with the Treaty (X (Controlled companies established in third countries), C 135/17, paragraph 60). The differences in treatment permitted by Article 65(1)(a) TFEU must not constitute, according to Article 65(3) TFEU, a means of arbitrary discrimination or a disguised restriction. The Court has held, consequently, that such differences in treatment are permitted only when they concern situations which are not objectively comparable or, otherwise, when they are justified by an overriding reason in the public interest. The comparability of a cross-border situation with an internal situation within a Member State must be examined having regard to the aim pursued by the national provisions at issue as well as to the purpose and content of those provisions (UBS Real Estate, C 478/19 and C 479/19, paragraph 47). Only the relevant distinguishing criteria laid down by the legislation in question must be taken into account in determining whether the difference in treatment resulting from that legislation reflects an objective difference in situations (UBS Real Estate, C 478/19 and C 479/19, paragraph 48).

According to the Court's settled case-law, a restriction on the free movement of capital is permissible if it is justified by overriding reasons in the public interest, if it is suitable for securing the attainment of the objective which it pursues and if it does not go beyond what is necessary in order to attain that objective (UBS Real Estate, C 478/19 and C 479/19, paragraph 60). The Court has accepted on the past as a valid justification the need to ensure the effectiveness of tax supervision, the collection of taxes and the need to ensure the coherence of the tax system. However, in order to guarantee the effectiveness of fiscal supervision, the tax authority may require the taxpayer to provide the proof that it considers necessary in order to determine whether the conditions for according the tax advantage in question, provided for in the legislation at issue, have been met and, consequently, whether to grant the advantage requested (Persche, C 318/07, paragraph 54), as well as for ensuring the effective collection of tax. As regards the administrative burden on the tax authorities of the Member States of taxation that would result from taxpayers being allowed the opportunity to provide the information to demonstrate that those conditions have been met, it should be noted that administrative disadvantages are not alone sufficient to justify a barrier to the free movement of capital (van Caster, C 326/12, paragraph 56). As far as the need to preserve the coherence of a tax system is concerned, the Court has held that a direct link has to be established between the tax advantage concerned and the offsetting of that advantage by a particular tax levy, the direct nature of that link falling to be examined in the light of the objective pursued by the legislation in question (UBS Real Estate, C 478/19 and C 479/19, paragraph 66). Such a direct link does not appear to be present in the proposed legislation.

Lastly, according to the Court's settled case-law unfavourable tax treatment contrary to a fundamental freedom cannot be justified by the existence of other tax advantages, even supposing that such advantages exist (van Caster, C 326/12, paragraph 31).

Conclusion

My conclusion is that the proposed legislation would introduce a restriction to the free movement of capital that cannot be justified by an overriding reason of public interest and therefore it is incompatible with the TFEU.

PART C

Question 5

The answer to this question should summarise the CJEU case law on losses utilization. It should mention the Marks and Spencer seminal judgment and follow the CJEU's sequence of arguments. The existence of restriction/different treatment when the scheme is only offered to domestic companies, and the justifications that can be used to justify such a different treatment: Balanced allocation of taxing rights, combatting tax avoidance and the danger of losses being used twice. Then, reference should be made to the proportionality principle and the need for 'final losses' to be taken into account somewhere. Any additional case law (X Holding, Papillon, Philips Electronics and so on) in this category (subsidiaries' losses taken into account by the parent) would add bonus points.

The candidates should also refer to the losses 'transfer' by a PE to the parent and the relationship between the taxability of profits and utilization of losses (balanced allocation of taxing rights) as this has been identified in a line of case law (e.g. Nordea bank (C-48/13) and Timac Agro (C-388/14)). Bonus points for reference to Aures Holding (C- 405/18) and the relationship between the 'finality of losses' and the transfer of the place of effective management. Candidates should also refer to the W AG judgement (C-538/20) where the CJEU found that freedom of establishment was not infringed when a Member State did not allow the deduction of final losses of a 'foreign' PE when the parent's state of residence had waived its power to tax the profits (and losses) of that PE under a double tax treaty.

Question 6

The candidates would be expected to explain here that in order to overcome the freedom of establishment 'obstacle', the GloBE directive has extended (in relation to the OECD Pillar Two Model Rules) its scope of application to large scale domestic groups. A second question to address is whether de facto discrimination (similar to the one discussed in Tesco/Vodafone, see above) could arise against foreign entities, due to the high revenue threshold. Following the CJEU's analysis in Tesco/ Vodafone, the answer should be no.

In a similar vein, there does not seem to be a danger from a state aid law perspective. The candidates could also consider whether the directive is compatible with the principles of subsidiarity and proportionality – this is a matter that has been discussed a lot in literature with opposing views, so any justified answer would bring bonus points. Bonus points for discussing whether the 'initial phase relief' in the directive could establish unfavourable treatment of cross-border situations vis-à-vis domestic ones.

Question 7

The establishment of an EU common corporate tax base has been on the Commission's policy agenda for a long time. The origin of this agenda goes back to the study on company taxation in the European Community carried out by the Ruding Committee in 1992. In 2001 the Commission presented a Company Tax Study and a related Communication which identified the development of a common consolidated tax base as the most promising policy option in the long term.

In 2011 the Commission tabled its proposal for a directive on a Common Consolidated Corporate Tax Base (CCCTB), which was subsequently modified and led to the publication of compromise proposals in 2012 and 2014. Member states were willing to discuss a common tax base but not the consolidation issues or the formulary apportionment issues. During 2015 and 2016 the work on the common tax base was stopped, as the focus had turned to the implementation of the results of the OECD BEPS project.

In 2016 the Commission relaunched its CCCTB proposal by submitting proposals for a Directive on a Common Corporate Tax Base (CCTB) and a Directive on Common Consolidated Corporate Tax Base (CCCTB), while at the same time withdrawing the initial 2011 proposal. The Commission adopted a staged approach: the first stage aimed at harmonizing the tax bases in the member states (the CCTB proposal) and the second stage would deal with the consolidation issues (CCCTB) and the formulary apportionment of the consolidated European profit.

There are two equally important general policy objectives underlying the CCTB/CCCTB proposals: the first one is to stimulate growth and investment within the EU and the second one is to enhance the fairness of corporate income tax within the EU. The first objective, to stimulate growth and investment in the EU, is served through the creation of a harmonised tax base and the expected reduction of the administrative burden for EU multinationals that have to comply with the different tax systems of the member states in which they operate. Similarly, the establishment of a one-stop-shop approach, i. e. the designation of the tax authority of one member state as the sole tax authority responsible for the consolidation and sharing mechanism further reduces the administrative burden, filing and documentation requirements for EU multinationals. In addition, the consolidation and sharing mechanism is considered as a fair and efficient response to profit shifting and base erosion concerns and as a tool to address tax planning issues within the EU.

The main features of the 2016 CCTB/CCCTB proposals are the following:

- It is an autonomous profit determination system for tax purposes, i.e. not linked to any specific existing system;
- It follows the generally accepted accounting principles;
- It includes participation exemption rules for major shareholdings;
- Provides for super-deductions in order to stimulate growth;
- Provides for cross-border loss relief;
- It included provisions to address BEPS issues (CFC rules, GAAR, mismatches, interest deduction limitation rules);
- Provided for a sharing formula of the profits that are determined following the determination of the consolidated tax base;
- Adopts the one-stop-shop approach so that the group has to deal with a single tax administration (principal tax authority);
- It is provided as a mandatory regime for large companies, i.e. companies belonging to a consolidated group for financial accounting purposes with a total consolidated group revenue in excess of EUR 750 million;
- SMEs that (due to their size or for any other reason) are excluded from the mandatory application may opt to apply the CCTB regime; if they opt to apply it, this choice is valid for a period of five years, automatically extended for successive 5-yer terms, unless the company notifies that it wants to withdraw;
- The tax rate at which companies are taxed under the CCTB/CCCTB regime is determined by the member state.

Question 8

The “rule of reason” is a concept developed by the Court of Justice in its Cassis de Dijon judgment (Case 120/78). Under this concept the Court has allowed unwritten reasons of public interest for restricting free movement rights. Under the rule of reason a restrictive national measure but is not mentioned in the treaty maybe acceptable if it is considered necessary in order to protect a legitimate public interest it does not distinguish between domestic and the comparable cross-border situation and respects proportionality, i.e. its restrictive effect does not go beyond what is necessary to protect that legitimate interest. The Court applies the rule of reason test in the same way as far as all treaty freedoms are concerned and also as far as all areas of law are concerned, including direct taxation.

The Court’s rule of reason test consists of the following steps:

1) Does the person invoking the protection of the treaty have sufficient treaty status?

2) Is the area to which the measure belongs harmonised? If yes, then it would be a matter of compatibility of the national measure with the secondary legislation that has been developed (it is no longer a matter of treaty freedoms).

3) If the measure belongs to an area that has not been (fully) harmonised, does it discriminate between domestic and cross-border situations? If the measure is directly discriminatory it cannot be upheld, unless it is justified by a provision in the treaty itself.

4) If the measure applies without distinction to cross-border and domestic situations, is it restrictive, in the sense that it creates obstacles to the exercise of the treaty freedom, making the cross-border situation less attractive?

5) If the measure is restrictive, does it serve a legitimate purpose, in other words is it justified by a mandatory requirement of public interest?

6) If the measure is justified, is it suitable (appropriate) to achieve that purpose?

7) And lastly, is the measure proportionate in relation to the legitimate aim pursued? Or does it go beyond what is necessary, resulting in an “overkill”?

The Court has summarised its rule of reason test in its Gebhard judgment (C-55/94).

Over the years, several justifications have been put forward in order to defend national direct taxation measures that were challenged as infringing the treaty freedoms. In general mere economic and budgetary policy goals are not acceptable as mandatory requirements of public interest. The court has accepted as a valid justification the need for effective fiscal supervision (Cassis de Dijon, Case 120/78; Futura, C-250/95). A similar justification, the need to ensure the effective collection of income tax has also been accepted by the Court as valid justification (Scorpio, C-290/04, and also Truck Center, C-282/07 and National Grid Indus, C-371/10). Another justification that has been accepted by the Court is the need to protect the cohesion of a tax system (first recognised in Bachmann, C-204/90), or the coherence of the tax system or, in more recent cases, the principle of symmetry or principle of territoriality (Krankenheim, C-157/07; N, C-470/04). A similar justification, overlapping with the principle of fiscal coherence and the principle of territoriality, is the need to safeguard the balanced allocation of taxing powers (Marks and Spencer, C-446/03; Oy AA, C-231/05), which has emerged as perhaps the most important one. Of similar importance is the need to prevent abuse of rights, especially the need to combat wholly artificial arrangements (Cadbury Schweppes, C-196/04).

Other examples of possible justifications that were put forward by member states but were not accepted by the Court include the need to prevent gambling, divorces and suicides (Lindman, C-42/02); administrative difficulties to obtain information from abroad (Bachmann, C-204/90); the setting off of the disadvantage by another advantage that is granted to the taxpayers affected by the measure (avoir fiscal, case 270/83); an argument that the discrimination is minor (avoir fiscal, case 270/83) or that discrimination can be avoided (by for example incorporating a subsidiary to carry out an activity otherwise carried on through a branch; avoir fiscal, case 270/83); the loss of tax revenue (ICI, C-264/96; Saint Gobain, C-307/97).