THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

December 2022

MODULE 3.01 – EU DIRECT TAX OPTION

ADVANCED INTERNATIONAL TAXATION (THEMATIC)

TIME ALLOWED – 3¼ HOURS

This exam paper has **three** parts: **Part A**, **Part B** and **Part C**.

You need to answer **five** questions in total. You will **not** receive marks for any additional answers.

You must answer:

- **Both** questions in **Part A** (25 marks each)
- **One** question from **Part B** (20 marks)
- **Two** questions from **Part C** (15 marks each)

Further instructions

- All workings should be made to the nearest month and in appropriate monetary currency, unless otherwise stated.
- You must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.
- Marks may be allocated for clarity of presentation of your answers.
- The time you spend answering questions should correspond broadly to the number of marks available for that question. You should therefore aim to spend approximately half of your time answering Part A, and the other half answering questions in Parts B and C.
- There is no separate reading time, so you can start typing your answers as soon as the exam begins. However, we recommend that you set aside some time to thoroughly read each question and plan each of your answers.

PART A

You are required to answer BOTH questions from this Part.

1. ABC is a multinational enterprise registered in Homeland, an EU member state. ABC has several subsidiaries and branches across the EU and the world.

   You are required to answer the following questions:

   1) WOW is a subsidiary of ABC resident in Blueland, another EU member state. ABC's management team seeks to utilise the group consolidation regime in Homeland, enabling the consolidation of profits and losses at the level of the parent company. However, Homeland's tax authority has refused to take WOW's losses into consideration.

   Is Homeland's position compatible with EU law? Is Homeland required to allow ABC to use WOW's losses for consolidation purposes? (10)

   2) ABC also has a permanent establishment (PE) in another EU member state, Pinkland. The PE has been making losses for the past three years, and ABC intends to take these losses into account.

   Can ABC do so, under EU law? Does it matter if the double tax agreement between Homeland and Pinkland provides for exemption of profits and losses? (7)

   3) ABC has another subsidiary, LIZ, in Redland, an EU member state with a statutory tax rate of 12%. ABC holds 80% of the capital in LIZ. Despite being profitable, LIZ has not distributed any profits to ABC in the past two years. The Homeland tax authority intends to apply its Controlled Foreign Company (CFC) legislation to ABC. ABC complains that this violates its freedom of establishment.

   Can Homeland apply its CFC legislation in this case? Is it compatible with EU law? (8)

   Total (25)

2. Company A is established in Country A, and is part of an EU multinational group whose parent company is registered in Country F. In December 2011, Company A acquired a 15% shareholding in Company B (established in Country B), from Company C (established in Country C). The acquisition was financed with a loan received from F-Bank, established in Country F.

   All four countries are EU member states and all four companies (Company A, Company B, Company C and F-Bank) are members of the same multinational group.

   In subsequent years, Company A made interest payments to F-Bank. F-Bank was able to offset the interest income with losses incurred from other transactions.

   According to the corporate income tax rules in Country A, no deduction is granted for interest paid to a company within the same group that is resident in a different EU member state, on the basis that the principal reason for the loan is deemed to be the obtaining of a tax benefit which would not exist if both companies had been residents in Country A. Accordingly, the Country A tax authority has denied the interest deduction.

   You are required to explain, with reference to the Treaty on the Functioning of the European Union and the case law of the Court of Justice of the European Union, whether EU law can provide Company A with any remedy.

   You should identify which freedom applies, and your answer should include an analysis of whether the national rule gives rise to a restriction. You should consider any relevant grounds for justification, as well as the proportionality principle if you consider it relevant. (25)

PART B

You are required to answer ONE question from this Part.

3.

1) Mrs Jones is tax resident in Dreamland and receives income from dividends from Napland. Both Dreamland and Napland are EU member states. Under the Dreamland-Napland double tax agreement (DTA), any economic double taxation that arises from the resulting taxation of dividends will be relieved by way of credit in Dreamland for the tax paid in Napland. In contrast, for domestic investments (intra-Dreamland), economic double taxation is relieved by way of exemption.

   The statutory tax rate in Napland is 25%, while in Dreamland it is 40%. In order for Dreamland to offer a credit for the tax paid paid in Napland, Mrs Jones needs to provide a declaration showing the applicable effective corporate tax rate in Napland. Mrs Jones claims that this imposes an excessive burden on her.

   You are required to assess whether the applicable method of relief by Dreamland (the imputation method) is compatible with EU law. Would your answer change if Dreamland had DTAs in place with other member states, with provisions that incoming dividends from those member states are exempt from tax in Dreamland? (10)

2) The tax authority of Dreamland has since been notified that Mrs Jones is the owner of several bank accounts in Snoozeland, another EU member state. Mrs Jones has never included any income from Snoozeland in her tax returns. Dreamland has therefore requested Snoozeland to provide information regarding Mrs Jones' accounts with MO Bank and ER Bank, specifically:

   - bank statements for the past three years;
   - the beneficial owners of the accounts; and
   - statements detailing any financial assets of which Mrs Jones appears to be the beneficial owner.

   MO Bank and ER Bank have provided this information to the Snoozeland tax authority, which in turn has shared the information with the Dreamland tax authority. Upon receipt and assessment of the information, the Dreamland tax authority has imposed a penalty on Mrs Jones for failure to disclose part of her income in her tax returns for the past three years.

   Mrs Jones complains that the fine should be cancelled as she was not given the right to be heard and contest this information at any stage in proceedings in either of the two states (the information collection in Snoozeland and the assessment in Dreamland).

   You are required to explain whether the fine is contrary to EU law. (10)

Total (20)

4. The government of Member State A is considering the introduction of a new sector specific corporate income tax, to be based on turnover and calculated according to a steeply progressive scale of rates within various tax bands. The government believes that such a tax is justified as it is to be imposed on taxpayers whose ability to contribute to the costs of public expenditure exceeds the general obligation to pay tax.

Regarding the scope of the tax, the draft law contains two alternatives:

1) To impose the tax on the turnover of the undertaking concerned; or

2) In case of undertakings that are members of multinational groups, to impose the tax on the consolidated turnover of the linked undertakings, as this would imply a higher ability to pay.

The government has not yet decided which of the two options to follow.

You are required to advise the government of Member State A, with reference to the Treaty on the Functioning of the European Union and the case law of the Court of Justice of the European Union, whether such legislation is compatible with the fundamental freedoms.

You should identify which freedom applies, and your answer should include an analysis of whether the national rule can potentially give rise to discrimination. (20)

PART C

You are required to answer TWO questions from this Part.

5. A Spanish company, DUPLA SA, has held 100% of the capital of a Luxembourg company, STRESS SA, since 1 January 2019. STRESS SA paid a dividend to DUPLA SA on 1 February 2019 from profits that had been earned in 2018, before its acquisition by DUPLA SA.

You are required to answer the questions below.

1) Which obligations, if any, does the Parent-Subsidiary Directive (PSD) impose on the member states involved, concerning the dividend payment at issue? Would your answer change if STRESS SA was constituted as an Undertaking for Collective Investment in the form of a Société d'Investissement à Capital Variable (SICAV), exempt from corporate income tax? (6)

2) Assume that DUPLA SA holds its shares in STRESS SA via a permanent establishment (PE) located in Italy. The Italian tax authority seeks to fully tax the dividends from STRESS SA that are attributable to DUPLA SA's Italian PE. Explain whether Italy is permitted to do so, according to the PSD. (3)

3) The Italian tax authority has since imposed a withholding tax labelled as 'equivalence levy' on any payment made from DUPLA SA's PE in Italy to DUPLA SA's head office in Spain. The levy is justified by Italy on the basis that a withholding tax would be imposed on dividends paid to the Spanish parent if the PE were a subsidiary, as Spain exempts such dividends.

Explain whether both the Italian equivalence levy and withholding tax on subsidiaries comply with the PSD. (3)

4) The Spanish tax authority exempts 100% of the dividends when they are received by DUPLA SA. However, when DUPLA SA subsequently distributes income to a foreign shareholder, it is subject to a 5% 'solidarity levy'. The tax base for this levy is the amount of the dividend paid to shareholders.

Explain whether such a 'solidarity levy' is in compliance with the PSD. (3)

Total (15)

6. **You are required to explain whether the implementation of the Anti-Tax Avoidance Directive in the EU has resulted in a level playing field in relation to tax avoidance.** (15)

7. **You are required to discuss, with reference to the case law of the Court of Justice of the European Union, the concept of 'balanced allocation of taxing rights' as justification for restrictive tax measures.** (15)

8. **You are required to discuss the arguments that support the proposition that the Anti-Tax Avoidance Directive's exit tax rule is contrary to EU law.** (15)