THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2021

MODULE 3.01 – EU DIRECT TAX OPTION

SUGGESTED SOLUTIONS

PART A

Question 1

The Member State provision is a discriminatory restriction that potentially engages either Article 49 TFEU (ref Bosal Holding C-168/01) or Article 63 TFEU (ref Verkooijen C-35/08).

Whilst both fields might be engaged depending upon the objective or purpose of the legislation, which will determine which of the freedoms is primarily engaged (FII GLO (2) C-35/11). Notwithstanding this, each has its specific area of application (Fidium Finanz C-452/04) and may be generally regarded as mutually exclusive (Gebhard C-55/94). Where the national legislation could engage both, regard is paid to the facts and to the level of investment. However relief from national legislation that engages Art. 63 TFEU will not be lost in relation to a third country investment just because the interest is a controlling interest (FII GLO (2) C-35/11).

Part 1

The restrictive provision is triggered at a 25% ownership threshold. That level is generally high enough to enable the shareholder to exert definite influence (Commission v Italy C-326/07 or Idrima Tipou C-81/09).

In the circumstances described, the claim would fall within the field of Article 49 TFEU but no relief is available as non-EU Co is resident outside of the EU.

However, if sufficient of the other investors are connected with each other and can, acting together, exert definite influence over the company, the circumstances might dictate that Article 63 TFEU will be engaged and relief will be available (Columbus C-298/05).

Part 2

Whilst the objective of the national legislation is unchanged, the circumstances of the investment are different and EU Parent is not in a position to exercise definite influence over non-EU Co, which might be a subsidiary of one of the other investors.

It might be different again if non-EU Co is a joint venture company and there is a side shareholders' agreement providing EU Parent with greater powers over the business of non-EU Co. In that case, Article 49 TFEU might be engaged (Columbus C-298/05) and no relief will be available.

Part 3

The objective of the national legislation is different and Article 63 TFEU will be engaged (FII GLO (2) C-35/11).

Question 2

This question is 'open-ended' and invites the student to demonstrate his knowledge and understanding of:

- Abuse of law.
- The Treaty freedoms of movement that might be engaged.
- "Wholly artificial arrangements" distinguished from artificial pricing.
- How the principle of proportionality might be applied against MS anti-avoidance provisions.
- "Exit taxation".

Marks will be awarded for any relevant points but some reference to those 5 key point headings is expected.

PART B

Question 3

Part 1

Comparability: deferral relief is denied under national rules because the property that Mr E proposes to buy will not be situated in EUstate. The national legislation therefor would deter the purchase of a principal private residence in another Member State and infringes Article 63 TFEU. However, as the relief is only available for a property in which Mr E will reside, the denial of relief also restricts Mr E's exercise of free movement to take up his employment. The principal restriction is to Article 45 TFEU as the purchase of a new principal private residence is to satisfy his needs in consequence of his move to take up employment. The restriction to Article 63 TFEU may be regarded as secondary to that to Article 45 TFEU – Fidium Finanz C-454/04.

Relevant case law could include Commission v Sweden C-104/06 and Commission v Portugal C-345/05.

It should be noted that Mr E would suffer the charge if he remained in EUstate and simply rented or if he 'downsized'. Accordingly, the denial of deferral relief could only be restrictive if he reinvests the whole of the proceeds of disposal in a replacement residence in his new state of residence. If he invests only part of the proceeds, part or all of the charge levied by EUstate may not give rise to a restriction.

Part 2

Having regard to the objective of the deferral scheme, EUstate can justify the charge on the ground of coherence of the tax system. The exit charge relates to a tax liability that accrued as a result of taxable events that were triggered by Mr E's actions (purchases of property) in the past and it can be distinguished from the exit tax charges examined by the Court in, say, National Grid Indus C-371/10 or N C-470/04. The coherence is that the scheme merely delays collection of duty until the buyer has the disposal proceeds from which he can pay the duty.

In contrast to the situation in Commission v Spain C-269/09, which concerned income accrued but not assessed at the time of migration, the duty in this situation has already been assessed and is payable because Mr E is not reinvesting the prior year gains that had funded the purchase of the residential property sold.

Question 4

Part 1

Article 63 TFEU is engaged. The first step in the analysis is to determine whether the Homea legislation gives rise to a restriction. A differing rule is applied depending upon the location of the immoveable property but that rule defines Homea's taxing jurisdiction in relation to tax on capital gains. The Court's case law is very muddled in such circumstances (see Bevola C-650/16).

The Hostia charging provision does not treat a resident owning foreign immoveable property in the same way as a resident owning immoveable property in the territory and it may be to his advantage or to his disadvantage. The purpose of the charging provision is to define taxing jurisdiction and regard could be paid to Aures C-405/18. In view of the uncertainty created by the Court's case law, any reasoned argument should be accepted. The restriction, if there is one, can be justified by reference to taxing powers and coherence of the tax system (K C-322/11 Para.71).

Part 2

K C-322/11 can be distinguished because the DTC in that case enabled the home state to take account of gains on foreign immoveable property for the purposes of progressive taxation albeit that the home state at the time only applied fixed rate taxation to capital gains. The DTC did not constrain home state jurisdiction. However, in the circumstances specified, Homea legislation does constrain jurisdiction where Hostia has the right under the DTC between them to tax gains realised on immoveable property located in its territory. The ability to justify the restriction, if there is one, is unchanged. Again, any reasoned argument should be accepted.

PART C

Question 5

The ‘exit tax’ charge will be analysed by reference to principles developed by the Court in National Grid Indus (C-371/10) and subsequent case law (ATAD only applies to persons subject to corporation tax).

Part 1

The Court has not considered the specific case of a tax depreciation clawback but would probably follow ATAD Art.5 that applies to the difference between market value and tax base value without distinguishing depreciation from appreciation. The tax assessed by the home state, at the option of Mr S, could be recovered immediately or paid over 5 years (DMC C-164/12 para 64), possibly subject to interest.

The permanent loss of part of the depreciable cost as a result of the home state clawback of depreciation being based on a higher valuation than the tax basis for Hostia’s tax depreciation is a result of disparities between the two systems of taxation and there is no remedy for that under the Treaty (Lindfors C-365/02 paragraph 34).

Part 2

As an alternative, Mr. S could provide the equipment under a lease at an arm’s length rent to a Hostia company (set up for the purpose) that subleases to the branch on a back-to-back basis. The lease would be protected under Article 56 TFEU (provision of services). Mr S’s right to continue to receive home state depreciation allowances would be protected – see Jobra case C-330/07.

Question 6

Part 1

Art. 45 TFEU & Commission v Estonia C-39/10. If Ms P is taxed by Originia as a resident, her tax liability would be: (4,000 + 10,000 – 12,000 = 2,000) x 25% = Euro 500 as compared with taxation as a non-resident: Euro 4,000 x 20% = Euro 800. Ms P suffers a higher level of taxation by Originia simply because she exercised a freedom of movement to take up residence in Hostia and to take up part-time employment there (paragraph 56). Accordingly, the more onerous taxation that she has suffered is such as to deter her from exercising the freedom of movement. Originia should allow Ms P to be taxed as a resident if she so elects.

Part 2

Ms P's tax in Hostia will be (10,000 – 9,000) x 15% = Euro 150 + Euro 4,000 x 15% = Euro 600 less credit relief for Originia tax on the income, which will extinguish the Hostia liability if Ms P is taxed as a non-resident by Originia.

If Ms P is taxed as a non-resident of Originia, she will pay Euro 800 to Originia and Euro 150 to Hostia = Euro 950. Marks will be awarded for reference to Gilly C-336/96 noting that the Treaty cannot require Hostia to provide relief for surplus Originia tax credit against the Euro 150 liability on Hostia income.

If Ms P is taxed as a resident of Originia, she is taxed at 25% on only half of her pension income but would be entitled to claim a tax credit for Hostia taxation. [Candidates are not being tested on whether they can solve the maths!]

Hostia taxation would be Euro 200 (+ Euro150) and Originia taxation would be Euro 400. The aggregate taxation would be Euro 750 and, thus, preferable.

Individually, Originia is 2,000 x 25% = 500 – (DTR) ½ x 200 = 400.

Hostia is 150 + (4,000 x 15% = 600- (DTR) 400 = 200) = 350.

Even though Ms P is a resident of Hostia, she should still be entitled to claim the tax credit for Hostia tax suffered by her on the income when it is taxed by Originia as she is being taxed as if she was a resident of Originia.

Question 7

Art.49 TFEU is engaged. Group Steria C-386/14 is directly in point but the question is seeking a discussion of the issues.

[It should be noted that the question specifies that there is taxation of the dividend from ForeignSub, not a notional disallowance of holding expenses, which seems to have distracted the Court in Groupe Steria. It could be argued that the French tax provision does not appear to disallow those expenses but makes an adjustment to the assessment by reference to those expenses as a proxy for taxing the dividend. Otherwise, the disallowance would not be restricted to the amount of the dividend. Importantly, there is no indication that there would be any disallowance of holding costs in a period in which no dividend is paid.]

Does an advantage arise under the different rules? Different rules are applied but are the situations comparable? A different rule applied to a different situation does not give rise to a restriction. Note: the profits of Sub are taxed in full on Parent whilst the profits of ForeignSub are taxed on Parent only to the extent distributed.

If a restriction is considered to have been created by the different rules applied, can the rules be justified? On what grounds? Coherence (x-reference Papillon C-148/07). The non-taxation of the dividend from Sub cannot be considered separately from the tax integration process, which involves consolidating the subsidiary as if it was a division of Parent (Papillon).

Question 8

Part 1

Art.56 TFEU is engaged. The denial of the grant may deter Ms B from attending a private college outside of Homea and that would obstruct the provision of services by private colleges located in other Member States. Art. 21 TFEU is potentially engaged but Art.56 TFEU also applies to protect the rights of potential recipients of services and, so, Art.21 TFEU would not be considered by the Court.

A publically funded college may not provide services for a consideration, which is necessary to engage Art. 49 TFEU. In such case, Art. 21 TFEU will be engaged (Schwarz C-76/05).

Part 2

If Ms B suffers discriminatory treatment under Hostia's income tax code, she potentially would have a claim pursuant to Art.45 TFEU. In the circumstances described, Ms B has no income other than the contribution from her parents, which should be exempt from tax in Hostia. Even if she did succeed in obtaining the grant from Homea, that, too, would be most likely exempt from taxation in Hostia. The comparator is whether such sources would be taxable in Hostia if sourced in that state. Accordingly, as in her period of temporary residence in Hostia, Ms B will be potentially taxable on the whole of her global taxable income, she should be entitled to receive a personal allowance to set against her earnings equal to the allowance that might be claimed by a resident of Hostia, having regard for time apportionment, if such would be applied to an allowance claimed by a resident (Wallentin C-169/03).

Question 9

Art. 49 TFEU is engaged (SGI C-318/10). Brief comparability analysis. Discussion could embrace, for instance, Baars C-251/98 and Columbus Containers C-298/05 – there are many cases. Homea is likely to have transfer pricing provisions. Justifiable restriction on ground of preservation of taxing powers (SGI, Impressa Pizzarotti C-558/19, Hornbach-Baumarkt C-382/16).

Proportionality – adjustment based on arm's length pricing – additional reference to Thin Cap GLO C-524/04 or Lammers C-105/07, chance for taxpayer to defend the pricing.

Reference to Hornbach paragraph 56: could InvestCo argue that it acted as a shareholder, agreeing to the pricing to maintain EngineerCo's business and balance sheet, or to avert 'tripping' banking loan covenants?