

**“Are the existing mechanisms and instruments available to the institutions of the EU sufficient to achieve effective harmonisation of Member States’ direct tax regimes?”**

**A thesis submitted for the degree of Master in Letters (M.Litt.)**

**September 2017**

**Jeremy N F Norman, MA, LL.M, ADIT, Solicitor**

**School of Law**

**University of Dublin, Trinity College**

**DECLARATION**

*I declare that this thesis has not been submitted as an exercise for a degree at this or any other university and it is entirely my own work.*

*I agree to deposit this thesis in the University's open access institutional repository or allow the Library to do so on my behalf, subject to Irish Copyright Legislation and Trinity College Library conditions of use and acknowledgment.*

*Signed by Jeremy N F Norman.....*

*Date.....*

# SUMMARY

This thesis addresses the question of whether the existing mechanisms and instruments available to the institutions of the EU are sufficient to achieve the effective harmonisation of Member States' direct tax regimes.

In addressing this question I have examined a number of distinct areas.

## **Competence in direct tax matters**

As the treaties do not confer competence in matters of direct tax on the EU, either on an exclusive or a shared basis, it follows that, in principle, Member States are free to frame their direct tax rules as they see fit.

## **EU policy on direct taxes**

The desirability of a convergence or harmonisation of Member States' direct tax systems has been recognised since the earliest days of the Community. I consider a wide range of material to illustrate the evolution of the Commission's thinking in this area and its aims and goals. Despite changes in the terminology used, evidence suggests that harmonisation is still very much the Commission's goal.

## **'Hard' law**

With the exception of the Anti-Tax Avoidance Directive, the directives implemented on direct tax matters thus far deal with specific and relatively uncontroversial matters. The Commission's current 'flagship' proposal on direct taxes is the draft Common Consolidated Corporate Tax Base Directive ('CCCTB'), which if implemented would represent a major piece of 'positive' integration and a substantial step towards tax harmonisation.

## **'Soft' law**

Though there has been much soft law on direct tax matters, the most important of which has been the Code of Conduct on Business Taxation, its non-binding nature means that compliance on the part of Member States is effectively voluntary.

## **The case law of the Court of Justice**

In the mid-1980s the Court established the principle that Member States had to exercise their competence in direct tax matters consistently with EU law, and in particular with the four fundamental Treaty freedoms and the principle of non-discrimination. I examine the evolution of the Court's jurisprudence in direct tax matters, its methodology, its self-imposed limitations on its competence and the range of 'unwritten' justifications it has developed in addition to the derogations expressly set out in the Treaty.

## **Article 116**

The EU's ability to legislate on direct tax matters has been severely handicapped by its use of Article 115 of the Treaty as the legal basis for such legislation, as this requires Member State unanimity. There seems to be no legal reason why Article 116, which requires only qualified majority voting, should not be used as an alternative basis for direct tax legislation where the measures address to a significant extent distortions in the conditions of competition. The reason the use of Article 116 has not been seriously considered by the Commission thus far is likely be more political than a matter of legal principle.

## **EU law and anti-tax avoidance**

Various soft law initiatives in this area have been launched by the Commission over the years. Matters took concrete form with the implementation of an Anti-Tax Avoidance Directive in 2016 as part of the EU's response to the G20/OECD Base Erosion and Profit Shifting ('BEPS') project. This directive is more wide-ranging than previous direct tax directives and in part represents positive as opposed to negative integration.

## **State aid**

The Commission's use of its State aid powers to challenge tax-favoured schemes available to, or in practice only utilised by, a limited group of taxpayers have been relatively uncontroversial. Its use of these powers in the last three years to challenge Member States' tax policies and administrative procedures in relation to a number of household name multinationals, on the other hand, has been extremely controversial. Ireland has lodged an appeal against the Commission's ruling in the Apple case, though this is unlikely to be heard for some considerable time.

## **EU VAT system as a model?**

The EU VAT system was introduced in the form of directives, which Member States were left to implement with a considerable discretion as to tax rates and exemptions, etc. I consider whether in the light of the experience with the VAT system it would be a good model to follow if an EU-wide direct tax system were to be introduced.

## **Conclusions**

The Court's case law and the application by the Commission of the State aid provisions has made some significant contribution towards tax harmonisation but it has necessarily been piecemeal, uncoordinated and 'negative' in nature. Soft law, being non-binding, is of only limited value.

In my opinion the obstacles to the functioning of the internal market and distortions to the conditions of competition that result from the existence of 28 uncoordinated national tax systems can only be substantially eliminated through the introduction of a comprehensive EU-wide common tax system. Such a system would involve a common tax base (to eliminate tax base competition) and a limitation on the range of permissible tax rates (to ensure that tax rate competition was kept within reasonable boundaries). Whilst Member States might be allowed some latitude in the tax base, too much latitude can result in serious distortions as has been the case under the VAT regime. The CCCTB incorporates the principle of a common tax base, but it is apparent that its proposed consolidation of profits and their formulary apportionment between Member States is too much of a leap for most Member States at the present time.

If it continues to be impossible to obtain the unanimity needed to pass legislation under Article 115, serious consideration should be given to using Article 116 as an alternative basis.

# CONTENTS

## ABBREVIATIONS

Chapter 1	INTRODUCTION	1
Chapter 2	SCOPE AND OVERVIEW	4
Chapter 3	COMPETENCE AND DIRECT TAXES	11
Chapter 4	THE EU'S POLICY ON DIRECT TAX HARMONISATION AND SOURCES OF EU LAW	
	- EU policy on tax harmonisation	17
	- 'Hard' law	36
	- 'Soft' law	54
	- The Court's case law	61
Chapter 5	AN ALTERNATIVE TO THE NEED FOR UNANIMITY – ARTICLE 116?	113
Chapter 6	EU LAW AND ANTI-TAX AVOIDANCE	118
Chapter 7	STATE AID AND DIRECT TAXES	130
Chapter 8	THE EU VAT REGIME – A MODEL OR A WARNING?	143
Chapter 9	CONCLUSIONS	152
	BIBLIOGRAPHY	177

## ABBREVIATIONS

AG	Advocate General
BEPS	Base Erosion and Profit Shifting
CCCTB	Common Consolidated Corporate Tax Base
CJEU	Court of Justice of the European Union, consisting of the Court of Justice and the European General Court (formerly the Court of First Instance)
Commission	European Commission
Council	Council of the European Union (commonly referred to as the Council of Ministers)
Court/ECJ	Court of Justice (informally referred to as the European Court of Justice)
EC	European Community
ECOFIN Council	Economic and Financial Affairs Council
EEA	European Economic Area
EEC	European Economic Community
EGC	European General Court (formerly the Court of First Instance)
EU/Union	European Union
G20	Group of Twenty
IBFD	International Bureau of Fiscal Documentation
OECD	Organisation for Economic Co-operation and Development
TEU	Treaty on European Union (concluded in Maastricht in 1992) as amended by the Treaty on the European Union (concluded in Amsterdam in 1997) and

the Treaty Amending the Treaty on European Union and the Treaty Establishing the European Union (signed at Lisbon in 2007).

Treaty/TFEU

Treaty on the Functioning of the European Union, being the Treaty Establishing the European Community (concluded in Rome in 1957) as amended by the Treaty on the European Union (concluded in Maastricht in 1992), the Treaty on the European Union (concluded in Amsterdam in 1997) and the Treaty Amending the Treaty on European Union and the Treaty Establishing the European Union (signed at Lisbon in 2007). The name of the 1957 Rome Treaty was changed by the 1992 Maastricht Treaty to the Treaty Establishing the European Community and by the 2007 Lisbon Treaty to the Treaty for the Functioning of the European Union.

VAT

Value Added Tax (and its equivalents)

## **Note**

Unless otherwise stated, references to Articles are to Articles of the TFEU as amended.





## Chapter 1

# INTRODUCTION

In marked contrast to indirect taxes such as value added tax, direct taxes such as income tax, corporation tax and capital gains tax do not lie within the exclusive legislative competence of the EU. The reasons for this are explained in chapter 3. In the absence of EU competence, Member States are in principle free to operate their direct tax systems as they see fit, albeit this freedom is subject to a number of important caveats which are examined in the body of this work.

The principle that Member States have legislative competence over their direct tax systems has resulted in a number of features that the Commission finds objectionable on the grounds that they represent impediments to the operation of the single market and the exercise of the four fundamental treaty freedoms. Again, these are examined in the body of this work.

Since almost the earliest days of the Community there has been an ongoing debate as to whether a Community-wide harmonisation of direct taxes was (a) desirable, and (b) practicable. This debate proceeded at a more or less leisurely pace until the global financial crisis around 2008 added a whole new urgency and impetus and put taxation in the forefront of media scrutiny and public debate in an unprecedented way.

Following the 2008 crash governments wanted two things. Firstly, scapegoats. Secondly, people or organisations with deep pockets that they could tax to help bail them out of debt. Multinationals were quickly identified as suitable candidates on both counts. Their financial affairs were put under the microscope and revelations soon emerged about their tax planning practices. Although these were common at the time and had been for many years, governments professed to be scandalised and the cry went up, "Something must be done!"

Tax, and in particular tax planning (or avoidance as all forms of it were indiscriminately rebranded by the media and politicians) became front page news and entered the public consciousness in an unprecedented way. This continues to be the case.

A direct result of the political and public outcry on multinational tax avoidance was the G20/OECD project on Base Erosion and Profit Shifting ('BEPS'), which represents the biggest shake up in the international tax system for a century and aims at nothing less than the elimination of artificial cross-border tax avoidance.

The EU's response to the tax avoidance debate forms an important part of this work, but it is only one element of a much larger whole.

A parallel debate that has been generating almost as much heat has been the relationship of the Member States with the EU and whether continuing integration is either necessary or desirable. The UK's recent Brexit decision does not seem to have curbed the Commission's ambitions; if anything it seems to have had the opposite effect.

Tax is an important element of the integration debate. Most Member States see continuing sovereignty over tax matters as highly symbolic, though it is probably vested with more significance than in reality it merits.

The Commission's position, and it makes no secret of it, is that continued integration is the only way to go. As far as the Commission is concerned the only questions for negotiation are how quickly that integration should take place and through what mechanisms should it be achieved.

Owing to this combination of events, the inter-relationship between Member States' tax systems and the EU has never been more topical or intriguing.

For the reasons detailed in this work, the Commission's view is that moves toward a harmonisation of Member States' direct tax systems would not only eliminate impediments to the operation of the single market and exercise of the fundamental treaty freedoms but also many of the results of 28 competing tax regimes that could be branded unfair or conducive to tax avoidance. The material set

out in this work makes it clear that, at least in the long-term, the Commission would like to see a substantial degree of harmonisation in the field of direct taxes. The central question addressed in this work is whether the various institutions of the EU, between them, already have the tools at their disposal to achieve an effective harmonisation of Member States' direct tax regimes, or whether a radical 'X-factor' is needed to further the task.

Material is current as of 31 August 2017.

## Chapter 2

# SCOPE AND OVERVIEW

### 2.1 Introduction

This chapter is intended as a brief introduction to the principal matters that will be addressed in detail in the subsequent chapters of this work.

It is appropriate at the outset to frame working definitions of the expressions 'harmonisation' and 'direct' (as opposed to 'indirect') taxes as these recur throughout.

'Harmonisation' can be taken as meaning the elimination of differences, which in the tax context would involve the equalisation, or at least the substantial convergence, of tax rates and tax bases (ie, the way in which the amount on which tax is charged is computed). Harmonisation has a different meaning to 'coordination', which in the tax context would involve governments reaching agreements over specific aspects of taxation or of their respective tax systems, such as agreements to reduce or remove special regimes that exempt or apply reduced tax rates to certain activities.

'Direct' taxes are essentially those that are imposed on a particular person (eg, income tax, corporation tax, capital gains tax), as opposed to 'indirect' taxes that are paid on transactions by a person or entity in a supply chain and passed on to the final consumer as part of the price of goods or services (eg, Value Added Tax).

### 2.2 Competence

It is fundamental to all that follows to establish whether direct tax matters fall to be dealt with at EU or at Member State level.

As a starting point I will consider the extent to which the treaties give the EU competence to legislate in the field of direct taxes. The basic principle is that the EU is only competent to legislate in areas

where the treaties confer that competence (either on an exclusive or shared basis)<sup>1</sup>. Competence to legislate on indirect tax matters is conferred on the EU by Article 113 TFEU. There is no corresponding conferral of competence regarding direct taxes. Thus, in principle, Member States are free to legislate on direct tax matters as they see fit.

This freedom is, however, subject to significant limitations as a result of the development by the Court of the principle that Member States' must exercise their competence in direct tax matters in a manner consistent with the fundamental freedoms and principle of non-discrimination set out in the Treaty. The first major case in which this principle was applied was the 1986 decision in *Avoir Fiscal*<sup>2</sup>. Prior to this, the general understanding had been that as far as direct taxes were concerned Treaty provisions were simply not engaged. Since *Avoir Fiscal* there have been many cases in which the Court has applied the fundamental freedoms (mainly freedom of establishment) and principle of non-discrimination in direct tax matters. This has been described as 'tax harmonisation through the back door', particularly by those who believe that the Court is not content to act as a mere interpreter of the treaties but that it actively promotes an integrationist agenda at every opportunity. A major part of this work will be devoted to analysing the themes and principles that emerge from these cases, the ever more imaginative way in which the Court has applied them, and how much further the Court might be able to develop them in future. Although, in my view, the Court can go considerably further than it has hitherto in applying the fundamental freedoms to strike down Member States' direct tax provisions, it must be recognised that the Court can only go so far. The two primary reasons for this are firstly, that the fundamental freedoms can only be engaged where the tax provision concerned is discriminatory or restrictive. Where the Member State applies the same rule regardless of the nationality or residence of the taxpayer it is, generally, not susceptible to challenge on fundamental freedom or discrimination grounds. Differences between Member States' tax systems are not *per se* incompatible with EU law. Secondly, the Court can only

---

<sup>1</sup> Consolidated Version of the Treaty on European Union [2008] OJ C115/13, Article 4.1.

<sup>2</sup> Case 270/83 *Commission of the European Communities v French Republic* [1986] ECR 00273 (commonly referred to as the *Avoir Fiscal* case).

judge the cases that come before it, whether these originate in references from Member States' national courts or as a result of infringement proceedings brought against Member States by the Commission. Even if harmonisation is on the Court's agenda, the Court can only take the process so far and then only on a haphazard and piecemeal basis as cases come before it. The Court's striking down of particular national tax measures has the character of 'negative' integration, as opposed to 'positive' integration such as the introduction of a legislative measure that would apply in a uniform way across the EU.

### **2.3 EU direct tax policy**

Since the early 1960s a number of reports have been produced under EU auspices considering the merits of and potential for direct tax harmonisation. They are valuable sources of material setting out why direct tax harmonisation is seen as desirable from the EU's perspective and the specific Treaty aims and objectives that such harmonisation would facilitate.

### **2.4 'Soft' law**

An important source of material produced by the Commission concerning direct taxes is 'soft' law. This has been voluminous and has taken many forms, including recommendations, resolutions, communications, notices and codes of conduct. All share the characteristic that they are non-binding on Member States, but are useful indicators as to the goals that Commission aspires to and the sorts of measures it might like to adopt were it able to do so.

### **2.5 'Hard' law**

Apart from the Court's rulings, the other primary source of EU 'hard' law on direct taxes is legislation in the form of the treaties themselves, directives, regulations or decisions. As noted previously, the treaties do not confer competence over direct tax matters on the EU. Nevertheless, a number of directives have been passed using the general provisions for the approximation of laws contained in Chapter 3 of Title VII of the Treaty. In the absence of a specific legal basis for direct tax legislation, all of these directives were introduced through the mechanism of Article 115 (approximation of laws

affecting the establishment or functioning of the internal market). Measures passed under Article 115 are subject to a 'special legislative procedure' requiring Member State unanimity, and it is no coincidence that the directives passed thus far have been relatively uncontroversial. A salutary example of the difficulties the Commission is liable to encounter where directives are proposed on more controversial matters was the debacle over the original Common Consolidated Corporate Tax Base ('CCCTB') Directive proposal, tabled in 2011 and which did not even gain sufficient support to be put to a vote by the Council. Note that whilst Article 114 (approximation of laws having as their object the establishment or functioning of the internal market) only requires the 'ordinary legislative procedure', ie, majority voting, it does not apply to fiscal provisions. The Commission has relaunched the CCCTB proposal in modified form and it is very much the 'flagship' proposal as far as direct tax harmonisation is concerned.

## **2.6 Article 116 as an alternative legal basis?**

Given the difficulties involved in obtaining Member State unanimity for all but the most uncontroversial measures, which the admission of new Member States has only exacerbated, and frustrated by the failure of its proposed CCCTB Directive, it would be no surprise if the Commission was at least thinking about possible alternative legislative bases. A move to majority voting for direct tax measures has been canvassed a number of times in the past but has consistently been rejected by Member States. The reason for this is not difficult to see. Control over its taxes has been seen as a key indicator of a nation's sovereignty and the notion of 'no taxation without representation' is a strong one which goes to the heart of democratic accountability. The difficulties the Commission would face if it sought to employ a legislative base for direct tax measures that required only majority voting should not be underestimated, and at least in the present political climate it seems highly unlikely to happen. But does an alternative legal basis already exist, and if yes could it – in principle and leaving political considerations aside - be used for the implementation of direct tax measures? I will examine the possibility that Article 116 could provide such a basis. This is a provision for the approximation of laws where the laws of a Member State distort the conditions of

competition in the internal market such that the distortion needs to be eliminated. A fundamental difference between Articles 115 and 116 is that the latter requires only qualified majority voting. At first blush it may appear that there is nothing in principle to preclude the use of Article 116 in the context of direct tax to eliminate distortions that affect competition. It is at least arguable that some of the differences in Member States' direct tax laws have the effect of distorting the conditions of competition, such that Article 116 becomes a valid alternative mechanism. For example, if Member State A has a corporation tax rate of 12.5% and Member State B has a rate of 25%, could this not be said to distort competition as between businesses based in the two States? The use of Article 116 is not a possibility that appears to have been considered thus far by the Commission, at least publicly, perhaps because a move to a majority voting mechanism for direct tax is simply not a politically practical possibility at the present time, but such comment as is available from academics appears to be mainly of the view that there is nothing in principle that would rule out Article 116 as an alternative legal basis for direct tax legislation.

## **2.7 EU and anti-tax avoidance**

I have already mentioned the principle that Member States' competence in the field of direct tax must be exercised in a manner consistent with EU law and in particular with the exercise of the fundamental freedoms if it is not to be susceptible to challenge before the Court. A related area in which the Court has been active is that of Member States' anti-tax avoidance provisions. Tackling tax avoidance, especially by multinationals, is extremely topical at present. Most countries are introducing targeted anti-avoidance measures (aimed at eliminating specific perceived abuses) and many are also introducing General Anti-Avoidance/Anti-Abuse Rules ('GAARs') that are not aimed at any specific abuse but are capable of being invoked by the tax authority where avoidance or an abuse is perceived which is not caught by any existing targeted anti-avoidance provision. In addition to this, the OECD, in conjunction with the G20, is currently in the process of carrying out its Base Erosion and Profit Shifting ('BEPS') project. This is a massive undertaking which aims at nothing less than the elimination of international tax avoidance. It has been described as the biggest reform of



global taxation in a lifetime. The OECD submitted its final reports and recommendations at the end of 2015 and these are currently in the process of being implemented. Many of the OECD's recommendations are to be incorporated into the bilateral double tax treaties of the countries participating in the project, including all of the EU's Member States<sup>3</sup>. The principle that Member States' tax rules should be consistent with the exercise of the fundamental freedoms if they are not to be susceptible to challenge by the Court applies equally to provisions contained in a Member State's bilateral double tax treaties. The principle has now been well established by the Court that Member States' anti-tax avoidance/anti-abuse rules should be directed only at 'wholly artificial arrangements' if they are to be considered justified and proportionate. Many of the measures likely to be introduced in their national tax systems by Member States as a result of BEPs are likely to target arrangements which whilst substantially artificial could not be described as wholly artificial. Commentators are already highlighting the potential for conflict between EU law and some of the anti-avoidance provisions being introduced by Member States in response to BEPS. The Commission's own response to the anti-avoidance debate, apart from its soft law pronouncements, has been the 2016 Anti-Tax Avoidance Directive<sup>4</sup>.

## **2.8 State aid**

Another limitation on the principle that direct taxes are solely a matter for Member States themselves is the application of the EU's State aid rules. These can apply where, for example, Member States apply tax-favoured regimes available only to a limited group of taxpayers, or which in practice are only used by a limited group of taxpayers. Since 2014 the State aid rules have been invoked by the Commission against a number of household name multinationals. This is a highly topical and evolving area.

---

<sup>3</sup> Although not all of the EU's Member States are members of the OECD, all the EU Member States are participating in the BEPs project.

<sup>4</sup> Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market [2016] OJ L193/1.

## **2.9 EU VAT regime as a possible model?**

I will consider whether the EU VAT regime would be a good model to follow if the EU were to have the power to legislate on direct tax matters or whether it should be seen as a warning of what can go wrong when too much discretion is left to the individual Member States.

## **2.10 Conclusions**

In the concluding chapter I consider where matters currently stand in the direct tax field, the extent to which measures already taken fall short of substantive harmonisation, whether the case made out by the Commission for further harmonisation is sufficiently compelling, whether legislative measures currently proposed by the Commission but not yet implemented (and in particular the CCCTB) are likely to achieve the degree of harmonisation required, and, if not what further measures are likely to be necessary.

I consider in particular whether the EU possesses the mechanisms and instruments necessary to achieve further harmonisation in the eventuality that the Member State unanimity required to implement hard law via the legal basis thus far adopted for such measures is not achieved and whether it may be necessary to consider a more radical approach to future legislation.

## COMPETENCE AND DIRECT TAXES

### 3.1 Principle of conferral

The EU is empowered to legislate only in those areas in which competence is conferred on it by the EU treaties. Competences not conferred on the EU remain with the Member States. This principle is set out in Article 4 of the TEU. Article 5 of the TEU provides that where the treaties do confer competence on the EU it must be governed by the principles of subsidiarity and proportionality.

Where competence is conferred on the EU this does not give it legislative *carte blanche*. Article 5.2 TEU provides that the EU can only act in the pursuance of objectives set out in the Treaty. Hence EU legislative proposals are always at pains to set out the specific Treaty objectives that the proposed legislation would further or promote.

### 3.2 Subsidiarity

Article 5.3 TEU provides that under the principle of subsidiarity, where the EU does not have exclusive competence it can act only in so far as the objectives of the proposed action cannot sufficiently be achieved by Member States but rather, by reason of the scale or effects of the proposed action, be better achieved at EU level. Article 5.4 TEU provides that under the principle of proportionality the content and form of EU action shall not exceed what is necessary to achieve the objectives of the Treaties. A Protocol<sup>5</sup> which was annexed to both the TEU and TFEU by the 2007 Lisbon Treaty, sets out the framework for the practical application of the principle of subsidiarity, a feature of which is that Member States' national parliaments may within eight weeks of the publication of draft legislation submit a reasoned opinion to the Commission stating why it does not consider that the proposed act complies with the principle of subsidiarity. Where one-third or more

---

<sup>5</sup> Protocol (No 2) on the application of the principles of subsidiarity and proportionality [2008] OJ C115/0206.

of national parliaments lodge such an opinion, the draft legislation must be reviewed. This process has come to be known as the 'yellow card' procedure.

### **3.3 Conferral of competence and direct tax**

Article 3(1) TFEU confers exclusive competence on the Union in matters of, *inter alia*:

- the customs union; and
- the establishment of competition rules necessary for the functioning of the internal market.

Whilst Article 3 TFEU confers exclusive competence on the Union in indirect tax matters (these being an inherent part of the rules relating to the customs union), it does not confer exclusive competence on the Union in respect of direct tax matters.

Article 4 provides that competence shall be shared between the Union and Member States in the areas listed in that Article. The areas in which competence is shared do not include direct tax.

Article 2.1 provides that where exclusive competence has been conferred upon the Union, only the Union may legislate.

Article 2.2 provides that in the case of a shared competence both the Union and Member States may exercise the competence, save that the Member States may exercise their competence only to the extent that the Union has not exercised its own.

Whilst the effect of the Treaties is to reserve competence in direct tax matters exclusively to the Member States, there is nothing to stop the Member States agreeing to legislation at EU level if they consider it desirable. The question then is which of the legal bases for legislation contained in the Treaty is the appropriate one.

The only Treaty Articles specifically relating to tax matters are Articles 110 to 113. However, these, including Article 113 under which provisions may be adopted for the harmonisation of national legislation, apply only to taxes of an indirect nature. The various EU legislative provisions on customs duties and VAT were adopted under Article 113.

### **3.4 Treaty bases for direct tax legislation**

Given the lack of a specific legal basis for legislation on direct taxes, the EU's direct tax legislation thus far has been passed under the general Treaty provisions for the approximation of laws set out in Chapter 3 of Title VII of the Treaty (Articles 114 to 118).

Article 114 requires only qualified majority voting under the ordinary legislative procedure, but is dis-applied by Article 114(2) in relation to fiscal provisions (which includes direct taxes).

Article 115 is the legal basis used thus far for the passage of legislation concerning direct taxes.

Article 115 provides for the issue of directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the establishment or functioning of the internal market. Crucially, Article 115 requires unanimity under the special legislative procedure.

It should also be noted that Article 115 only refers to directives, not regulations. This limitation on the choice of legislative instrument is probably not a significant factor as directly effective regulations would probably not be a practical proposition in direct tax matters given the complexity of the subject matter and the myriad interactions there can be with other areas of Member States' national tax codes. In matters of direct tax, directives are a much more practical and sensible way forward.

Article 116 provides for the issue of directives where the Commission finds that differences between Member States' laws or administrative procedures are distorting the conditions of competition in the internal market and that the distortions need to be eliminated. Directives under Article 116 may only be issued if after a process of consultation the Member State concerned has not eliminated the distortion in question. The attraction to the Commission of using Article 116 as a legal basis for the passing of directives on direct tax is that it requires only qualified majority voting under the ordinary legislative procedure. There has been no indication thus far, however, that the Commission has seriously considered using Article 116 to sidestep the impasse resulting from the requirement for unanimity under Article 115. Political considerations aside (though these should not be underestimated) there seems to be nothing in principle to prevent the use of Article 116 as the legal

basis for direct tax legislation in at least certain areas. I consider the possible use of Article 116 in a separate chapter.

Articles 117 and 118 are not relevant for present purposes.

Mention should be made in passing of Article 352. Article 113 in relation to indirect taxes provides for measures in relation to both the establishment and functioning of the internal market and distortions of competition. Articles 114 and 115 only provide for measures in relation to the establishment or functioning of the internal market, and Article 116 only provides for measures in relation to distortions of the conditions of competition in the internal market. Article 352 provides a legal basis for the adoption of measures to attain other (unspecified) Treaty objectives in cases where the Treaty has not provided the necessary powers. As Article 352 requires unanimity under the special legislative procedure it does not seem to offer any additional possibilities over Articles 115 and 116 other than that whereas the only form of legislation permitted under Articles 115 and 116 is directives, Article 352 only refers to 'measures', which could *inter alia* include regulations as well as directives.

It is difficult to envisage any EU direct tax legislative measure that would not have as its primary focus either the establishment and functioning of the internal market or the elimination of distortions of competition. In which case it is hard to see a role for Article 352 in the direct tax arena.

Article 289 provides for two alternative legislative procedures; the 'ordinary legislative procedure' as defined in Article 294, or a 'special legislative procedure'. If a special legislative procedure is required, this will be stipulated in the Article that is being used as the legal basis for the particular legislation, which will also specify the threshold required for the measure to be passed (usually unanimity, as in the case of Article 115).

The 'ordinary legislative procedure' is set out in Article 294. Article 294(13) provides that measures subject to the ordinary legislative procedure are passed by the Council on the basis of qualified majority voting.

### **3.5 Summary of conditions necessary for direct tax legislation**

For direct tax legislation to be passed, assuming Article 115 is used as the legal basis, the following three essential conditions would have to be satisfied.

1. Existing Member States' tax laws, or the lack of them, directly affect the establishment or functioning of the internal market (this is the Treaty objective that the legislation would further or promote).
2. Action by Member States would be insufficient to achieve the desired objective (compliance with the subsidiarity principle).
3. The proposed EU legislation does not exceed what is necessary to achieve the Treaty objective (the proportionality principle).

### **3.6 Enhanced cooperation procedure**

Mention should be made of the enhanced cooperation procedure set out in Article 20 of the TEU and Articles 326-334 of the TFEU. The enhanced cooperation procedure requires the participation of a minimum of nine Member States and is intended to be a measure of last resort, to be employed only where the Council has established that the objectives of such cooperation cannot be attained within a reasonable period by the Union as a whole.

No measures concerning direct tax have as yet been passed under the enhanced cooperation procedure.

### **3.7 State aid**

The application in direct tax matters of the Treaty provisions relating to State aid is considered in a separate chapter.

### **3.8 Competence of the Court**

The Court's competence in direct tax matters stems from landmark case law in the mid-1980s that established the principle that the competence of the Member States in the field of direct tax must be exercised consistently with Community Law, in particular the principle of non-discrimination and the rights provided under the four fundamental freedoms. The establishment of this principle and subsequent development of the Court's case law on direct taxes is considered in detail in Chapter 4. The scope and application of the fundamental freedoms are also covered in that chapter.



## THE EU'S POLICY ON DIRECT TAX HARMONISATION AND SOURCES OF EU LAW

### 4.1 EU's policy on direct tax harmonisation

That tax matters would have to be taken into account in framing the rules governing the European Economic Community was recognised in the 1957 EC Treaty. This included two specific provisions relating to tax. Firstly, it was recognised that the free movement of goods and to a lesser extent services could be severely hampered by allowing Member States to set tariffs for imported goods or services that disadvantaged goods or services being imported from other Member States. Article 95 of the original 1957 Treaty (now Article 110 of the TFEU) prohibited Member States from imposing, directly or indirectly, any internal taxation on the products of other Member States in excess of that imposed on similar domestic products. The internal taxes referred to are principally 'indirect' ones such as sales taxes, customs duties and VAT.

Secondly, Article 220 of the 1957 Treaty provided that, *inter alia*, 'Member States shall, as far as necessary, engage in negotiations with each other with a view to securing for the benefit of their nationals...the elimination of double taxation within the Community'. Article 220 became Article 293 of the EC Treaty but was repealed by the Lisbon Treaty, largely because it had no direct effect and in practice most if not all Member States had either provisions in their domestic legislation or under bilateral double tax treaties that dealt with the problem, making the exhortation in Article 293 redundant.

Neither of these two tax provisions contained in the original EC Treaty applied to direct taxes. It was, however, recognised early on that differences between Member States' direct tax systems were problematic and could affect the way the common market was supposed to function, for example by affecting investment decisions and impeding cross-border transactions.

The Commission's first major attempt to consider the matter was to set up a Financial and Fiscal Committee which reported in 1962<sup>6</sup> and was referred to as the Neumark Committee after its chairman Fritz Neumark, a German economist. Its mandate<sup>7</sup> was to study two questions:

1. if and in what measure the disparities in public finance currently existing between Member countries partly or even entirely hinder the establishment of the Common Market bringing into being and guaranteeing conditions analogous to those of an internal market; and
2. to what extent it is possible to remove the disparities which considerably impede the development and functioning of the Common Market.

The mandate acknowledged that indirect taxes would be the main focus of the Committee's work (in particular as these had been made a Community competence in the 1957 Treaty), but it expressly required the Committee to address direct taxes as well. The mandate stressed that the Committee should above all concern itself with the impact of tax differences on competition and the distortion of competition: it is noteworthy that at this very early stage the Commission had recognised that differences in Member States' tax systems could have a significant effect on competition as well as affecting the functioning of the internal market.

The Committee found (unsurprisingly) that there were wide differences between the tax systems of the six Member States, but that these resulted from differing social and historical conditions and the different characters of their people. The Committee advocated increasing co-operation between national tax authorities and a process of convergence which would lead to the introduction for companies engaged in business in more than one Member State of common rules for calculating the taxable base and a tax reporting and assessment requirement for such companies in only one Member State. The Committee also recommended that income from cross-border activities should

---

<sup>6</sup> IBFD, 'The EEC Reports on Tax Harmonization – The Report of the Fiscal and Financial Committee and the Reports of the Sub-Groups A, B and C', (IBFD 1963) ('Neumark Report') available online at: <http://www.steuerrrecht.jku.at/gwk/Dokumentation/Steuerpolitik/Gemeinschaftsdokumente/EN/Neumark.pdf> accessed 17 May 2018.

<sup>7</sup> *ibid*, Appendix A at page 161.

be shared between the Member States concerned. These recommendations anticipated many of the fundamental principles underlying the CCCTB by almost half a century.

As to a more complete harmonisation of tax systems, however, not only did the Committee find that the differences in tax systems were justified by the fact that individual States pursued different economic and social policies, but it concluded that any attempt to completely unify the structures of national tax systems was both undesirable and bound to fail. In any event, the Committee observed that ‘...complete unification of the tax systems of the Member States – even if it is held...that it is politically achievable – would not be considered as necessary from the aspect of integration policy, since experience proves that on many grounds *moderate* [my italics] differences limited to the nature and to the rate of taxes do not hinder the free play of competition<sup>8</sup>.

Five years on, in 1967, the Commission published a ‘Programme for tax harmonisation’<sup>9</sup>, which set out proposals for concrete action in a number of specific areas. The starting principle was that whilst tax systems should be as neutral as possible so as not to distort investment decisions or competition, harmonisation must be limited to what is really necessary either for the establishment of or for the smooth functioning of the Common Market. The document outlined the measures already taken and to be taken in future in connection with indirect taxes. As far as direct taxes are concerned, it should be borne in mind that at this point no legislation at Community level had yet been implemented. The document stated that ‘The proposed measures [in connection with direct taxes] are required by the gradual liberalisation of capital movements, the need for structural reorganisation and a higher degree of industrial combination, and the way competition is developing in the field of investment<sup>10</sup>. It is worth mentioning in passing the importance when considering any of the Commission’s pronouncements on taxes to identify the grounds the Commission gives as to why a degree of tax

---

<sup>8</sup> Neumark Report (n 6), P102 at para 6.

<sup>9</sup> Commission, ‘Memorandum to the Council of 8 February 1967 – Programme for the harmonization of direct taxes’, Bulletin of the European Economic Community, Supplement No 8 [1967] (‘1967 Memorandum’).

<sup>10</sup> *ibid*, p4, Direct taxes, para 1.

harmonisation is desirable or necessary, as in order to legislate the EU must link the legislation to a specific Treaty objective.

The following direct tax proposals were set out in the document:

- The elimination of withholding taxes on cross-border dividends and interest<sup>11</sup> (this was subsequently legislated for in the Parent-Subsidiary Directive<sup>12</sup> and the Interest and Royalties Directive<sup>13</sup>).
- To ensure that cross-border corporate restructurings and amalgamations are not made too costly or prevented by tax regulations<sup>14</sup> (this was subsequently legislated for in the Mergers Directive<sup>15</sup>).
- To spell out more clearly the obligation of Member States to consult the Commission in connection with corporate tax incentives that are likely to engender distortions of Competition<sup>16</sup> (covered by the application of the State aid provisions under Articles 107 & 108 TFEU).
- A uniform definition and method of calculation of taxable corporate profits (ie, the tax base) and alignment of the rates of corporation tax in the six countries<sup>17</sup> (neither of which proposals have yet been implemented).
- Co-ordination of the methods of control and collection of taxes, without which harmonisation would not have the required effect<sup>18</sup> (subsequently legislated for in the Mutual Assistance Directive<sup>19</sup>).

---

<sup>11</sup> *ibid*, p4, Direct taxes, section I (1).

<sup>12</sup> Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States [1990] OJ L225/6.

<sup>13</sup> Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States [2003] OJ L157/49.

<sup>14</sup> 1967 Memorandum (n 9), p4, Direct taxes, section II.

<sup>15</sup> Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States [1990] OJ L225/1.

<sup>16</sup> 1967 Memorandum (n 9), p4, Direct Taxes, section III (1).

<sup>17</sup> *ibid*, p5, Direct taxes, sections 2 & 3.

<sup>18</sup> *ibid*, p5, Direct taxes, section 4.

<sup>19</sup> Council Directive 77/799/EEC of 19 December 1977 on mutual assistance by Member States in the field of direct taxation and taxation of insurance premiums [1977] OJ L336/15.

Some of the directives referred to above have been replaced or recast subsequent to their introduction. Direct tax directives are covered in more detail in the section on hard law.

As noted above, all but one of the proposals set out in the 1967 document formed the basis of future directives. These were able to achieve the required Member State unanimity as they were relatively uncontroversial and did not smack too much of overt tax harmonisation. The proposal for a uniform calculation of the tax base and alignment of corporate tax rates, on the other hand, failed to achieve the necessary Member State support, though a proposal for a common corporate tax base is currently on the table as part of the revamped CCCTB proposal – this is examined below in the section on hard law.

The Commission raised the issue of tax rates again with a 1975 proposal for a directive<sup>20</sup> on harmonising corporate tax rates within a 45%-55% range<sup>21</sup> (which was typical of the average national corporate tax rates at the time – today average corporate tax rates are almost 30% lower). Ironically, the fact that the proposal dealt only with tax rates and did not advocate a convergence or harmonisation of the corporate tax base provoked criticism from both Member States in favour of harmonisation, which saw the proposal as not going far enough, and Member States which saw any form of harmonisation as a threat to their sovereignty over direct tax matters. The Commission's task of achieving unanimity for its legislative proposals in this area had not been eased by the addition of new Member States from the beginning of 1973. After a lengthy period of inconclusive to-ing and fro-ing the proposed directive was formally withdrawn in 1990<sup>22</sup>.

For understandable reasons the Commission's focus in the early years of the Community had been on putting in place a common scheme of VAT and customs duties to facilitate the physical movement of goods in and out of, and within, Community borders. A deadline of 31 December 1992 had been

---

<sup>20</sup> Commission, 'Proposal for a Council Directive concerning the harmonization of systems of company taxation and of withholding taxes on dividends' COM(75) 392 final, 23 July 1975, Bulletin of the European Communities, Supplement 10/75.

<sup>21</sup> *ibid*, Article 3(1).

<sup>22</sup> Commission, 'Communication from the Commission to the Council and to the European Parliament: Guidelines on company taxation' SEC(90) 601 final, p10, para 30.

set for the completion of the single market and as this approached the question of whether further measures needed to be taken on direct taxes attained new urgency and impetus.

Given the manifest failure of its previous proposals for harmonisation and the need to make progress, the Commission changed tack in 1990 with a Communication about policy in the area of business tax<sup>23</sup>. The preamble stated that:

The purpose of this communication is to set out the guidelines which the Commission plans to follow in the field of company taxation and the measure which it thinks should be taken at Community level to create a company tax environment tailored to the establishment and further development of the internal market<sup>24</sup>.

The Commission's summary of the issues and its position are then succinctly stated in the introduction, which is worth reproducing<sup>25</sup>:

According to conventional economic analysis, any form of company taxation is liable to bring about economic distortions (lack of neutrality) because it may give rise to decisions on the location, nature and financing of investment [which] would not have been taken in the absence of company taxation. Such distortions arise because company taxation introduces a bias into the relationship between an investment project's economic rate of return and the after-tax rate of return to the investor. It should be pointed out that in the Community context the extent of this tax bias on an investment project may vary between Member States depending on differences in the tax base, the rate of tax and, sometimes, the characteristics of the tax system.

From a theoretical viewpoint, the possibility could therefore be considered of harmonising national company tax systems at Community level so as to ensure complete tax neutrality.

---

<sup>23</sup> Commission, 'Communication of the Commission to the Council and to the European Parliament: Guidelines on company taxation', SEC(90) 601 final.

<sup>24</sup> *ibid*, p1, para 1.

<sup>25</sup> *ibid*, pp1-2, paras 3-6.

However, there are a number of considerations why the Community should hold back on the harmonisation of company tax systems in the Member States, particularly in view of the principle of subsidiarity. Member States should remain free to determine their tax arrangements, *except where these would lead to major distortions* [my italics]. A further analysis is necessary to check the possible existence and extent of such distortions, and particularly those which might affect decisions as to the location of investment<sup>26</sup>.

Quite apart from the differences in the tax burden on companies, there are many other factors determining the decisions of direct investors. These include, for example, the need to locate a project close to the market served, differences in labour costs, the quality of public services and economic infrastructures.

*In view of these factors, the Commission has reached the conclusion that Community action should concentrate on the measures essential for completing the internal market. The important question of the advisability and possible forms of the harmonisation of company taxation should be re-examined closely and on new bases before any proposals can be presented* [my italics].

In short, the Commission had decided to park the direct harmonisation issue for now in favour of the more pressing matter of the completion of the single market, but clearly it had not abandoned it altogether.

The Commission went on to note that the removal of physical and technical barriers to free movement that would accompany the completion of the single market could bring about a spontaneous alignment by Member States of their tax systems as a result of competitive pressure, such that action at Community level might prove unnecessary. Concern was expressed, however, that market forces alone might not be sufficient to bring about the degree of alignment desirable to

---

<sup>26</sup> Such analysis was a primary task of the subsequently founded Code of Conduct Group's work on 'harmful tax competition'.

meet the needs of an integrated market and, in particular, that some Member States might attempt to outbid each other in cutting company taxes, leading to a 'race to the bottom'. Experience in the years that followed has demonstrated that these fears were all too justified.

The Commission proposed that a fresh study be carried out by a committee of independent experts<sup>27</sup>, the mandate of which<sup>28</sup> would be to answer the following main questions.

1. Do the disparities which exist between corporation taxes and the tax burdens on companies from one Member State to the next induce distortions in investment decisions affecting the functioning of the internal market?
2. If so, can those distortions be eliminated simply through the interplay of market forces and competition between national tax systems or are Community measures required?
3. Should any action at Community level concentrate on one or more elements of company taxation, namely the different corporation tax systems, the differences in tax treatment associated with the legal status of companies, the tax base or rates?
4. Should any measures envisaged lead to harmonisation, approximation or the straightforward establishment of a framework for national taxation? What would be the effect of such measures or the absence of such measures on Community objectives such as cohesion, environmental protection and fair treatment of small and medium sized firms?

The Commission stated that in light of this study it would decide what proposals for measures it should present to the Council. The committee would be given a maximum of one year to submit its report. The committee that was set up was known as the Ruding Committee, after its chairman Onno Ruding, a former Dutch finance minister.

---

<sup>27</sup> Commission, 'Communication from the Commission to the Council and to the European Parliament: Guidelines on company taxation' SEC(90) 601 final, pp11-12, paras 34-35.

<sup>28</sup> *ibid*, p12, para 35.



It might be mentioned in passing that the Commission's evidently new approach was favourably received by Member States<sup>29</sup>, which saw it as more respectful of their sovereignty in direct tax matters, a fact which is likely to have facilitated the passing at around this time of some of the directives that had their genesis in the Commission's 1967 'Programme for tax harmonisation', referred to above, and also the introduction of an inter-governmental Convention on transfer pricing adjustments between associated enterprises in different Member States<sup>30</sup>.

As the Neumark Committee had done 30 years earlier, the Ruding Committee<sup>31</sup> found that differences between national tax systems produced distortions in the functioning of the single market. Its key conclusions and recommendations<sup>32</sup> were that:

- Market forces will not be able to iron out differences in national tax systems. Community action is necessary.
- Member States' tax provisions that cause distortions or discrimination should be eliminated.
- Community action does not mean uniformity. The Community should set a minimum Community-wide 'floor' for the tax base and rates but Member States would be free to impose higher taxes than the minimum prescribed by the 'floor'.
- Double taxation on cross-border income flows should be eliminated.
- Fiscal competition between Member States should be curbed.

---

<sup>29</sup> Eg, Claudio Radaelli, *The Politics of Corporate Taxation in the European Union* (Routledge 1997) at p89 writes '...the business community reacted with extremely positive comments to the 1990 policy change and multinational companies seem to have much appreciated (and supported with their lobbying) the initiatives of the Commission.'; and at p92 'Framing of the policy problems in terms of harmonisation correlated with a decision style based upon confrontation, whereas a tax discourse in terms of subsidiarity, neutrality and mutual recognition aided negotiation'.

<sup>30</sup> Convention 90/436/EEC of 23 July 1990 on the elimination of double taxation in connection with the adjustment of profits of associated enterprises [1990] OJ L225/10 ('Arbitration Convention').

<sup>31</sup> Commission, 'Report of the Committee of Independent Experts on Company Taxation', Official Publications of the EC, ISBN 92-826-4277-1, March 1992 ('Ruding Committee Report')

<sup>32</sup> *ibid*, Policy recommendations at pp201-219.

- There should be full transparency as regards all tax reliefs granted by Member States to attract investment, for example, there should be no special deals done behind closed doors between a national tax authority and prospective investors.

One matter the Ruding Committee did not comment on was the unanimity voting rule in tax matters, and although this was not strictly within the Committee's mandate it was seen by many commentators as an unjustified omission. Indeed at least one of the Committee's members privately expressed the view that the rule should be abolished<sup>33</sup>.

On the initiative of Christiane Scrivener, Commission Member with special responsibility for taxation, the Commission gave its initial responses to the Ruding Committee report in June 1992<sup>34</sup>, the general tenor of which was that the Commission would follow a less ambitious line than the Ruding Committee had recommended and that action in the immediate term would be confined to four areas:

- cross-border dividend payments;
- international asset transfers;
- capitalisation rules; and
- bilateral tax treaties with non-EU countries.

An accompanying press release<sup>35</sup> stated that 'In Mrs Scrivener's view, it is important not to be carried away by a drive for harmonization which is not justified on economic grounds and which would not be consistent with the principle of subsidiarity and the respective responsibilities of the Member States and the Community'.

---

<sup>33</sup> Franz Vanistendael, 'The Ruding Committee Report: a Personal View', *Fiscal Studies* Vol 13, No 2, May 1992, pp85—95. Vanistendael states (p93, section 3, para 1) that 'The report does not contain a recommendation with respect to the abolition of the unanimous voting rule on tax matters. This is, in my view, an unjustified omission. The argument for not mentioning this in the report is, of course, that it exceeds the Committee's mandate, but it is now quite clear that Member States will have to relinquish some...of their taxing power on companies if they want to avoid major distortions due to unbridled tax competition in the internal market'.

<sup>34</sup> Commission, 'Commission Communication to the Council and to Parliament subsequent to the conclusions of the Ruding Committee indicating guidelines on company taxation linked to the further development of the internal market' SEC(92) 1118 final.

<sup>35</sup> Commission, Press Release P-92-38, 26 June 1992.

This cautious approach was likely influenced by the hostility with which the recently promulgated Maastricht Treaty had been greeted in some Member States and the rejection of the Maastricht Treaty in a 1992 Danish referendum.

Adding to the Commission's difficulties in pushing through legislation on direct tax matters was the fact that the principles of subsidiarity and proportionality were given legal force in the Maastricht Treaty<sup>36</sup>. Although subsidiarity had been mentioned in the 1957 Treaty of Rome, it had not been regarded as having any legal status<sup>37</sup>. Post-Maastricht, EU action would be subject to this additional legal constraint. It should also be borne in mind that around this time the Court was ruling against Member States' tax systems for breaches of the fundamental freedoms, making Member States nervous about what appeared to be a steady erosion of their national tax sovereignty. All of which made the Commission's task more difficult.

The next significant step was the publication by the Commission in 1996<sup>38</sup> of a discussion paper for an informal meeting of ECOFIN ministers. It emphasised that in the past tax had too often been discussed in isolation rather than in the wider context of EU policies. The main challenges set out in the paper were as follows.

1. The stabilisation of Member States' tax revenues. Here the Commission had in mind the effects of 'unfair' tax competition, which eroded a Member State's tax revenues by its taxable base (particularly capital) being relocated to other countries which offered a lower effective tax burden. This point was especially significant post-Maastricht given that Member States were now required to meet requirements on fiscal discipline.
2. The negative effect of tax competition on the smooth functioning of the internal market.

---

<sup>36</sup> Consolidated Version of the Treaty on European Union [2008] OJ C115/13, Article 5.

<sup>37</sup> This was confirmed by the Court of First Instance in Case T-29/92 *Vereniging van Samenwerkende Prijsregelende Organisaties in de Bouwnijverheid and others v Commission of the European Communities* [1995] ECR II-00289.

<sup>38</sup> Commission, 'Tax policy of the European Union', SEC(96) 487 final.

3. That as a result of the ease with which capital can be relocated, the share of Member States' tax revenues derived from workers, who are generally less mobile than capital, is increasing.

The Commission also observed that the advent of Economic and Monetary Union ('EMU') would make the need for the elimination of tax distortions all the more urgent, and that it made little sense to on the one hand eliminate distortions due to exchange rate fluctuations (which would be a result of EMU) but on the other hand to do nothing about distortions due to tax mismatches.

The Commission then set out the reasons why co-ordinated action on tax was required<sup>39</sup>.

There is a clear contrast between the need for progress in tax co-ordination and the decisions adopted so far in this area, which has been substantially lagging relative to many other areas of European integration. Tax co-ordination at the EU level has suffered from two main obstacles: the decision making rules and the lack of an overall perspective showing the economic and social downside of failing to reach decisions.

The requirement of unanimity in the Council for all tax decisions is obviously a strict one. The sheer number of significant Commission proposals in the taxation domain presently on the Council's table (18) and the number of proposals withdrawn by the Commission (30) in the same field are clear evidence of this.

Even if the unanimity requirement were to be maintained, more progress might still be made if greater consideration were given – in the presentation of Commission proposals – to the wide-ranging consequences of failure to adopt the various proposals. The costs of accepting certain proposals are often clear to Member States, while the costs of rejecting them are less so.

Yet, as indicated above, repeated failure to achieve progress in tax co-ordination has substantially contributed not only to maintaining distortions in the single market, but also –

---

<sup>39</sup> *ibid*, section IV (pp 10-11).

less visibly – to generating unemployment and even to creating opportunities for tax base erosion. *The apparent defence of national fiscal sovereignty has gradually brought a real loss of fiscal sovereignty by each Member State in favour of the markets, through tax erosion, especially on the more mobile tax bases* [my italics]. In order to counteract this phenomenon each Member State has to some extent been driven to overcharge labour.

A different approach would have consisted of better co-ordination among Member States in the areas of taxation. A deliberate and limited pooling of fiscal sovereignty by individual Member States to their collective decision-making would have avoided an unconscious surrender of sovereignty by each of them to market forces, in a field that should remain the prerogative of public policy.

The 1996 paper concluded that no Member State alone can remove the tax obstacles and the causes of tax degradation. Inactivity, it claims, is not a valid option and the Commission intends to examine, whilst fully respecting the subsidiarity principle, solutions for those problems where the Member States cannot by acting individually resolve them.

What emerges strikingly from this document is that the 'h'[armonisation] word has been almost entirely replaced with 'co-ordination'; in fact the only references to harmonisation in the document are that a degree of harmonisation will be proposed only where necessary and that there is no issue of harmonisation *per se*. Also striking is the Commission's seeming identification of the real villains of the piece as the markets, not the Member States who have merely been unwitting dupes. Leaving aside the real truth of the assertion, the Commission's stark message to the Member States that the real threat to their revenues is not to be found in tax co-ordination/harmonisation but in tax competition, which thrives in the absence of harmonisation, appears to have struck a chord.

The results of the Commission's deliberations following the discussion document were published in 1997<sup>40</sup>. The proposed package inevitably bore the signs of compromise, and it was expressly stated that whilst some Member States were in favour of a more ambitious package other Member States wanted more limited measures. Nevertheless, the Commission was optimistic that all of the Member States would agree to the package set out. The package contained three components:

- a code of conduct for business taxation (this is examined in the section on 'soft' law);
- measures to eliminate distortions to the taxation of capital income (this was the subject of the Savings Directive<sup>41</sup> and is examined further in the section on 'hard' law); and
- measures to eliminate withholding taxes on cross-border interest and royalty payments between companies (this was the subject of the Interest and Royalties Directive of 2003<sup>42</sup> and is examined further in the section on 'hard' law).

The fact that all three elements of the package were duly implemented suggests that the Commission had at last struck a balance between what was theoretically desirable and what was politically and practically possible.

Since then the Commission has issued a number of Communications on direct taxation matters, mostly addressing a particular issue or area and sometimes providing guidance for Member States on the implications of particular Court decisions. A Communication was released in 2006 on the more general subject of tax co-ordination<sup>43</sup>. Whilst this largely reprised the arguments previously made as to why tax co-ordination was desirable, it is noteworthy as being the first unveiling of the Commission's proposal for what it believed would be a systematic way of addressing the underlying tax problems which exist for corporate taxpayers operating in more than one Member State. The

---

<sup>40</sup> Commission, 'A package to tackle harmful tax competition in the European Union. Communication from the Commission to the Council and the European Parliament', COM(97) 564 final.

<sup>41</sup> Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments [2003] OJ L157/38.

<sup>42</sup> Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States [2003] OJ L157/49.

<sup>43</sup> Commission, 'Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee - Co-ordinating Member States' direct tax systems in the internal market', COM(2006) 823 final.

proposed solution was to provide multinational groups with a common consolidated corporate tax base ('CCCTB') for their EU-wide activities. The Commission aimed to present a comprehensive legislative proposal for the CCCTB in 2008. I consider the resulting proposed CCCTB Directive in the section on 'hard' law.

The 2006 Communication goes on to note that even if the CCCTB was in place, tax problems would remain. For example, the CCCTB would not apply to all corporate taxpayers and it would not apply at all to individuals. The Communication also broke new ground in referring to 'abuse' and 'unintended non-taxation' as consequences of un-coordinated national tax systems. As will be seen in the chapter on tax avoidance, these terms have assumed considerable significance.

The Communication draws the distinction between harmonisation and co-ordination in the following terms: 'Whereas harmonisation results in the creation of a common body of Community legislation which supersedes national laws, co-ordination builds on domestic systems to render them compatible with the Treaty and with each other. The aim of co-ordination is not to replace national tax systems by a uniform Community system but to ensure that such national systems can be made to work seamlessly together<sup>44</sup>'. On the face of it the distinction seems plausible enough, but in practice one might wonder just how national tax systems are going to be 'compatible...with each other' and to work 'seamlessly together' short of being to all intents and purposes harmonised into a single system.

Whilst the international tax system has long recognised that juridical double taxation (ie, the same person being subjected to tax by more than one jurisdiction on the same income) should be eliminated, and the OECD's model double tax convention provides alternative Articles for double tax relief by exemption (model Article 23A) or credit (model Article 23B), there is nothing in the model convention or international tax law generally that precludes or provides relief for the occurrence of economic double taxation (ie, different taxpayers being taxed on the same income or gain, as most

---

<sup>44</sup> *ibid*, p4, para 2.

commonly occurs when a company is taxed on its profits and its shareholders are taxed on what is effectively the same income when it is distributed to them in the form of dividends). It should be noted that whilst juridical double taxation rarely if ever arises unless the taxpayer is subject to tax in more than one jurisdiction, economic double taxation can arise in a domestic as well as a cross-border situation and frequently does so in company-shareholder situations where the jurisdiction concerned operates a 'classical' corporate tax system. Hence the long and intricate debates that took place in the late 1950s and 60's when measures to harmonise Member States' corporate tax systems were first seriously considered as to whether a harmonised system should be on the 'classical' or 'imputation' model. The former would afford no relief for economic double taxation, whilst the latter would afford relief by granting a shareholder an 'imputation' credit corresponding to the tax paid by the company on its profits, which the shareholder could set off against his liability to tax on dividends received. Some Member States had classical corporate tax systems and some had imputation systems (which continues to be the case) and lack of agreement as to the type of system that should be adopted were harmonisation to take place was certainly one of the factors making it difficult for Member States to find common ground (which situation also continues to be the case). Recommendations as to which type of system the EU should prefer evolved over time. The Neumark Committee recommended a 'split rate' system, under which a company pays tax on its distributed profits at a lower corporation tax rate than on its distributed profits<sup>45</sup>, as was in place at the time in Germany. The van den Tempel Report in 1970, the focus of which was company taxation in the Community and the taxation of those profits in the hands of shareholders, recommended a 'classical' system<sup>46</sup>. In its 1975 draft Directive on harmonising corporate taxes, however, the Commission recommended adoption of the 'imputation' system<sup>47</sup>.

---

<sup>45</sup> Neumark Report (n 6), p122, para 7.

<sup>46</sup> Commission, 'Corporation Tax and Individual Income Tax in the European Communities', Competition approximation of legislation series No 15, 1970 (authored by AJ van den Tempel), p41, para 159,

<sup>47</sup> Commission, 'Proposal for a Council Directive concerning the harmonization of systems of company taxation and of withholding taxes on dividends' COM(75) 392 final, 23 July 1975, Bulletin of the European Communities, Supplement 10/75, p7, para 4.



In a 1980 Report to the Council<sup>48</sup> the Commission recognised that aligning Member States' tax policies was not straightforward due to their sovereignty in direct tax matters and the differences in the economic and social underpinnings of their tax systems. In particular, the Commission recognised that the harmonisation of tax rates was especially difficult and could occur only at a much more advanced stage of economic integration, but that "Then, however, it will be absolutely necessary, since the harmonisation of structures and bases of assessment will no longer be sufficient<sup>49</sup>".

The Commission's response to Ruding marked a move from its advocating full-on harmonisation towards piecemeal *ad hoc* measures. There was an implicit recognition that in the early years the Commission's approach in direct tax matters and its emphasis on harmonisation had been overly ambitious and that targeted measures against specific tax obstacles stood a better chance of success than wide-ranging harmonisation proposals that challenged not only fundamental aspects of Member States' tax systems but their sovereignty over direct tax matters. The ECOFIN Council agreed with the Commission's position, rejecting the Ruding Committee's proposal for a minimum corporate tax rate of 30% and raising the issue of subsidiarity. It was around this time that concerted rhetoric began against 'unfair' tax competition and 'double non-taxation'.

All the same, it should not be thought that the Commission has entirely shelved its proposals for more ambitious root and branch reform, which have a habit of reappearing whenever the Commission judges the time to be ripe. Whatever problems the EU may have, a lack of vision and ambition on the part of the Commission has not been one of them. Whilst national governments and politicians come and go, the Commission has always been prepared to play a long game. As Professor Alain Barrere noted in the 1962 Neumark Report<sup>50</sup>:

---

<sup>48</sup> Commission, 'Report from the Commission to the ECOFIN Council on the scope for convergence of tax systems in the Community', COM(80) 139 final.

<sup>49</sup> *ibid*, p14, para 9.

<sup>50</sup> Neumark Report (n6), p185, Appendix E.

The drafters of the Treaty of Rome were not mistaken; the Common Market will be a gradual achievement obtained by integration of economies and harmonisation of the juridical framework of economic activity. It will be necessary to overcome resistance arising not only from habits of thought, or settled positions threatened with change, but also from political, economic and social structures which are the product of a long historical evolution and little by little have been engrained into habits of production, saving and consumption. The alteration of these structures and particularly of tax structures is always slow and requires time to become effective. To the extent that policies can hasten the process, it is expedient to settle common aims, sometimes to be reached by different routes.

Although Professor Barrere would likely have been disappointed with how little progress has been made towards integration more than 50 years after he penned those words, it must be remembered that the Community at that time consisted of only six countries, not the 28 of today.

An indication that the Commission recognises Member States' sensitivities over the erosion of their sovereignty in direct tax matters was the decision taken at a meeting of the European Council on 18-19 June 2009 to the effect that 'Nothing in the Treaty of Lisbon makes any change of any kind, for any Member State, to the extent or operation of the competence of the European Union in relation to taxation<sup>51</sup>'. This passage was almost certainly included to reassure Ireland, that country having rejected ratification of the Lisbon Treaty in a referendum held just a few days earlier, in the hope that its second referendum in 2009 would produce a positive result.

Aside from the genuinely radical CCCTB proposal, the focus of the EU in recent years and currently has been on tackling tax evasion and avoidance rather than advocating measures to bring about harmonisation *per se*. Rather the EU seems to have settled on a step-by-step ('softly-softly') approach, firstly by promoting the EU coordination of the interpretation and application of common tax principles, perhaps involving a common and uniform concept of an 'EU tax resident' to replace

---

<sup>51</sup> Commission 'Presidency conclusions of the European Council 18 and 19 June 2009', Press Release 19 June 2009, Document No. 11225/09, Annex 1, section B.

the myriad of definitions and concepts currently applied to tax residence by the various Member States. The ground would then have been firmly laid for further steps towards a broader program of tax harmonisation.

Luca Cerioni<sup>52</sup> writing in 2015 encapsulates the dilemma faced by the EU:

Over the last few years, the objectives which have been set out by the European Commission as regards the desired developments in the area of direct taxation within the EU (in parallel with the increasing concern at the wider international level to fight cross-border tax evasion and avoidance), have made it clear, in my view, that EU tax policy faces a difficult challenge: to reconcile the protection of Member States' tax revenues with the elimination of all tax obstacles to cross-border taxpayers' investments and activities, and with the simplification of the overall framework concerning direct taxation within the EU.

Cerioni's own proposed 'supranational' solution would represent an interesting advance on the EU's existing (revised) CCCTB proposals. I examine this as a possible way forward in the final chapter of this work. He admits that the solution he is proposing is going off the beaten track as far as EU and international tax law is concerned, but perhaps if the CCCTB once again fails to be adopted something off the beaten track may be what is needed to make any real progress in the direct tax area.

The requirement for unanimity under the legal basis thus far employed for direct tax legislation (Article 115) has clearly been a stumbling block. As to whether qualified majority voting (the ordinary legislative procedure) should be adopted for tax measures, the Commission made submissions to the intergovernmental conferences<sup>53</sup> preparing the Nice (2001) and Lisbon (2007) treaties to the effect that there should be a move to qualified majority voting for some types of

---

<sup>52</sup> Luca Cerioni, *The European Union and Direct Taxation* (Routledge 2015) p xii.

<sup>53</sup> Commission, 'Communication from the Commission - Supplementary contribution of the Commission to the Intergovernmental Conference on institutional reforms – Qualified majority voting for Single Market aspects in the taxation and social security fields' COM(2000) 114 final; Commission, 'Communication from the Commission to the Council – Reforming Europe for the 21<sup>st</sup> Century, COM(2007) 412 final, p6 (extension of qualified majority voting) .

direct tax measure (though not including the setting of tax rates). The matter was also discussed at the intergovernmental conference of 2003-04. The Commission's view is that in the enlarged EU, retaining unanimity for all taxation decisions may make it impossible to achieve any of the necessary tax coordination. However, the idea of a move to qualified majority voting has been consistently rejected by the Member States. It is an irony that the increased number of Member States makes the need for a move away from the requirement for unanimity ever more pressing, but at the same time all the less likely that such a proposal will gain the unanimous consent that would be required.

Finally, it should be recognised that legislative measures are not the only weapons that the Commission has at its disposal. It is able to play a significant role in aiding and abetting the Court in the process of negative integration by instituting infringement proceedings against Member States whose tax rules it considers to be discriminatory or otherwise in breach of the treaty freedoms. It is also increasingly applying the Treaty State aid provisions in the context of Member States' direct tax measures and tax administration procedures, a subject which is dealt with in a separate chapter.

## **4.2 'Hard' law**

### **4.2.1 General policy and background**

The EU's general policy on direct tax and the main legislative proposals that have been proposed over the years but not implemented have been considered in the preceding section.

I will address in this section those hard law direct tax measures that have in fact been implemented. These are relatively few and limited in scope. I will mention in addition three current draft directives, namely, a directive on double taxation dispute resolution which I touch on very briefly and the pair of draft directives that together constitute the amended Common Consolidated Corporate Tax Base ('CCCTB') proposal, which I consider at some length since if the CCCTB is implemented it would represent a huge step towards a harmonised corporate tax system.

The dependence of the EU on the unanimity of the Member States for the implementation of direct tax legislation and the reluctance of those Member States to be seen to part with any more of what

remains of their sovereignty in that field has meant that little hard law has been implemented thus far except in relatively uncontroversial matters.

Article 288 provides that in the exercise of the EU's competencies the institutions shall adopt either:

- regulations – these are binding in their entirety and directly applicable in all Member States;
- directives – these are binding as to the result to be achieved but the choice of form and methods is left to the Member States;
- decisions – these are directed at specific cases and are binding on those to whom they are addressed; or
- recommendations and opinions – these have no binding force.

The only legal basis so far employed for the passage of legislation on direct tax matters has been Article 115, under which only directives may be issued.

If enough Member States (a minimum of nine) support a legislative measure but it fails to gain unanimous support it is open to those Member States to enter into 'enhanced co-operation' with one another under the provisions of Articles 326-334. There is nothing in the enhanced co-operation procedure that precludes its application in the field of direct tax, but thus far no tax measures have been the subject of an enhanced co-operation process.

I do not propose to examine all of the directives in force in any detail. My aim is simply to highlight the particular matters to which each of the various directives apply. It will be observed that the subject matter of the directives is relatively uncontroversial, hence it was possible to achieve the required unanimity for implementation, though many of the detailed provisions were the subject of compromise in order to reach the necessary agreement.

The following directives on direct tax matters are currently in force:

- Parent-Subsidiary Directive<sup>54</sup>;

---

<sup>54</sup> Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States [2011] OJ L345/8.

- Merger Directive<sup>55</sup>;
- Interest and Royalties Directive<sup>56</sup>;
- Mutual Assistance Directive for the Exchange of Information<sup>57</sup>;
- Mutual Assistance Directive for the Recovery of Claims<sup>58</sup>;
- Taxation of Savings Income in the Form of Interest Payments Directive<sup>59</sup>; and
- Anti-Tax Avoidance Directive<sup>60</sup>.

#### 4.2.2 Parent-Subsidiary Directive

Introduced in its original form in 1990 the Directive has been recast several times, most recently in 2011. The aim of the Directive is to exempt from withholding taxes dividends and other profit distributions paid by subsidiary companies to their parent companies and to eliminate double taxation of such income at the level of the parent company. The general aim is to put a cross-border group of companies in the same position as a group of companies within a single Member State. In the case of a purely domestic group of companies most Member States would avoid double taxation in these circumstances either by exempting the profit distribution from tax in the parent company's hands or taxing it in the parent company's hands but allowing the parent company to set off a credit representing the appropriate proportion of the corporate tax paid by the subsidiary on the profits out of which the distribution was made. Where a parent company receives distributed profits from a subsidiary in another Member State the Directive requires that the Member State of the parent company must either exempt the distributed profits from tax or allow a credit for corporate tax paid

---

<sup>55</sup> Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States [2009] OJ L310/34.

<sup>56</sup> Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States [2003] OJ L157/49.

<sup>57</sup> Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation [2011] OJ L64/1.

<sup>58</sup> Council Directive 2010/24/EU of 16 March 2010 concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures [2010] OJ L84/1.

<sup>59</sup> Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments [2003] OJ L157/38.

<sup>60</sup> Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market [2016] OJ L193/1.

by the subsidiary, as described above in the context of a purely domestic situation. The Directive also requires that such distributions be exempted from withholding tax in the Member State of the subsidiary.

A parent company is defined, rather generously, as one holding at least 10% of the shares in its 'subsidiary', having been reduced from a minimum of 25% in the original Directive.

#### **4.2.2 Merger Directive**

The Merger Directive was also first introduced in 1990 and recast several times, most recently in 2009. The general aim is to put cross-border mergers, divisions, transfers of assets and exchanges of shares on the same footing for tax purposes as would be the case if the transactions were carried out within a single Member State (where reliefs would generally apply such that the transactions can be carried out on a tax-neutral basis).

#### **4.2.3 Interest and Royalties Directive**

This was introduced in 2003 and although amended a number of times has not been completely recast. The general aim is similar to that of the Parent-Subsidiary Directive, viz, to eliminate double taxation. The Interest and Royalties achieves this by abolishing withholding taxes on payments of interest or royalties by a company in one Member State to an associated company in another. The result is that there is only one incidence of tax on the interest or royalties, ie, the tax levied on the recipient company by its home Member State. A company is defined by the Directive as associated with another if it holds a shareholding of at least 25% in the other company (or vice versa), or if a third company has a shareholding of at least 25% in each.

#### **4.2.4 Mutual Assistance Directive for the Exchange of Information**

Increasing globalisation and mobility of capital and workers made it imperative that a comprehensive EU-wide structure was put in place to provide for the mutual exchange of information between national tax authorities. Prior to the Directive, arrangements between Member States for such exchange of information had been a matter of bilateral negotiation, which left many gaps and

inconsistencies. The exchange of information Directive was first introduced in 1977 (its relatively early introduction indicating that Member States needed little persuading of its merits). By the 2000s the 1977 Directive was no longer fit for purpose and was completely recast in 2011. The exchange of information Directive is seen as (and used as such in practice) a major weapon in the fight against tax evasion and avoidance.

#### **4.2.5 Mutual Assistance Directive for the Recovery of Claims**

The forerunner to the current Directive was introduced in 1976, but again by the 2000s needed a complete recasting to be made fit for purpose. The Directive enables Member States to obtain the assistance of other Member States to enforce tax debts.

The existence of this Directive, together with its sister Directive on the exchange of information, has greatly increased co-operation between national tax authorities. The two Directives have also resulted in a substantial reduction in the number of cases in which the Court is prepared to entertain claims by Member States that a national measure is justified on the grounds that it is necessary for effective fiscal supervision.

#### **4.2.6 Savings Directive**

The Savings Directive is the only directive relating specifically to the taxation of individuals. It was introduced in 2003 as part of a 'package to tackle harmful tax competition', which also included the Code of Conduct on Business Taxation and the Interest and Royalties Directive. The Savings Directive does not prohibit withholding taxes imposed by the Member State of the payer, but requires that relief from double taxation be given by the Member State of the recipient. The Directive also provides for the automatic exchange of information between Member States' tax authorities in respect of payments of interest made by persons resident in a Member State to individuals resident in another Member State. This enables Member States' tax authorities to identify interest payments made to resident individuals and to check whether the interest receipts have been disclosed on their tax returns. Given the lack of resource in most national tax authorities, the primary benefit of the



existence of the information exchange power is that taxpayers are more likely to disclose interest payments if they think that their tax authority might know about them, even though in practice the risk of discovery may be remote.

#### **4.2.7 Anti-Tax Avoidance Directive**

This is examined in some detail in the chapter on EU law and tax anti-avoidance.

#### **4.2.8 Proposed directive on Double Taxation Dispute Resolution Mechanisms in the European Union**

The draft directive<sup>61</sup> was published on 25 October 2016. It would replace an existing inter-governmental Convention<sup>62</sup> dating from 1990. The directive's key improvements over the existing Convention are that the dispute resolution procedures are to apply for all businesses and not just some businesses, that the scope of the procedures is extended from solely transfer pricing and permanent establishment issues to all cross-border issues relating to business profits, and that perhaps most importantly of all it makes the procedures subject to a defined timetable with a right for taxpayers to enforce adherence to the procedures and timetable through their national courts.

The proposed directive was agreed by ECOFIN in May 2017 and should be adopted later in 2017.

Assuming that implementation proceeds as planned, Member States will be required to adopt the directive in their domestic legislation by 30 June 2019.

#### **4.2.9 Proposed Common Consolidated Corporate Tax Base ('CCCTB') Directive**

The CCCTB Directive is by far the most important and far-reaching EU legislation on direct taxes that has been proposed. The directives implemented thus far on direct tax have addressed limited and specific issues and have been based on existing international tax principles, seeking to fill in gaps and remove anomalies that the international tax system does not address. The CCCTB on the other hand

---

<sup>61</sup> Commission, 'Proposal for a Council Directive on Double Taxation Dispute Resolution Mechanisms in the European Union' COM(2016) 686 final.

<sup>62</sup> Convention 90/436/EEC of 23 July 1990 on the elimination of double taxation in connection with the adjustment of profits of associated enterprises [1990] OJ L225/10.

would represent a complete recasting of the corporate tax system, involving a move from the traditional principle whereby companies are subjected to tax on their worldwide income by the State in which they are established and subjected to tax by other States on income arising in those States, with the State in which the company is established giving relief for the tax paid in the other States, either by credit or exemption. I should emphasise that these broad principles do not necessarily apply in every Member State or in every case. The CCCTB would replace this framework with a system under which companies operating in other Member States through a 'permanent establishment' (broadly, a branch or dependent agency), or groups of companies whose members are in different Member States, would file a single tax return in their home Member State and the aggregate profits would be apportioned between the Member States in which they operate through a formulaic apportionment method. Each Member State would then tax the share of profits apportioned to it at the tax rate of its choice. How fundamental a break with the traditional corporate tax system this represents cannot be overstated. The draft directive was proposed in 2011 but failed to gain sufficient support and in the event was not put to the vote. Had it been implemented, the legal basis would have been Article 115 (requiring unanimous consent). The radical nature of the proposals, the perceived impact on Member States' tax sovereignty and fear that it could represent a Trojan Horse to complete harmonisation, and the lack of proper costings as to the impact on individual Member State's tax revenues, were all contributory factors behind the lack of support. The proposal was shelved for a time but relaunched in a modified form in 2016.

The thinking underlying the CCCTB proposal is that the combination of the limited EU direct tax legislation implemented thus far, the case law of the Court, which can address only certain types of problem, and bilateral double tax treaties is not sufficient to fully deal with the problem of tax obstacles and distortions, and that such obstacles and distortions can be removed only through radical measures.

The CCCTB would certainly address many of the existing problems giving rise to tax obstacles and distortions but would not be a panacea for all direct tax problems that exist. For example, the CCCTB

would not apply to all corporate taxpayers and it would not apply at all to other individuals or other categories of taxpayer. Whilst it would remove the underlying conditions for many of the current tax planning strategies based on the exploitation of disparities between Member States' tax systems, the CCCTB would to a degree create new ones, as companies will undoubtedly seek to manipulate the formulaic apportionment factors such that as much profit as possible is subjected to tax in those Member States with the lowest corporate tax rates. The CCCTB proposals (both the original and revised versions) would allow Member States the right to determine their own rates of corporate tax, with no minimum rate being imposed. Ideally, the Commission would probably have liked to set a common corporate tax rate as well as a common tax base, but it would have recognised that this in effect amounted to total harmonisation, which would be a political bridge too far for all but the most enthusiastic Euro-integrationists. The VAT Directives permit Member States to set their own VAT rates but with a minimum of 15%. Allowing Member States to set their own corporate tax rates without setting a minimum would still allow the possibility of damaging tax rate competition between Member States. The CCCTB as proposed would represent a halfway house to full harmonisation – a standardised tax base but with each Member State allowed to set its own tax rate. The Commission describes the CCCTB as “A Single Corporate Tax System for a Single Market<sup>63</sup>”. Apart from the ability of Member States to set their own tax rates, the CCCTB would represent the harmonisation of corporate direct tax in all but name. The distortions caused by tax rate differentials would still remain, but no doubt pressure would subsequently be exerted on Member States to converge their corporate tax rates, or agree to a minimum rate as in the VAT system.

Whilst many of the Member States have been dubious about the CCCTB proposals, companies operating across borders have been generally supportive because of the substantial savings in tax compliance costs that they stand to make.

---

<sup>63</sup> Commission, ‘Communication from the Commission to the European Parliament and the Council Building a fair, competitive and stable corporate tax system for the EU’ COM(2016) 682 final, p5.

The original CCCTB proposal successfully negotiated the 'yellow card' procedure, under which national parliaments can assess whether a proposed measure complies with the principles of subsidiarity and proportionality and if they are not satisfied can lodge 'negative' votes<sup>64</sup>. If sufficient negative votes are received within eight weeks of the publication of a proposal the Commission is required to review it. The CCCTB proposal had the support of the European Parliament, which incidentally wanted it to be made mandatory, which would have even further reduced the likelihood of it receiving the unanimous support of the Member States. Given the number of Member States that had indicated their opposition to the proposal in the yellow card procedure, and bearing in mind that the veto of just one Member State would have been enough to torpedo it, the proposal was shelved. Suggestions had been made that it might be adopted by a limited group of Member States under the enhanced cooperation procedure, but even this did not progress. In 2012 Germany and France signalled their intention to work towards a common corporate tax regime, including the alignment of both the tax base and tax rates, but this joint effort appears to have been put on hold pending the outcome of the revised CCCTB proposal. If (as currently appears likely) the revised CCCTB proposal fails to gain the unanimous support of the Member States it remains to be seen whether the necessary minimum of nine Member States agree to adopt the proposal under the enhanced cooperation procedure, and if this too fails, whether France and Germany will reactivate their proposed common tax regime.

The enhanced cooperation procedure requires the participation of a minimum of nine Member States and is intended to be a measure of last resort, to be employed only where the Council has established that the objectives of such cooperation cannot be attained within a reasonable period by the Union as a whole<sup>65</sup>. It may well turn out to be the case that the Council feels all other options have been exhausted and that in the circumstances a procedure of last resort is justifiable. Even so, CCCTB via enhanced cooperation would be a second best solution, though probably better than

---

<sup>64</sup> The Netherlands, Ireland, UK, Sweden, Malta, Poland, Romania and Bulgaria were the eight Member States to lodge negative votes on the proposal.

<sup>65</sup> Consolidated Version of the Treaty on European Union [2008] OJ C115/13, Article 20(2).

nothing. If it proves a success, then companies in Member States that are not participating will presumably put pressure on their governments to think again.

At the time of writing the prospects of the CCCTB being implemented in its current form seem remote. Nevertheless, for the time being the CCCTB remains the Commission's flagship proposal in the corporate tax field.

#### **4.2.9.1 Original CCCTB proposal – key features**

The original proposal for a CCCTB was published as a draft directive in March 2011<sup>66</sup>. It would only have affected EU companies (of any size) that do business in more than one Member State. For those companies the attraction would have been that they would only need to file a tax return with the tax authority of their home Member State instead of filing a return in every Member State in which they do business. Annex I to the draft Directive set out for each Member State the legal forms of company to which the CCCTB could apply. In the case of a group of companies (which for CCCTB purposes would include the parent company and subsidiaries in which it held a more than 75% interest), only the parent company would file a tax return, including the profits or losses of the entire group, in its home Member State. Profits or losses for all the companies would be computed according to a standardised (common) tax base. The aggregate profits of the group, excluding all intra-group transactions, would then be apportioned to each Member State in which the group carried on business under a formula comprising three equally weighted factors based on company-specific data: labour, assets and sales. The idea behind these categories is that they would result in profits being taxed where they are earned. For specialist types of business such as financial institutions sector-specific formulae would be available. The asset factor excludes intangible and financial assets and inventory. The labour factor consists of two equally weighted elements; payroll costs and the number of employees. Sales are treated as having taken place in the country in which the customer is located. The labour, assets and sales data is collated for each Member State in which

---

<sup>66</sup> Commission, 'Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)' COM(2011) 0121 final.

the group does business and the group's consolidated profits are apportioned to each of those Member States according to the proportion the aggregated labour, assets and sales figures referable to each Member State bears to the labour, assets and sales figures for the group as whole.

The CCCTB would offer groups of companies a 'one-stop shop' for filing tax returns. This alone could represent a very substantial compliance cost saving for large groups. Additional attractions to companies were that intra-group transactions were automatically eliminated in computing the amount of profits to be apportioned between the Member States instead of being taxed in one Member State and being allowed as a tax deduction in the other. Other benefits to companies would include:

- Cost savings through computing profits according to a standardised tax base instead of a different tax base in every Member State where the group operates<sup>67</sup>.
- The need for transfer pricing on intra-group transactions within the EU would be eliminated<sup>68</sup>.
- Tax issues surrounding thin capitalisation of group subsidiaries would similarly be eliminated as these also represent intra-group transactions which normally fall to be dealt with as a transfer pricing matter<sup>69</sup>.
- The difficult matter of reliefs for cross-border losses, which has been the subject of a number of cases before the Court, would fall away entirely as profits and losses of the entire group would be consolidated<sup>70</sup>.

---

<sup>67</sup> Commission, 'Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)' COM(2011) 121 final, Explanatory Memorandum, section 1, para 1.

<sup>68</sup> *ibid*, Explanatory Memorandum, section 1, para 4.

<sup>69</sup> *ibid*, Explanatory Memorandum, section 1, para 4.

<sup>70</sup> *ibid*, Explanatory Memorandum, section 1, para 4. A leading case on cross-border loss reliefs is Case C-446/03 *Marks & Spencer plc v Halsey* [2005] ECR I-10837, in which a UK parent company sought to reduce its UK taxable profits by losses made by foreign (EU resident) subsidiaries. Had the subsidiaries been UK resident such an offset would have been allowed. As a result of the case the UK rules were (eventually) changed to allow an offset of EU subsidiaries' losses, but only in the very limited circumstances where there was no possibility of the losses ever being utilised in future in the subsidiary's home jurisdiction.

- Dividends received by participating companies would be treated as exempt income and not included in the taxable base<sup>71</sup>, thereby eliminating the problems of economic double taxation that can currently arise on dividend payments between companies.
- For companies participating in the CCCTB double tax treaties between Member States would become redundant as far as intra-group transactions were concerned as a consequence of the consolidation of group profits and losses.
- If the aggregation of the group's taxable base produced a loss, this would be carried forward and offset against the consolidated profits of future years<sup>72</sup>.

The directive was drafted on the basis that all Member States would participate. Although the Commission probably recognised that obtaining unanimous approval by the Member States would be a challenge, it is procedurally bound to propose legislation for adoption by all the Member States.

Although it was envisaged that all Member States would adopt the directive, companies would be given the option as to whether to participate in the CCCTB or not. This notwithstanding that the European Parliament had wanted the CCCTB to be mandatory for all companies and was probably a political calculation on the part of the Commission that making the scheme mandatory for all companies would make it less likely to garner the necessary Member State support. Those companies and groups that chose not to participate would carry on their tax affairs as before.

The CCCTB would standardise the tax base and the method by which the net group profits are apportioned amongst the Member States in which the group carries on business. It will not affect corporate tax rates, over which Member States will retain their full sovereign rights. Tax competition, which for multinational corporates the CCCTB would eliminate in other respects, would still exist in the form of tax rate differentials. The amount of profits apportioned to each Member State under the formula apportionment will be charged to tax at the Member State's rate of corporate tax. Member States could also if they wished tax profits apportioned to them under the

---

<sup>71</sup> *ibid*, proposed Directive, preamble, para 11.

<sup>72</sup> *ibid*, proposed Directive, preamble, para 15.

CCCTB at a different rate to the corporate tax rate they apply to companies operating purely domestically.

Simultaneously with the publication of the draft directive, the Commission issued a press release indicating that for most Member States the tax base under the CCCTB would be broader than their existing national tax bases by a factor of 7.9%<sup>73</sup>. Notwithstanding the Commission's assertion, many Member States were worried about the potential adverse impact on their tax revenues and the lack of any proper costings. Doubtless this contributed to the directive's disappointing level of support.

The exclusion of intangible assets from the asset factors was controversial. The justifications, which are well founded, are that these assets are difficult to value, especially when they have been generated internally, and that ownership is easily transferred and if they were included in the asset factor multinational businesses might be tempted to move ownership to group companies in the jurisdictions with the lowest corporate tax rates so as to give the most favourable outcome in terms of allocation of profits to the Member States.

Given the nature of such a ground-breaking and radical proposal, there are as might be expected many points of detail that would need to be dealt with. The difficulties involved in resolving these points of detail with the agreement of the Member States should not be underestimated. Neither should the challenges that would be faced with the practical implementation and administration of the scheme. If a single country were implementing a fundamentally new tax compliance system, what would typically happen is that it would be trialled using a manageable number of taxpayers so that problems can be identified, systems perfected, staff trained, etc, without the national tax system being overwhelmed if something goes wrong. In the case of the CCCTB this is unlikely to happen as it is probably procedurally impossible for the Commission to seek to implement legislation that would initially apply to only a limited number of taxpayers.

---

<sup>73</sup> Commission, Press Release 16 March 2011 'Questions and answers on the CCCTB' [MEMO/11/171], section 'Would the CCCTB lead to the broadening of the tax base in most Member States?'



#### 4.2.9.2 Revised CCCTB proposal – key features

Despite its failure to gain anything like enough support from Member States when it was first floated in 2011, the Commission resurrected its proposal for a CCCTB, albeit in modified form. A relaunch of the CCCTB was one of the five key areas for action identified in an action plan adopted by the Commission in June 2015<sup>74</sup>. Detailed proposals for the relaunch were announced on 25 October 2016<sup>75</sup>, on which date two proposed directives were published (as the new CCCTB is to be implemented in two steps). The re-calibrated (as the Commission puts it) CCCTB is designed to be more attractive to businesses by simplifying the rules and enhancing the scope for compliance cost savings. Additional attractions to business have been included in the new proposals, such as a ‘super-deduction’ for spending on research and development and a tax deduction for the notional cost of equity financing. The latter is an interesting alternative approach to tackling the distortion caused by the bias towards companies raising finance through debt (on which they get a tax deduction for interest paid) in preference to equity capital (as no tax deduction is normally available for dividends). Many Member States have tackled this problem by putting a cap on the maximum amount of debt interest a company can deduct. The Commission’s proposal approaches the problem from the other end and would allow what is in effect a tax deduction for a notional interest cost of equity capital, putting debt and equity on a more equal footing for tax purposes. No doubt the Commission hopes that businesses will now put greater pressure on their Member States’ governments to agree to the proposals.

The Commission recognised that the original CCCTB proposal was ‘...too ambitious for Member States to agree in one go<sup>76</sup>’. To facilitate swifter progress. The CCCTB has been broken down into what should be a more manageable two-step process. The first step would be the agreement on a

---

<sup>74</sup> Commission, ‘Communication from the Commission to the European Parliament and the Council A fair and efficient corporate tax system in the European Union’ COM(2015)302 final .

<sup>75</sup> Commission, ‘Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)’ COM(2016) 683 final.

<sup>76</sup> Commission website: <[https://ec.europa.eu/taxation\\_customs/business/company-tax/common-consolidated-corporate-tax-base-ccctb\\_en](https://ec.europa.eu/taxation_customs/business/company-tax/common-consolidated-corporate-tax-base-ccctb_en)> accessed 18 May 2018 (see section entitled ‘Relaunching the CCCTB’, para 2).

common tax base. The Commission envisages that consolidation could follow soon afterwards to allow the full benefits of the system to be unlocked. Taking the two steps together, the key features of the CCCTB would remain largely as outlined above in connection with the original proposal. Under the revised scheme, the setting of corporate tax rates would remain the prerogative of the Member States, meaning that the opportunity for tax rate competition would remain.

One significant difference between the original and revised versions of the CCCTB is that the original CCCTB would have been optional for all companies or groups of companies. The revised version has been made mandatory for large (total revenues exceeding €750m pa) multinational groups, which the Commission considers have the greatest capacity for aggressive tax planning, to ensure that their profits are taxed where they are really made. The scheme would remain optional for other companies and groups, meaning that the same problems of tax obstacles and distortions would remain for non-participating companies, and that Member States would have to bear the costs of running two corporate tax systems in parallel. Actually, much of the 'problem' represented by tax distortions (which is to say the existence of differences between Member States' tax systems) is that multinational groups see these differences in a positive light as opportunities to make tax savings through tax planning which exploits those differences. Whilst the revised proposals take the matter out of the hands of the largest multinationals, this will still leave a large number of quite substantial multinational operators the choice between the tax compliance cost savings they might make by participating in the scheme and the tax saving opportunities they would forego.

Another significant difference between the original and revised proposals is that the latter includes a raft of anti-avoidance provisions.

As with the original proposal, the revised CCCTB would be implemented by all Member States. The proposed directives would therefore require the unanimous agreement of the Member States.

#### 4.2.9.3 Reaction to the revised CCCTB proposal

The proposal was discussed at the ECOFIN Council in November 2016 and again in May 2017. The published outcome of the May 2017 meeting merely states that the CCCTB proposal was discussed and that the discussions would continue<sup>77</sup>. According to a report of the CCCTB discussions at the May 2017 meeting<sup>78</sup> the President of the Council proposed that only the first part of the proposal (the common tax base) would be discussed, but as will be seen from some of the comments cited below some of the representatives commented on the consolidation stage of the proposal as well as the common tax base. Apparently, few of the Member State representatives gave the proposal unconditional support, and criticism and reservations were the predominant theme of the discussion. Some of the areas where particular concerns were expressed were:

- To what extent would Member States be allowed a degree of flexibility in implementing reliefs such as the research and development ‘super deduction’ and notional interest deduction for equity capital. Pierre Moscovici, one of the EU’s tax commissioners, agreed that Member States should be given a certain degree of flexibility in order to reach an agreement but warned that this flexibility should not undermine the benefits of the scheme<sup>79</sup>.
- Should the tax base be relatively broad (ie, few exemptions and reliefs) or relatively narrow (ie, a larger number of exemptions and reliefs). A broad tax base means that the amount of income liable to tax is greater but, as a result, the tax rate can be lower. Conversely, a narrow tax base results in less income being liable to tax but with the consequence that the tax rate must be higher to bring in the same amount of tax revenue as a broad base and lower tax rate. Currently, there is a wide discrepancy amongst Member States as to which end of the spectrum their tax base lies. Denmark, Sweden and Finland have particularly broad tax bases at present and indicated that unless the common tax base is a similarly broad one they will not

---

<sup>77</sup> Council, ‘Outcome of the Council meeting’, 23 May 2017, 9581/17, p4.

<sup>78</sup> Online article by Adelina Marini dated 12 June 2017, ‘The Second CCCTB Proposal Seems Also Headed for a Failure’ <<http://www.euinside.eu/en/news/the-second-ccctb-proposal-seems-to-be-headed-for-another-failure>> accessed 18 May 2018.

<sup>79</sup> *ibid*, para 2.

support it as they calculate that they would lose revenues. They expressed the view that the most effective corporate tax system is one with a broad base and a low rate<sup>80</sup>.

- Doubts were expressed by Cyprus<sup>81</sup> and the Netherlands<sup>82</sup> as to whether the proposal complied with the subsidiarity principle (even though the original proposal had passed through the 'yellow card' procedure).
- Some Member States do not consider that the proposal strikes the right balance between harmonisation and flexibility<sup>83</sup>.
- There was concern that the need for Member States to run two different tax systems (one for companies opting into CCCTB and one for those that do not) would make administration difficult and involve a substantial increase in the costs of tax administration for the Member States, which the smaller economies could ill afford<sup>84</sup>.
- Ireland, which has opposed the proposal from the outset, approved the idea of enhanced deductions for research and development spending but considered that flexibility was needed to allow member states to retain the research and development incentives that they already have<sup>85</sup>.
- Belgium approved the common tax base in principle provided that it allows Member States a certain degree of flexibility, but is not in favour of measures that go beyond harmonising the base<sup>86</sup>.
- Concern was expressed by a number of Member States as to the impact of the harmonised tax base on their corporate tax revenues and it was clear that much more work on costings still remained to be done<sup>87</sup>.

---

<sup>80</sup> *ibid*, para 3.

<sup>81</sup> *ibid*, para 4.

<sup>82</sup> *ibid*, para 6.

<sup>83</sup> *ibid*, paras 2, 4 & 5.

<sup>84</sup> *ibid*, para 4.

<sup>85</sup> *ibid*, para 5.

<sup>86</sup> *ibid*, para 5.

<sup>87</sup> *ibid*, paras 3, 4, 6 & 8.

- Austria supported the common tax base in principle but was opposed to the imposition of a research and development super deduction, which it considers is a matter that should be left to individual Member States<sup>88</sup>.
- The Luxembourg representative gave the most detailed critique<sup>89</sup>. In his view there was an unnecessary overlap between the anti-avoidance provisions in the revised CCCTB and those contained in the EU's existing Anti-Tax Avoidance Directive, as well as with the globally agreed base erosion and profit shifting ('BEPS') recommendations. He considered that many aspects of the proposal would lead to confusion, not clarity, and that whilst full harmonisation of corporate taxes might strengthen the EU institutionally it might not necessarily strengthen the EU economically. He also warned that the proposed incentives for research & development might conflict with EU State aid rules. According to experts' estimates in Luxembourg, the cost of introducing the common tax base and consolidation would be 0.8% of GDP.
- Italy recognised the proposals as a unique opportunity to create a predictable and more stable EU tax framework, but advocated compromise in order to strike a balance between flexibility and consistency in the application of rules<sup>90</sup>.
- The representative of the Czech Republic observed that the fact that the proposal for the CCCTB has been on the table for six years has led to a convergence of Member States' tax systems. If a little more work was done on the proposal it should be possible to achieve agreement.<sup>91</sup>
- The German Finance Minister, last to speak, brought an additional tone of scepticism. In his view the discussion had increased the problems rather than lessened them. He emphasised that as well as safeguarding the integrity of the single market the EU needed to retain its

---

<sup>88</sup> *ibid*, para 7.

<sup>89</sup> *ibid*, paras 7 & 8.

<sup>90</sup> *ibid*, para 9.

<sup>91</sup> *ibid*, para 10.

competitiveness. He concluded that “We should be careful not to raise too high expectations”.<sup>92</sup>

As I mentioned, the focus of the May 2017 ECOFIN Council discussion was the first part of the CCCTB proposal (common tax base). The second part (consolidation and apportionment) is likely to meet with even greater doubts and concerns. Even if only the common tax base stage is implemented, and even if in order to achieve Member State agreement it is found necessary to allow Member States a considerable degree of latitude as to its implementation, this would still represent a great step on the road towards harmonisation.

## **4.3 ‘Soft’ law**

### **4.3.1 Background**

The primary reason for the EU’s reliance on soft law in the field of direct tax is of course the unanimity requirement for hard law measures.

Soft law, whatever particular form it takes, is of persuasive or exhortatory value only and is not legally binding.

In addition to the more formal, but still non-binding, recommendations and opinions referred to by Article 288, EU soft law has taken a number of other forms. For example, resolutions, communications, notices and consultations. The differences between these various forms is of no great significance for present purposes.

It might be thought that ‘soft’ law initiatives have little real effect and represent little more than a ‘virtue signalling’ exercise by the EU. To be sure soft law relies mainly on peer pressure (in this case that of other Member States) and on pressure from the media and the public. The power this pressure can exert should not be underestimated, however, particularly since the 2008 financial crisis and the subsequent unprecedented media and public focus on tax, with the nebulous proposition

---

<sup>92</sup> *ibid*, para 11.

espoused by politicians that taxpayers should pay their 'fair' share. 'Naming and shaming' taxpayers of all types, but especially multinationals, has proved to be a powerful incentive for high profile taxpayers to put their affairs in order and cease to employ some of the more egregious tax avoidance schemes that were regarded as perfectly standard planning in the not too recent past. These public pressures apply to governments and, through them, national tax systems as well as companies. A government offering a tax break, whether in the form of a low rate or a special relief, that has the effect of attracting investment that might otherwise have gone elsewhere is nowadays likely to attract opprobrium from the international community. The overall result could be a tendency over time towards harmonisation, so that no country can be accused of acting 'unfairly' in the setting of its tax policies.

Soft law initiatives have come to form a significant part of the EU's push towards greater direct tax harmonisation, or co-ordination. Part of the reason for this is the very limited progress that the EU has been able to make thus far on implementing hard law measures and that the 'negative' integration resulting from the Court's judgments is necessarily limited in scope. As well as having persuasive value, soft law is also a useful way for the Commission to set out goals and objectives that the limited number of hard law directives and case law of the Court have been unable to achieve, and to set out its priorities and the main issues it would like to see addressed. Invariably, soft law that is issued will reference the specific Treaty objectives that the soft law is intended to promote.

That said, it must be recognised that measures that are merely persuasive are very much an imperfect means of achieving a genuine harmonisation of national tax systems. In the absence of Community competence in the field of direct taxation, however, and without the unanimity required for the implementation of hard law measures there is little more for the present that the Commission can do.

The EU has been canny in recent years, both in its soft law initiatives and its proposals for new directives, in putting the emphasis on 'co-ordination' rather than on 'harmonisation'. The former term presumably sounds less provocative and less threatening to Member States' sovereignty over

direct tax matters. The EU has also been shrewd in capitalising on the widespread public revulsion at some of the more egregious tax avoidance indulged in by high profile taxpayers by portraying itself as a champion of the people against aggressive tax avoiders, which has somewhat put Member States on the back foot when it comes to resisting the EU's taxation initiatives – a reversal of the position that had prevailed hitherto.

The EU's employment of soft law in the tax context has been the subject of a detailed study by Hans Gribnau<sup>93</sup>. He makes the point that although the Code of Conduct, for example, is non-binding, peer pressure has ensured that Member States have taken it seriously and amended their tax measures to comply with it<sup>94</sup>. Although the Code of Conduct is generally regarded as an effective political instrument<sup>95</sup>, one criticism Gribnau makes of it is that whilst the dialogue involves the Member States themselves, a wider involvement of civil society would make for a more responsive and legitimate process<sup>96</sup>. As to the relationship between soft law and hard law, Gribnau remarks:

There is often a subtle interplay between soft law and hard law. This also goes for the Code of Conduct which was reinforced by a more strict interpretation by the Commission of the Treaty rules on State aid. The State aid criteria and the Code of Conduct have a dominant influence on the national debates on corporate income tax. Thus, the combination of hard law and soft law was used to convince the Member States to take their obligations with regard to tax coordination more seriously. Soft law itself may also have hard edges. Notable is the fact that the results of the Primarolo report [the report drawn up by the Code of Conduct Group in 1999 to identify tax measures that may fall within the scope of the Code of Conduct and named after Dawn Primarolo, its Chairman] were presented as *acquis communautaire* in the negotiations with new Member States. Here, a switch appears to have been made: soft law became a form of 'extremely hard law'. Of course, this treatment

---

<sup>93</sup> Hans Gribnau, 'Soft Law and Taxation: EU and International Aspects', [2008] *Legisprudence* Vol 2 No 2, pp67-117.

<sup>94</sup> *ibid*, pp83, para 4.

<sup>95</sup> *ibid*, p84, para 1.

<sup>96</sup> *ibid*, pp68-69. This theme and its significance for EU legitimacy is developed at greater length at pp85-93.



may lead to considerable pressure from new Member States on the old Member States to fully comply with the Code. Finally, soft law instruments from different institutional contexts may reinforce each other. In this respect it is interesting that the Code of Conduct explicitly refer to the OECD's transfer pricing guidelines, on the one hand, and that the Code has had a significant impact on the work of the OECD in the field of harmful tax competition, on the other<sup>97</sup>.

#### **4.3.2 Code of Conduct for Business Taxation**

Perhaps the most important of the EU's soft law initiatives on direct tax is the 'Code of Conduct for Business Taxation'. This emerged from the 1997 Commission paper 'Towards Tax Co-ordination in the European Union'<sup>98</sup>. The paper set out three proposals on direct taxation, two of which were implemented as directives and are dealt with in the section on hard law. The third proposal was for a Code of Conduct for Business Taxation, which was adopted on 1 December 1997 in the form of a Resolution<sup>99</sup>. The Code of Conduct set out proposals for dealing with what was termed 'harmful tax competition' and was endorsed by the Council in the form of a resolution.

The Code of Conduct is not legally binding. Its adoption committed Member States:

- (i) not to introduce any new tax measures that showed certain 'harmful' characteristics listed in the Code (this element was termed 'standstill'); and
- (ii) to amend or repeal existing tax measures with such characteristics ('rollback').

The Code defines 'harmful' tax measures as those (including administrative practices) '...which affect or may affect in a significant way the location of business activity in the Community<sup>100</sup>' and '...which

---

<sup>97</sup> *ibid*, pp84-85.

<sup>98</sup> Commission, 'Communication from the Commission to the Council – Towards tax co-ordination in the European Union – A package to tackle harmful tax competition' COM(97)0495 final.

<sup>99</sup> Resolution of the Council on a code of conduct for business taxation [1997] OJ C2/1.

<sup>100</sup> *ibid*, Code of Conduct, para A.

provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question ....<sup>101</sup>.

Monitoring the compliance, or otherwise, of Member States' tax regimes with the Code of Conduct is very much an ongoing exercise, particularly with the accession of new Member States, and a Code of Conduct Group was set up by ECOFIN in 1998 charged with this responsibility. The Group reports to the Council and since its inception has reported on a large number of specific Member State tax measures that it considers should be rolled back. In most cases Member States have either repealed the measures concerned or modified them to remove the objectionable features. It should be borne in mind that all this has been achieved on a largely voluntary basis.

In addition to its ongoing work in connection with the Code of Conduct and harmful tax practices, the Code of Conduct Group has been given a central role by the Council<sup>102</sup> in the screening of jurisdictions and drawing up an EU list of non-cooperative jurisdictions for tax purposes. In its brief to the Code of Conduct Group, the Council emphasised that the Group's work should be carried out in coordination with the OECD's work on BEPS, as clearly there is a significant overlap. The Code of Conduct Group was tasked with selecting and screening third country jurisdictions (ie, other than EU Member States) with regard to a number of tax good governance criteria, including fair taxation, anti-BEPS measures and in particular tax transparency<sup>103</sup>. The intention was that the list of non-cooperative jurisdictions would be ready for the Council to endorse by the end of 2017. The Code of Conduct Group selected 92 jurisdictions for screening, of which 17 featured as non-cooperative on the list adopted by the Council in December 2017<sup>104</sup>.

---

<sup>101</sup> *ibid*, Code of Conduct, para B.

<sup>102</sup> European Council, 'Criteria and process leading to the establishment of the EU list of non-cooperative jurisdictions for tax purposes – Council conclusions (8 November 2016)' 14166/16 FISC 187 ECOFIN 1014.

<sup>103</sup> *ibid*, Annex, recital 7.

<sup>104</sup> European Council 'The EU list of non-cooperative jurisdictions for tax purposes – Council conclusions (adopted on 5 December 2017)' 15429/17 FISC 345 ECOFIN 1088.

There is little doubt that the Code of Conduct has been the most successful of the EU's soft law initiatives in direct tax<sup>105</sup> and not surprisingly the Commission has indicated that it wishes to strengthen the role of the Code of Conduct Group and change its working methods to enable it to react more efficiently to cases of harmful tax competition. Compliance with the Code of Conduct has become an important pre-condition of accession to the EU for new Member States. For example, regarding the accession of the ten new Member States in 2004, the Commission stated:

In parallel with the accession negotiations, in which the acceding countries committed themselves to comply with the principles of the Code of Conduct for Business Taxation and, notably, to introduce only new tax measures which are in conformity with these principles, the Commission undertook to assess an established list of tax measures in the acceding countries as to whether these could be considered as being harmful under the Code of Conduct. Following a report from the Commission of 6 June 2003, the Council concluded on 9 October 2003, which tax measures were harmful and which must be eliminated or amended in order to bring the corporate tax systems of the acceding Countries in line with the principle of the Code of Conduct by the date of accession<sup>106</sup>.

Again, however, whilst the Code of Conduct has been successful in eliminating a large number of 'harmful' tax measures from Member States' statute books, it is at best a vehicle towards 'negative' integration, as with the Court's case law in the direct tax field, as opposed to the 'positive' integration that can only meaningfully be achieved through binding legislation.

---

<sup>105</sup> Many specific examples of 'harmful' tax regimes that have been identified by the Code of Conduct Group and subsequently abolished or modified by the Member States concerned, including measures abolished or amended by the 2004 intake of new Member States prior to their accession, are set out in Tax-News.com, 'Spotlight on the EU Code of Conduct Group', 4 July 2017. Available online at: <[https://www.tax-news.com/features/Spotlight\\_On\\_The\\_EU\\_Code\\_Of\\_Conduct\\_Group\\_\\_574446.html](https://www.tax-news.com/features/Spotlight_On_The_EU_Code_Of_Conduct_Group__574446.html)> accessed 20 May 2018.

<sup>106</sup> Commission, 'Activities of the European Union in the tax field in 2003', 27 January 2004, DOC (2004) 1402, p15, para 6.

### 4.3.3 Soft law guidance on case law

One particularly helpful use of soft law is the guidance that the Commission sometimes issues (usually in the form of a Communication) following significant Court rulings. For example, in the field of ‘exit’ taxes the Commission was not only active in bringing infringement proceedings against Member States which retained dubious exit tax measures on their statute books following the landmark Court cases on that subject (two of which are examined below), but issued soft law guidance to Member States following some of those decisions to help them understand the implications of the Court’s rulings. Admittedly, not all of the Commission’s comments in these Communications were necessarily backed up by what the Court had actually said. Take for example the Commission’s Communication issued on 19 December 2006<sup>107</sup>. This was issued subsequent to the decisions of the Court in *Lasteyrie du Saillant*<sup>108</sup> and *N*<sup>109</sup>. The Communication recognised that a Member State has the right to assess accrued income or gains to tax when a taxpayer transfers their residence to another Member State as this is justified by the principle of fiscal territoriality linked to a temporal component, namely residence within the territory during the period in which the taxable profit arises, but that immediate collection or attaching onerous conditions to the deferral was not proportionate. Although *Lasteyrie du Saillant* and *N* concerned individuals, the Communication observed that the Court nowhere stated that the principles apply only to individuals and that, in the opinion of the Commission, they also apply to companies. This raised some eyebrows<sup>110</sup> as this assertion was yet to be backed up by jurisprudence of the Court (the Communication pre-dated the decision in *National Grid Indus*<sup>111</sup> in which the Court put it beyond doubt that the same principles do indeed apply to companies).

---

<sup>107</sup> Commission, ‘Communication of 19 December 2006 from the Commission to the Council, the European Parliament and the European Economic and Social Committee on exit taxation and the need for co-ordination of Member States’ tax policies’ COM(2006) 825 final.

<sup>108</sup> Case C-9/02 *Hughes de Lasteyrie du Saillant v Ministere de l’Economie, des Finances et de l’Industrie* [2004] ECR I-02409.

<sup>109</sup> Case C-470/04 *N v Inspecteur van de Belastingdienst Oost/kantoor Almelo* [2006] ECR I-07409.

<sup>110</sup> For example see Confederation Fiscale Europeenne, ‘Opinion Statement of the CFE ECJ Task Force on the Judgment in the Case of *CARTESIO Okato es Szolgaltato bt* [2008] ECR I-09641’, in *European Taxation 2009* (Volume 49) No 7, p379.

<sup>111</sup> Case C-371/10 *National Grid Indus BV v Inspecteur van de Belastingdienst*[2011] ECR I-12273.

## 4.4 The Court's case law

### 4.4.1 The Court's competence in direct taxes

Given the significance of the role that the Court's case law plays in matters of direct taxation today, it is easy to forget that until around the mid-1980s direct tax matters were regarded as purely a Member State competence, entirely outside the scope of the Treaties and, therefore, the Court's remit.

The fundamental principle that powers retained by member States were not absolute but had to be exercised consistently with Community law had been established well before this time in a number of non-tax cases. The principle was applied in a direct tax case for the first time in *Avoir Fiscal*<sup>112</sup>, but put into its most familiar formulation in *Schumacker*<sup>113</sup>, which is restated almost verbatim in almost every direct tax case the Court has subsequently considered:

Although, as Community law stands at present, direct taxation does not as such fall within the purview of the Community, the powers retained by the Member States must nevertheless be exercised consistently with Community law....[para 21].

This principle is as valid today as it was then and has been unaffected by the various revisions to the Treaties over the years.

### 4.4.2 What Community law is engaged?

What then, in the context of direct taxes, is the 'Community law' that the Member States' competence must be exercised consistently with? The case law on direct taxes since *Avoir Fiscal* has almost entirely concerned the four 'fundamental freedoms' set out in the Treaty, viz:

- Article 45 - freedom of movement for workers;
- Article 49 – right of establishment;

---

<sup>112</sup> Case C-270/83 *Commission of the European Communities v French Republic* [1986] ECR 00273.

<sup>113</sup> Case C-279/93 *Finanzamt Köln-Altstadt v Roland Schumacker* [1995] ECR I-00225.

- Article 56 – services; and
- Article 63 – capital and payments.

Article 45 provides that:

1. Freedom of movement for workers shall be secured within the Union.
2. 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.

Article 49 provides that:

Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State.

Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the Chapter related to capital.

Article 54 provides that:

Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Union shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States.

Article 56 provides that:

Within the framework of the provisions set out below, restrictions on freedom to provide services within the Union shall be prohibited in respect of nationals of Member States who are established in a Member State other than that of the person for whom the services are intended.

Finally, Article 63 provides that:

1. Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.
2. Within the framework of the provisions set out in this Chapter, all restrictions on payments between Member States and between Member States and third countries shall be prohibited.

To these four fundamental freedoms must be added the free-standing prohibition on discrimination on the grounds of nationality contained in Article 18. Furthermore, following the creation of Citizenship of the Union introduced through the Maastricht Treaty, Articles 20 and 21 provide that every citizen of the Union shall have the right to move and reside freely within the territory of Member States. The right of free movement afforded to citizens of the Union is additional to any rights available under the fundamental freedoms, but as the fundamental freedoms are only engaged where some form of economic activity is taking place, freedom of movement under Articles 20 and 21 would generally only need to be relied on (if needs be in conjunction with Article 18) where the movement is for non-economic reasons, for example, retirement. As the focus of this work is on taxation, which necessarily implies that some form of economic activity or transfer is being or has been undertaken, I do not consider the Article 20 or 21 rights any further.

The somewhat intricate inter-relationship between the general prohibition on discrimination on the grounds of nationality of Article 18 and the fundamental freedoms is examined in more detail

shortly, but it may be concluded that all of the four fundamental freedoms incorporate a prohibition on discrimination so I will not examine any of the small number of direct tax cases that have been founded on Article 18 as a stand-alone provision.

Another important freedom, indeed perhaps the most crucial of all as far as the single market is concerned, is that concerning the free movement of goods, dealt with in Articles 28 to 37. The tax issues surrounding movements of goods are primarily of an indirect tax nature (Value Added Tax, customs duties, etc), which are outside the scope of this work.

The principle that EU law (including the judgments of the Court) overrides the laws of the Member States was emphatically stated in *Van Gend en Loos*<sup>114</sup> and *Costa*<sup>115</sup> and was settled law long before *Avoir Fiscal* came before the Court.

It should also be noted at the outset that the fundamental freedoms are both directly applicable (ie, they do not need to be specifically incorporated in a Member State's domestic law) and as Treaty provisions have both vertical and horizontal direct effect (ie, they can be relied upon in a Member State court against either the Member State or against other persons). Action in direct tax cases invariably lies against the State, so horizontal direct effect is rarely if ever engaged.

The fundamental freedoms apply in both directions, viz, to movements to a Member State and to movements from a Member State. For example, the right of establishment provisions are most typically invoked into order to gain access to the market of another Member State, or equality in that market with nationals (in its expanded Article 54 sense) of that Member State, but can apply equally in the opposite direction, ie, to restrictions placed upon a national of a Member State who wishes to leave that Member State and establish himself in another one. The cases on freedom of establishment that I examine below include examples of movements in both directions.

---

<sup>114</sup> Case 26/62 *Van Gend en Loos v Nederlandse Administratie der Belastingen* English special edition 1963 00001.

<sup>115</sup> Case 6/64 *Flaminio Costa v ENEL* English special edition 1964 00585.



In addition to persons claiming Treaty rights before their national courts and tribunals which may then make references to the Court for a ruling on a particular matter, the Commission itself can institute legal proceedings before the Court through the infringement proceedings process where it considers that a particular Member State measure is contrary to EU law. The Commission is far from backward in taking infringement proceedings in direct tax matters, though it should not be assumed that it always gets its own way. For example, in a ruling from early 2015, *Commission v UK*<sup>116</sup>, the Commission was unsuccessful in challenging the UK law on cross-border corporate loss relief that had been amended following the long-running litigation in *Marks & Spencer*.<sup>117</sup>

Sometimes a matter can fall within the ambit of more than one freedom. In such cases the Court's approach is to assess to which freedom the measure in question most closely relates<sup>118</sup> and deal with the case solely in light of that predominant freedom. In practice this does not generally cause difficulties since although the four freedoms are framed differently, the Court's approach over the years has been to adopt a policy of 'converging interpretation' (expanded on below). This is both sensible and practical, since if the Court adopted a significantly different approach to each of the freedoms it would mean, firstly, that the decision as to which freedom was engaged could become crucial to the success or failure of the case, and secondly that there would be likely to be a great deal more inconsistency and lack of clarity as to what the law was in any particular circumstances, creating uncertainty for the Court itself, national courts, Member States and those seeking to rely on the freedoms. The converging interpretation approach means that the difference between which freedom is engaged is usually only significant where both Articles 49 and 63 are potentially engaged. Chiefly, this is because Article 49 is only engaged in the case of intra-Member State movements, whilst Article 63 can apply not only to intra-Member State movements but movements between a Member State and a third country (or vice versa). Cases where both Articles 49 and 63 are potentially engaged usually involve some form of investment (most often a shareholding), and in

---

<sup>116</sup> Case C-172/13 *European Commission v United Kingdom* ECLI: EU: C; 2013: 305.

<sup>117</sup> Case C-446/03 *Marks & Spencer plc v Halsey* [2005] ECR I-10837.

<sup>118</sup> Case C-452/04 *Fidium Finanz AG v Bundesanstalt* [2006] ECR I-09521.

such cases the Court's approach is to consider whether the Member State national's investment gives him/it a 'definite influence'<sup>119</sup> over the investee entity's decisions and allows him/it to determine its activities: if it does, the Court deals with the case only under Article 49; if it does not, the Court applies only Article 63<sup>120</sup>. What constitutes 'definite influence' in this context has not yet been made entirely clear: a 10% shareholding was found not to constitute a definite influence<sup>121</sup>, but a 48% holding was<sup>122</sup>, albeit this finding has been criticised. In the *Thin Cap GLO*<sup>123</sup> case, the UK tax rules in question applied only where a parent company held at least 75% of the shares in a subsidiary, and the Court ruled that this fell to be treated under Article 49. The same principle was applied in *Cadbury Schweppes*<sup>124</sup>, a UK case concerning the UK's controlled foreign companies tax rules which applied only to UK companies with a more than 50% shareholding in their foreign subsidiaries; the Court found that such a level of control gave the UK company a definite influence on the subsidiaries' decisions and allowed it to determine their activities, with the result that the case was dealt with under Article 49. The effect of this approach is that if an investment carries a definite influence such that the Court will only consider the case under Article 49, and the investment happens to be with a third country, to which Article 49 cannot apply, the Court will not substitute Article 63 and, consequently, the matter falls outside the scope of the Treaty. This basic distinction is modified where the national measure at issue applies in both situations where the investment gives definite influence and where it does not, or where it is not clear whether the claimants satisfy the definite influence test or not; in these circumstances the Court will consider both Articles 49 and 63. The approach is further modified where the national rule at issue applies to dividends received on an investment in a third country and does not apply exclusively to cases where the investor has a

---

<sup>119</sup> Case C-251/98 *C Baars v Inspecteur der Belastingen* [2000] ECR I-02787.

<sup>120</sup> As for example in Case C-47/12 *Kronos International Inc v Finanzamt Leverkusen* [ECLI: EU: C: 2014: 2200] which concerned the taxation of dividends and in which the national rules in question applied to all cases and not just those where the recipient of the dividends had a particular level of interest in the paying company, as a result of which the Court dealt with the case under Article 63.

<sup>121</sup> Case C-377/07 *Finanzamt Speyer-Germesheim v STEKO Industriemontage GmbH* [2009] ECR I-00299.

<sup>122</sup> Case C-282/07 *SPF Finances v Truck Center SA* [2008] ECR I-10767.

<sup>123</sup> Case C-524/04 *Test Claimants in the Thin Cap Group Litigation v Commissioners of Inland Revenue* [2007] ECR I-02107.

<sup>124</sup> Case C-196/04 *Cadbury Schweppes plc, Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue* [2006] ECR I-07995.

decisive influence; in those circumstances the Court will consider only Article 63, the effect of which is that if a national measure does apply only to cases where there is decisive influence the measure will fall within Article 49 and not Article 63 and, where the investment is with a third country, will not be susceptible to challenge under the Treaty since third country investments are covered by Article 63 but not Article 49.

#### **4.4.3 What is prohibited under the four freedoms?**

I will try as far as possible to address the position taking the four freedoms as a whole rather than dealing with each freedom separately. This is consistent with the Court's policy of converging interpretation, which it is able to adopt because the four freedoms essentially resolve into two basic rights. Firstly, a right of cross-border circulation, which might be termed market *access*, including rights as against both home and destination Member States to, respectively, leave and transfer to that State without hindrance. Secondly, a right of market *equality*, being the right not to be discriminated against on the grounds of nationality or origin.

Prohibited under the four freedoms are:

- discrimination; and
- restrictions (which term may be taken as synonymous with obstructions and hindrances) to the exercise of a freedom.

Discrimination on the grounds of origin or destination are chiefly concepts used in connection with the movement of goods, which as mentioned earlier does not normally give rise to direct tax issues.

The discrimination prohibited under Articles 45, 49 and 56, for the reasons given below, is discrimination on the grounds of nationality. For Article 63 purposes, again for the reasons given below, discrimination encompasses both that on the grounds of nationality and origin and destination. Not all the four freedoms define or refer to discrimination in the same way and it is worthwhile examining why such discrimination can be said to be prohibited under all of the freedoms.

Each of the four freedoms specifies what is prohibited under that particular freedoms, viz:

- Article 45 - *discrimination* based on nationality.
- Article 49 - *restrictions* on the freedom of establishment.
- Art 56 - *restrictions* on the freedom to provide services.
- Art 63 – *restrictions* on the movement of capital.

Clearly Article 45 is explicit that discrimination on the grounds of nationality is prohibited.

The second paragraph of Article 49 amounts to a requirement not to discriminate on grounds of nationality:

Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the laws of the country where such establishment is effected....

Article 57 provides a similar 'under the same conditions as are imposed by that State on its own nationals' requirement for the purposes of Article 56, and Article 61 provides that insofar as restrictions on the freedom to provide services have not been abolished, Member States shall apply those restrictions without distinction on the grounds of nationality or residence.

Discrimination is also referenced in the context of Article 63, though more obliquely. Paragraph 1(a) of Article 65 provides that for Article 63 purposes a Member State may: '...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'.

This is qualified, however, by paragraph 3 which states that what is permitted in, *inter alia*, paragraph 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'.

The references to discrimination in the context of Articles 45, 49, 56 and 63 are all specific manifestations of the free-standing prohibition against discrimination contained in Article 18. A

notable difference, though possibly of little or no practical significance, between the references to discrimination in connection with Articles 45, 49 and 56 and the reference to discrimination in connection with Article 63 is that the former all expressly refer to discrimination on the grounds of nationality, as does the free-standing prohibition on discrimination under Article 18, but the reference to arbitrary discrimination in Article 65 (applicable to Article 63) does not make it clear what sort of arbitrary discrimination is to be prohibited: discrimination on the grounds of nationality, or on the grounds of origin or destination, or both? Although discrimination is not defined (expressly or impliedly) for the purposes of Article 63 as being on the grounds of nationality or origin/destination, this is almost certainly deliberate as movements of capital can be discriminated against on either ground. For example, a national measure may provide a more favourable treatment for domestic investors than those from other Member States by discriminating (directly or indirectly) on the grounds of nationality. Alternatively, a national measure may provide a more favourable treatment for capital from a domestic source than from a foreign source, thereby discriminating on the grounds of origin/destination. Thus both types of discrimination may potentially apply for Article 63 purposes, whilst in the case of Articles 45, 49 and 56 discrimination if it exists is invariably (directly or indirectly) on the grounds of nationality rather than origin/discrimination. In this light the differences in the definition of discrimination in the various freedoms are explained.

Though Article 65(1)(a) allows for a difference in treatment it is interpreted strictly by the Court. In fact, the Court appears to require that any different treatment based on Article 65(1)(a) must be justified, in which case it is doubtful whether it adds anything at all to the justifications the Court would apply anyway under its 'rule of reason'. For example, in *Manninen*<sup>125</sup> the Court held that:

A distinction must therefore be drawn between the unequal treatment permitted under Article [65(1)(a)] and the arbitrary discrimination prohibited under Article [65(3)]. According to the case law, in order for national tax legislation such as that at issue in the main

---

<sup>125</sup> Case C-319/2 *Petri Manninen* [2004] ECR I-07477.

proceedings...to be regarded as compatible with the Treaty provisions on the free movement of capital, the difference in treatment must concern situations which are not objectively comparable or be justified by overriding reasons in the general interest. In order to be justified, moreover, the difference in treatment ...must not go beyond what is necessary in order to attain the objective of the legislation in question [para 29].

Article 54 expressly provides that companies and firms are to be treated as natural persons for right of establishment purposes. The free-standing prohibition against discrimination on the grounds of nationality (Article 18) does not similarly state that it also applies to companies and firms as well as natural persons. There have been cases, however, where the Court has interpreted Article 18 as applying to a company. For example *International Jet Management*<sup>126</sup>, where the company was not within the scope of any of the four freedoms so had to rely on Article 18.

In passing it should be noted that 'reverse discrimination', ie, a Member State discriminating against (as opposed to in favour of) domestic taxpayers, is outside the scope of the Treaty.

#### **4.4.4 The Court's approach to discrimination and restrictions**

A restriction (though the Court sometimes uses the terms 'obstacle' or 'hindrance', which should be taken as synonymous) is, broadly, a national measure that does not discriminate but which applies to all persons (ie, it is a 'measure without distinction' to use movement of goods terminology) but which in fact hinder intra-Union economic activity. All measures that prohibit, impede, or render less attractive the exercise of a freedom are regarded as restrictions. The national provision does not actually have to prevent the exercise of a treaty freedom to constitute a restriction; it is enough that the measure may have a dissuasive effect on taxpayers wishing to exercise it. Thus even the imposition of additional administrative requirements on a taxpayer establishing themselves in another Member State has been found disproportionate if they would not have applied to a taxpayer that established themselves in another part of the same Member State.

---

<sup>126</sup> Case C-628/11 *International Jet Management GmbH* ECLI: EU: C: 2014: 171.

As previously mentioned, the Court has adopted an approach of converging interpretation<sup>127</sup>. Strictly, its approach should be different depending on whether the national measure in issue involves discrimination or whether it is a restriction. I would also mention that in what follows ‘discrimination’ should be taken to mean discrimination on the grounds of nationality unless otherwise stated. In principle, discrimination should be absolutely prohibited unless it falls within one of the derogations expressly permitted in the Treaty itself, for example, public policy, public security or public health in the case of Article 45. Also in principle, such prohibition on discrimination should apply whether the discrimination is direct (overt) or indirect (covert). Where a measure is not discriminatory but constitutes a restriction on the exercise of a freedom then, as well as the derogations expressly written into the Treaty, the Court will apply its ‘rule of reason’ to determine whether the measure is justified. If it is found justified, then the final step will be for the Court to consider whether the measure is proportionate. These concepts will be explained further in what follows.

It should be mentioned in passing that there is a substantial body of literature on the concepts of direct discrimination, indirect discrimination and non-discriminatory restrictions, and the Court’s sometimes inconsistent approach to dealing with each in practice. Generally, in tax cases, it is considered that the Court has moved from a discrimination approach to a restriction approach though, as Christiana Panayi notes, without having abandoned the former<sup>128</sup>. The difficulties and lack of clarity that can arise from the blurring of the concepts of discrimination (particularly indirect discrimination) and restrictions, the evolving approach of the Court in this area and its general (but inconsistent) move towards a restriction rather than discrimination approach and consequent inconsistent application of justifications, are examined in depth by Ben Terra and Peter Wattel<sup>129</sup>. The subject is also treated at length in a study by Servaas van Thiel<sup>130</sup>. Van Thiel also considers the

---

<sup>127</sup> Ben Terra & Peter Wattel, *European Tax Law* (Abridged edition, Kluwer 2012), section 3.2.2 at p44.

<sup>128</sup> Christiana Panayi, *European Union Corporate Tax Law* (Cambridge University Press 2013), p152, para 3.

<sup>129</sup> Ben Terra & Peter Wattel, *European Tax Law* (6<sup>th</sup> unabridged edition, Wolters Kluwer 2012), section 3.2.7.1, pp83-92.

<sup>130</sup> Servaas van Thiel, *Free Movement of Persons and Income Tax Law: the European Court in Search of Principles* (IBFD 2002), chapter 4 at pp225-318.

meaning of the principles of equal treatment and non-discrimination in a multilateral Community<sup>131</sup>, and the difficulties the Court encounters in trying to reconcile these principles with the OECD's traditional view that residents and non-residents should generally be treated as being in different situations for tax purposes<sup>132</sup>.

The Court's policy of adopting a converging interpretation means that these principles can be examined for the four freedoms taken together. Such a policy would make the Court's job easier and make for greater legal certainty if was in fact applied consistently. The Court's current policy might be summarised as follows. Where a national measure is found to directly discriminate, the Court will generally (but not always) rule against the measure unless it falls within an express treaty derogation and will not consider 'unwritten' justifications under the rule of reason. Where a national measure indirectly discriminates, the Court generally approaches it in the same way as if it was a restriction and, therefore, will consider not only express Treaty derogations but justifications under the rule of reason. If it is accepted that in principle the Treaty freedoms prohibit discrimination, whether direct or indirect, unless it falls within one of the Treaty derogations, the Court's regular adoption of a restriction based analysis in cases which involve manifestations of indirect discrimination is arguably incorrect, and means that an indirectly discriminatory measure can potentially be saved by a justification under the rule of reason doctrine when strictly the rule of reason doctrine should not be applied to a discriminatory measure at all. The Court's approach is to an extent understandable, as it is consistent with its desire to move towards a converging interpretation (in the senses both of approaching all the freedoms in the same essential way and of applying the same analytical methodology to restrictions and indirect discrimination), and recognises the fact that in practice it can be extremely difficult to determine when a measure is indirectly discriminatory and when it is 'merely' restrictive. The Court appears to have failed thus far, at least in a direct tax context, to have provided a coherent distinction even between direct and indirect discrimination, let alone as between indirect discrimination and restriction. In view of the difficulties an attempt to distinguish

---

<sup>131</sup> *ibid*, chapter 5 at pp319-530.

<sup>132</sup> *ibid*, pp375-376 and pp393-401.



between indirect discrimination and restriction is likely to encounter and the fine distinctions that would have to be made, it seems unlikely that the Court will make any attempt to address the issue in the foreseeable future. Its approach, therefore, though perhaps legally questionable, is understandable and on the whole realistic and sensible.

The Court's approach in cases where a measure overtly discriminates on the grounds of nationality is still fairly robust, and unless they fall within an express Treaty derogation such measures will usually be struck down without considering justifications under the rule of reason. However, even before directly discriminatory direct tax rules started to be challenged under European law, relatively few Member States' tax rules did in fact discriminate overtly on the grounds of nationality. Much more common are rules that apply differently depending on whether a taxpayer (individual or corporate) is 'resident' for tax purposes in that Member State. These are much more problematic for the Court to deal with, as will be illustrated in what follows.

Discrimination has been described by the Court as the application of different rules to comparable situations, or of the same rules to different situations. As a general proposition, comparable situations must not be treated differently unless such treatment is objectively justified. The difficulty for the Court can be in determining the situations to be compared. Judging comparability has to be done on a case by case basis, taking into account the particular circumstances as well as the object and purpose of the national measure in question. The Court usually applies a similar comparability test whether the measure is restrictive or indirectly discriminatory. If the comparability test indicates that the situations being compared are objectively similar, the national measure is likely to be held to breach the freedom unless it can be justified and is proportionate. If the test indicates that the situations being compared are not objectively similar, then it is likely that the Court will conclude that no breach of the Treaty freedom has in fact occurred.

#### 4.4.5 Justifications

Where a national measure is discriminatory or restrictive, the Treaty freedoms themselves provide for only limited derogations, which being exceptions to the fundamental freedoms are interpreted and applied strictly by the Court.

In addition to these 'written' derogations, the Court has developed a body of 'unwritten' justifications, under what has come to be known as its 'rule of reason'. This originated in cases concerning movements of goods, most notably in *Cassis de Dijon*<sup>133</sup>, in which the Court introduced additional unwritten grounds of justification it called 'overriding reasons of public interest' in addition to the derogations set out in what is now Article 36. The unwritten grounds referred to in *Cassis de Dijon* included:

- the effectiveness of fiscal supervision;
- the protection of public health;
- the fairness of commercial transactions; and
- the defence of the consumer.

In *Gebhard*<sup>134</sup>, which concerned the freedom to exercise legal services in Italy, the Court summarised its rule of reason test for application to all the Treaty freedoms as having four criteria:

It follows...from the Court's case law that national measures liable to hinder or make less attractive the exercise of fundamental freedoms guaranteed by the Treaty must fulfil four conditions:

- they must be applied in a non-discriminatory manner;
- they must be justified by imperative requirements in the general interest;
- they must be suitable for securing the attainment of the objective which they pursue; and

---

<sup>133</sup> Case 120/78 *Rewe-Zentral AG v Bundesmonopolverwaltung fur Branntwein* [1979] ECR 00649 (commonly referred to as the *Cassis de Dijon* case),

<sup>134</sup> Case C-55/94 *Reinhard Gebhard v Consiglio dell'Ordine degli Avvocati e Procuratori di Milano* [1995] ECR I-04165.

- they must not go beyond what is necessary in order to attain that objective...[para 37].

Step 1 of the test would suggest that if a national measure is discriminatory (even if the discrimination is indirect) it cannot benefit from a justification under the rule of reason. As far as direct tax cases are concerned this step is more honoured in the breach than the observance. Where a measure could be said to indirectly discriminate the Court's usual practice is to apply the rule of reason doctrine as it would with a restriction. To cite but one such instance, in *Bachmann*<sup>135</sup> a German national working in Belgium and whose earnings were taxable in Belgium was unable under Belgian law to obtain a tax deduction for pension contributions, etc, paid to German companies. Only contributions paid to Belgian companies were deductible under Belgian law. As pension contributions would overwhelmingly be paid to Belgian companies by Belgian nationals, this rule clearly constituted indirect discrimination on the grounds of nationality against nationals of other Member States who were working in Belgium. Nevertheless, the Court applied the rule of reason and, furthermore, ruled the measure to be justified on the grounds of cohesion of the national tax system.

That the rule of reason doctrine applies in relation to indirectly discriminatory measures as well as restrictive measures has been supported by Mattias Dahlberg<sup>136</sup>, who claims that the view of some authors that the rule of reason doctrine and grounds of justification in the public interest do not apply in cases of indirect discrimination seems to be losing ground. Dahlberg does not, however, go so far as to claim that the rule of reason doctrine also applies in relation to direct discrimination. For example, in *Royal Bank of Scotland*<sup>137</sup> the Court found direct discrimination and went no further than to consider whether it fell within one of the express derogations in the relevant Article.

Dahlberg acknowledges that there are some commentators who would like to see the rule of reason doctrine also applied to measures constituting direct discrimination (albeit there have been isolated,

---

<sup>135</sup> Case C-204/90 *Hanns-Martin Bachmann v Belgian State* [1992] ECR I-00249.

<sup>136</sup> Mattias Dahlberg, *Direct Taxation in Relation to the Freedom of Establishment and the Free Movement of Capital* (Kluwer 2005) 119.

<sup>137</sup> Case C-311/97 *Royal Bank of Scotland plc v Elliniko Dimosio* [1999] ECR I-02651.

and probably anomalous, cases where this has actually happened). In principle I agree that there may be some merit in applying the rule of reason to direct as well as indirect discrimination. Is it not somewhat artificial that a measure should be struck down without further ado if it directly discriminates (subject to Treaty derogations) but has the possible benefit of the rule of reason if it only indirectly discriminates? And is not the distinction between discrimination and restriction somewhat artificial in any event? Would it not make more sense for the Court to formally acknowledge that it will treat cases of discrimination (direct and indirect) in the same way as restrictions?

The Court's approach was summarised as follows by Melchior Wathelet, a former judge of the Court and currently one of the Advocate Generals, in an article<sup>138</sup>, though he was careful to point out that these were only his personal views. Wathelet claimed that as regards direct discrimination, only express limitations and exceptions contained in the Treaty apply. He further explained that the Court, especially in relation to cases on direct taxation, after finding a difference in treatment [presumably after applying the appropriate comparator] will examine all justifications put forward, both statutory exceptions and limitations and grounds in the public interest '...without ruling whether the measures considered are [indirectly] discriminatory or not'.

In practice, the Court usually follows the approach outlined by Wathelet and ignores the first of the four *Gebhard* rule of reason steps in direct tax cases unless the measure is overtly discriminatory, and has moved towards a three step rule of reason which can be summarised in the following terms.

- Does the measure concerned distinguish between the cross-border situation and the comparable domestic situation (resident/non-resident; emigrant/non-emigrant; domestic source income/foreign source income, etc) in a manner impeding the exercise of free movement rights? This is the comparability assessment.

---

<sup>138</sup> Melchior Wathelet, 'The Influence of Free Movement of Persons, Services and Capital on National Direct Taxation: Trends in the Case Law of the Court of Justice', *Yearbook of European Law*, Vol 20, issue 1, 1 January 2001 pp1-33 at pp15-16.

- If so, and the measure is not within any the derogations contained in the relevant Treaty Article, is it justified by a legitimate aim (eg, curbing abuse, safeguarding coherence of the tax system, ensuring effective fiscal supervision)? This is the assessment of whether the measure in question can be justified under the rule of reason doctrine.
- If so, does the impeding effect go beyond what is necessary to attain that legitimate aim? This is the assessment of whether a measure is proportionate.

The Court is inconsistent as to the point at which it considers comparability<sup>139</sup>. Sometimes it will consider comparability at step one of the three step post-*Gebhard* rule of reason doctrine, ie, if the cross-border and domestic situations that have been determined by the Court to be the appropriate comparators are not objectively comparable, the Court will rule that the measure is not susceptible to challenge<sup>140</sup>. On other occasions, however, it will take an apparent distinction in treatment at face value as constituting a restriction and only consider lack of comparability as a possible justification at step 2<sup>141</sup>. The result is likely to be the same in either case, the only difference being that comparability is considered at different stages in the analysis. To all intents and purposes the distinction between indirect discrimination and restrictions seems to have been obliterated as far as direct tax cases are concerned when it comes to justifications<sup>142</sup>.

A clear statement on the matter from the Court would be helpful, however.

---

<sup>139</sup> For a discussion of the evolution of the Court's approach to the rule of reason test in direct tax cases and its occasional 'wandering' between steps 1 and 2 in considering comparability see Ben Terra & Peter Wattel, *European Tax Law* (Abridged edition, Kluwer 2012) at p45 and p62.

<sup>140</sup> As in Case C-282/07 *Belgium v Truck Center SA* [2008] ECR I-10767, para 36, in which the Court stated 'In order to determine whether a difference in tax treatment is discriminatory, it is...necessary to consider whether, having regard to the national measure at issue, the companies concerned are in an objectively comparable situation'. In *Truck Center* the Court found that the domestic and cross-border situations were not objectively comparable [para 41] and that consequently the difference in tax treatment did not constitute a restriction [para 50], having determined which the Court did not go on to consider justifications.

<sup>141</sup> As in Case C-446/03 *Marks & Spencer plc v Halsey* [2005] ECR I-10837, in which the Court found that a UK tax measure constituted a restriction [para 34] that was only permissible if justified [para 35]. The Court then went on to consider various possible justifications, including whether the companies concerned were not in comparable tax situations [para 36].

<sup>142</sup> Christiana Panayi, *European Union Corporate Tax Law* (Cambridge University Press 2013), p156, para 2: 'Finally, it ought to be pointed out that lately the distinction between discrimination and restriction seems to have been obliterated. When it comes to justifications, at least in a tax-related context, the Court...tends to merge the discrimination and restriction concept'.

Before turning to the types of justifications that the Court has accepted under its rule of reason doctrine, some matters that the Court has ruled do not constitute restrictions on the exercise of freedoms (viz, they are not considered a restriction in the first place so the question of whether a justification applies, either under a Treaty derogation or the rule of reason, does not arise) should be mentioned. These include the following.

- The parallel exercise of taxing powers by Member States, even if this gives rise to unrelieved double taxation<sup>143</sup>.
- A Member State applying different rules to residents and non-residents. The Court accepts that in principle residents of a Member State and non-residents are not in a comparable situation regarding tax matters since there are generally objective differences between them (*Renneberg*<sup>144</sup>). If, however the facts of the particular case and the national measure in issue are such that a non-resident is objectively in a comparable situation with a resident (as in *Schumacker* and *Renneberg*), the principle may be overridden.
- Disparities between Member States' tax systems. The Court has on many occasions reiterated that disparities are outside the scope of the Treaty freedoms, for example in *Perfili*<sup>145</sup>:

'...the Court has consistently held that, in prohibiting every Member State from applying its law differently on the ground of nationality, within the field of application of the Treaty, Articles...are not concerned with any disparities in treatment which may result, between Member States, from differences existing between the laws of the various Member States, so long as they affect all persons subject to them in accordance with objective criteria and without regard to their nationality... [para 17].'

It should be noted that the Court's acceptance that residents and non-residents are in principle not in comparable situations is nothing new but simply mirrors what has been a foundation of the

---

<sup>143</sup> Case C-128/08 *Jacques Damseaux v Belgium* [2008] ECR I-7735, paras 27 and 30.

<sup>144</sup> Case C-527/06 *RHH Renneberg v Staatssecretaris van Financien* [2008] ECR I-07735, para 59.

<sup>145</sup> Case C-177/94 *Gianfranco Perfili* [1996] ECR I-00161.

international tax system since long before the founding of the European Community. Most states have traditionally had very different sets of tax rules for residents and non-residents and this is regarded as perfectly normal and unobjectionable. The principle is expressly stated in the non-discrimination Article (24) of the OECD's model double tax treaty (which is used as the basis for the vast majority of the world's double tax treaties) which provides that:

Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected.

A question that has arisen is whether there is a principle of 'abuse of rights' in direct tax matters. The Court has accepted that there is a general principle of EU law that abuse of rights is prohibited<sup>146</sup>, viz, that a Member State is entitled to take measures to prevent persons from improperly or fraudulently taking advantage of EU law in order to circumvent national legislation. Although a principle of abuse of rights may be deduced from some VAT cases<sup>147</sup>, the Court has stated that it does not apply in non-harmonised areas such as direct taxes<sup>148</sup>. That said, whilst abuse of rights does not of itself bar access to treaty rights, it may, go some way to justifying a restriction.

The justifications accepted by the Court have evolved over time since rule of reason justifications were first broached in *Cassis de Dijon*, and, as will be seen, those employed in direct tax cases now include a number applicable solely in tax cases.

In *Cassis de Dijon* the Court referred to these additional unwritten grounds of justification as 'overriding reasons of public interest'. The principle categories of justifications thus far accepted by the Court in direct tax cases are as follows.

---

<sup>146</sup> Case C-126/10 *Foggia – Sociedade Gestora de Participacoes Sociais v Secretario de Estado dos Assuntos Fiscais* [2011] ECR I-10923 at para 50.

<sup>147</sup> Eg, Case C-255/02 *Halifax plc (and others) v Commissioners of Customs & Excise* [2006] ECR I-01609.

<sup>148</sup> Case C-417/10 *Ministry of Finance v 3M Italia SpA* ECLI: EU: C: 2012: 184, para 45

- The need for effective fiscal supervision. Acceptance of this justification has declined over the years owing to the proliferation of information exchange and mutual enforcement powers between tax authorities and especially the two Mutual Assistance Directives.
- The need to combat tax fraud.
- The need to preserve fiscal cohesion/coherence of the national tax system. Essentially, if in a particular situation a Member State does not tax income from a particular activity, it would be consistent with the principle of fiscal cohesion that it need not allow a tax deduction for the expenses related to that activity (and vice versa)<sup>149</sup>. The fiscal cohesion justification does not apply unless there is a direct link between the tax levy and tax advantage (eg, relief or deduction).
- The need to safeguard a balanced allocation of taxing powers/jurisdiction. In principle the Court accepts that that Member States are free to determine how to allocate powers of taxation between themselves and other Member States and “that a difference in in treatment between nationals of the two contracting States that results from that allocation cannot constitute discrimination<sup>150</sup>”. However, the Court expects fiscal jurisdiction should be allocated in a balanced and limited manner in accordance with international tax law and the territoriality principle. For example, it would be reasonable for a Member State to tax its residents on their worldwide income and to tax non-residents only on income which has its source in that Member State (eg, interest, dividends, royalties, or profits made from the activities of a branch located in that Member State). It would not, however, be reasonable for a Member State to tax non-residents on their worldwide income and if a Member State were to do so it is unlikely

---

<sup>149</sup> For a relatively straightforward application of the fiscal cohesion justification see Case C157/07 *Finanzamt für Körperschaften v Krankenhaus Ruhesitz am Wannsee-Seniorenheimstatt GmbH* [2008] ECR I-08061.

<sup>150</sup> Case C-376/03 *D v Inspecteur van de Belastingdienst* [2005] ECR I-05821.



that the Court would regard that as a balanced and limited allocation of taxing jurisdiction on that Member State's part.

- The need to prevent the double use of losses and loss trafficking. This justification is not sufficient in itself but may be used in combination with another justification<sup>151</sup>.
- The prevention of tax avoidance. The Court will now only accept this justification where the measure in question is targeted only at 'wholly artificial arrangements' that do not reflect economic reality and whose only purpose is to obtain a tax advantage<sup>152</sup>. This sets a very high bar indeed for a tax authority as almost any tax planning can be implemented with at least a veneer of commercial substance.

There is inevitably a degree of overlap between these categories of justification and the Court has been somewhat inconsistent as to which it applies in what appear to be broadly similar circumstances. In particular, the demarcation between the fiscal coherence and balanced allocation justifications is far from clear. Both may be regarded as safeguarding the integrity of a Member State's tax base, though this is not an expression that has been used by the Court.

Grounds not accepted by the Court as justifications include:

- A loss of revenue and erosion of a Member State's tax base.
- The availability of administrative remedies.
- The availability of counterbalancing advantages.

Article 63 can also apply to capital movements with third countries, but the Court has shown itself more willing to entertain justifications in the case of capital movements to/from third countries than those entirely intra-EU.

The categories of justification developed by the court, though subject to occasional change and periodic changes of emphasis, have remained broadly intact over recent years. What has changed,

---

<sup>151</sup> As in Case C-18/11 *Commissioners for Her Majesty's Revenue & Customs v Philips Electronics UK Ltd* ECLI: EU: C: 2012: 532.

<sup>152</sup> Eg, Case C-182/08 *Glaxo Wellcome GmbH & Co KG v Finanzamt Muenchen* [2009] ECR I-08591, para 81.

however, is that as far as tax measures are concerned the court is raising the bar ever higher as to what it will accept as justified and proportionate. This may be partly due to its integrationist tendencies, but can primarily be ascribed to the increasing degree of cooperation between Member States as regards the administration, enforcement and collection of taxes. The existence of the Mutual Assistance Directives in particular has been frequently cited in recent years by the Court as a reason to find Member States' tax measures unjustified or disproportionate.

In addition to the steady raising of the bar as to what will be accepted by the Court as justified and proportionate, the degree of economic cross-border linkage necessary for freedom of establishment to be engaged has steadily been diminished over the years to the point where it may now be said to be almost negligible.

#### **4.4.6 Illustrative cases**

The purpose of this section is to show how the principles and methodology outlined above are applied by the Court in practice and how the extent of the Court's jurisdiction in direct tax matters has developed since *Avoir Fiscal*. Only having done that will it be possible to appreciate the limitations on the Court's competence in this area. I have chosen four cases in connection with the right of establishment given its relative importance in direct tax cases, including two of the leading cases on exit taxes, and two each for the other three freedoms. The Court's policy of converging interpretation means that its approach is fundamentally the same for each of the four freedoms, so this limited number of cases should suffice to illustrate the key points.

A remark may be appropriate at this point as to the style of the Court's judgments. Its practice is to deliver a single, composite, judgment. This means that its judgments sometimes bear the signs of compromise and the reasoning is not always the most rigorous or easy to follow. The absence of dissenting judgments (unless the AG's preliminary opinion is not followed by the Court, or the AG reaches the same conclusion but through different reasoning) does not afford the opportunity to see an alternative legal argument. Nor as a rule does the Court entertain hypothetical situations so there is little that corresponds to the useful *obiter dicta* sometimes found in English law judgments. The

Court usually cites previously established principles verbatim from earlier cases, giving its judgments something of a ‘cut and paste’ quality. Where, as frequently happens, a previous case is cited but is not quite on all fours with the facts of the instant case it can make the reasoning particularly hard to follow. The fact that few of the Court’s judges appear to have much experience of tax cases in their home jurisdictions does not help<sup>153</sup>.

An extended analysis of the Court’s case law is not within the compass of this work and the cases selected are those in which certain key principles were first clearly established. Although the principles illustrated in these cases have been developed by the Court subsequently, the cases examined still represent fundamentally good law. The cases I will examine are as follows.

Article 45 (workers):

- *Bosman*<sup>154</sup>
- *Schumacker*<sup>155</sup>

Article 49 (right of establishment):

- *Royal Bank of Scotland*<sup>156</sup>
- *Avoir Fiscal*<sup>157</sup>
- *Lasteyrie du Saillant*<sup>158</sup>
- *National Grid Indus*<sup>159</sup>

Article 56 (services):

---

<sup>153</sup> Of the Court’s 28 current judges and 11 Advocates General, only Sweden’s Carl Gustav Fernlund appears to have any significant prior experience in the field of taxation, whether in a professional, political, academic or judicial capacity, according to the biographical information available on the Court’s website: <[https://curia.europa.eu/jcms/jcms/Jo2\\_7026/](https://curia.europa.eu/jcms/jcms/Jo2_7026/)> accessed 19 May 2018.

<sup>154</sup> Case C-415/93 *Union Royale Belge des Societes de Football Association v Jean-Marc Bosman* [1995] ECR I-04921.

<sup>155</sup> Case C-279/93 *Finanzamt Köln-Altstadt v Roland Schumacker* [1995] ECR I-00225.

<sup>156</sup> Case C-311/97 *Royal Bank of Scotland plc v Elliniko Dimosio* [1999] ECR I-02651.

<sup>157</sup> Case 270/83 *Commission of the European Communities v French Republic* [1986] ECR 00273.

<sup>158</sup> Case C-9/02 *Hughes de Lasteyrie du Saillant v Ministere de l’Economie, des Finances et de l’Industrie* [2004] ECR I-02409.

<sup>159</sup> Case C-371/10 *National Grid Indus BV v Inspecteur van de Belastingdienst* [2011] ECR I-12273.

- *Commission v Spain*<sup>160</sup>
- *Eurowings*<sup>161</sup>

Article 63 (capital and payments):

- *Manninen*<sup>162</sup>
- *Commission v UK*<sup>163</sup>

#### 4.4.6.1 *Bosman*

*Bosman* is a good example of the Court's approach to restrictions, ie, measures that do not discriminate on the grounds of nationality and apply equally to both nationals and non-nationals of the Member State concerned, but which represent a restriction or obstacle hindering the exercise of a Treaty freedom.

*Bosman*, a Belgian footballer, wished to leave his Belgian club and move to France to play for a French club. This required that a transfer fee be paid to the player's former Belgian club, and such a fee would have been payable whether the player had transferred to a foreign (ie, non-Belgian) club or a Belgian club. The rule thus did not discriminate (directly or indirectly) on the grounds of nationality. The Court considered whether the transfer rules formed an obstacle to the free movement of workers prohibited by Article 48 (now 45) of the Treaty.

The Court held that:

Provisions which preclude or deter a national of a Member State from leaving his country of origin in order to exercise his right to freedom of movement...constitute an obstacle to that freedom even if they apply without regard to the nationality of the workers concerned.....[para 96]

---

<sup>160</sup> Case C-153/08 *Commission of the European Communities v Spain* [2009] ECR I-09735.

<sup>161</sup> Case C-294/97 *Eurowings Luftverkehrs AG v Finanzamt Dortmund-Unna* [1999] ECR I-07447.

<sup>162</sup> Case C-319/02 *Petri Manninen* [2004] ECR I-07477.

<sup>163</sup> Case C112/14 *European Commission v United Kingdom* ECLI: EU: C: 2014: 2369.

The Court has also stated...that even though the Treaty provisions relating to freedom of establishment are directed mainly to ensuring that foreign nationals and companies are treated in the host Member State in the same way as nationals of that State, they also prohibit the Member State of origin from hindering the establishment in another Member State of one of its nationals or of a company incorporated under its legislation.... The rights guaranteed by Article 52 [now 49], et seq, of the Treaty would be rendered meaningless if the Member State of origin could prohibit undertakings from leaving in order to establish themselves in another Member State. The same considerations apply, in relation to Article 48 [now 45] of the Treaty, with regard to rules which impede the freedom of movement of nationals of one Member State wishing to engage in gainful employment in another Member State. [para 97]

It is true that the transfer rules at issue in the main proceedings apply also to transfers of players between clubs belonging to different national associations within the same Member State and that similar rules govern transfers between clubs belonging to the same national association.[para 98]

However, as has been pointed out by...the Advocate General..., those rules are likely to restrict the freedom of movement of players who wish to pursue their activity in another Member State by preventing or deterring them from leaving the clubs to which they belong even after the expiry of their contracts of employment with those clubs.[para 99]

Since they provide that a professional footballer may not pursue his activity with a new club established in another Member State unless it has paid his former club a transfer fee agreed between the two clubs..., the said rules constitute an obstacle to freedom of movement for workers. [para 100]

Consequently, the transfer rules constitute an obstacle to freedom of movement for workers prohibited in principle by Article 48 [45] of the Treaty. It could only be otherwise if those rules pursued a legitimate aim compatible with the Treaty and were justified pressing

reasons of public interest. But even if this were so, application of those rules would still have to be such as to ensure achievement of the aim in question and not go beyond what is necessary for that purpose..... [para 104]

The Court then considered possible justifications but found that none were acceptable. It followed that the question of whether justifications were proportionate did not arise.

Although *Bosman* is not a tax case it is a good illustration of the principles in cases involving restrictions/obstacles imposed by Member State on persons seeking to leave it and the Court's approach to the analysis. For companies, the tax restrictions most often encountered when the company wishes to transfer its legal seat or residence (broadly, its centre of operations) from one Member State (the residence or origin State) to another (the host or destination State) are forms of 'exit' taxes imposed by the origin/residence state. Two of these 'exit' cases are considered below as illustrations of the application of the principles set out in *Bosman* in a specifically tax context.

#### **4.4.6.2 Schumacker**

This case illustrates that point that whilst in principle the Court accepts that residents and non-residents are not in comparable situations, there are exceptions.

Schumacker was a Belgian national who whilst continuing to live in Belgium commuted to work in Germany. His sole income was the income from his German employment. Under the double tax treaty between Belgium and Germany the right to tax employment income earned in Germany was allocated solely to Germany. Germany taxed its residents on an unlimited basis, ie, on worldwide income, but taxed non-residents only on a limited basis, ie, on income that arose in Germany.

Certain German personal tax allowances and reliefs were available only to those subject to tax in Germany on an unlimited basis and Schumacker's claim to these was refused.

The question for the Court was whether the application by Germany of different rules to non-residents which resulted in a higher level of German tax liability for those individuals than was

imposed on German residents in a comparable situation was contrary to the freedom of movement of workers.

The Court noted that whilst the legislation at issue did not distinguish on the basis of nationality it did constitute indirect discrimination on the grounds of nationality as most non-residents would be non-German nationals [paras 27-28].

As to whether Schumacker was in a comparable situation with a German-resident worker, the Court noted the principle that, as a rule, residents and non-residents are not in a comparable situation with regard to direct taxes [para 31], which follows from the fact that in most cases the income of an individual predominantly arises in the Member State of which they are a resident and the part of their income taxable in another Member State is usually only a part of their total income. The Member State of residence is therefore, as a rule, in a better position to assess the individual's total personal and financial interests and grant the appropriate allowances and reliefs.

Schumacker's case fell outside the general rule, however, as the whole of his income was earned in Germany and whilst he was entitled to Belgian allowances and reliefs he had no income liable to Belgian tax against which to set those allowances and reliefs [para 36]. The Court ruled that in these circumstances there was no objective difference between the situations of such a non-resident and a resident engaged in comparable employment [para 37]. Therefore, the Court found, discrimination arose from the fact that the personal circumstances of the taxpayer were not taken into account in either the state of residence or the state of employment [para 41].

The German government's claims that the rule could be justified on the grounds either of the cohesion of the tax system or the effectiveness of fiscal supervision were rejected. As to cohesion, this was inappropriate as Germany taxed the whole of Schumacker's income, putting him in effectively the same position as a German resident, so it was unreasonable for Germany not to give him personal allowances [para 42]. The fiscal supervision argument was dismissed as the Mutual Assistance Directive enabled a Member State to obtain any relevant information it required [paras 43-45].

Incidentally, *Schumacker* is just one of those many cases where the Court expressly found indirect discrimination yet still entertained justifications under the rule of reason instead of taking the position that discrimination, whether direct or indirect, was absolutely prohibited unless it fell within a specific Treaty derogation.

#### **4.4.6.3 *Royal Bank of Scotland***

One of the relatively rare direct tax cases in which the tax rule in question discriminated overtly on the grounds of nationality was *Royal Bank of Scotland*. Royal Bank of Scotland plc had its legal seat in the UK and a branch in Greece. Greek law taxed the profits of domestic (ie, Greek) plcs at a rate of 35%. The tax rate applied to the profits of foreign companies (including their branches in Greece) was 40%. The question of whether this was compatible with EU law was referred to the Court by the Greek Administrative Court of First Instance. By virtue of Article 54, Royal Bank of Scotland was regarded as a national of the UK. The Court first considered the matter of comparability:

In order to determine whether a difference in tax treatment such as that resulting from [the Greek tax rule] is discriminatory, it is necessary to ascertain whether, for the purposes of the taxation of profits earned in Greece, a company having its seat in Greece and a branch established in Greece of a company having its seat in another Member State are in an objectively comparable situation. It is settled case law that discrimination consists in the application of different rules to comparable situations or in the application of the same rule to different situations. [para 26]

As far as direct taxation is concerned, the Court has held, in cases relating to the taxation of income of natural persons, that the situations of residents and non-residents in a given State are not generally comparable, since there are objective differences between them from the point of view of the source of the income and the possibility of taking account of their ability to pay tax or their personal and family circumstances. However, it has explained that, in the case of a tax advantage denied to non-residents, a difference in treatment between the categories of taxpayer might constitute discrimination within the meaning of the Treaty



where there is no objective difference such as to justify different treatment on this point as between the two categories of taxpayers. [para 27]

As far as the method of determining the taxable base is concerned, the Greek tax legislation does not establish, as between companies having their seat in Greece and companies which, whilst having their seat in another Member State, have a permanent establishment [broadly, a branch] in Greece, any distinction such as to justify a difference of treatment between the two categories of companies. [para 28]

It is true that companies having their seat in Greece are taxed there on the basis of their world-wide income (unlimited tax liability) whereas foreign companies carrying on business in that State through a permanent establishment are subject to tax there only on the basis of the profits which the permanent establishment earns there (limited tax liability). However, that circumstance, which arises in relation to that of the limited fiscal sovereignty of the State in which the income arises in relation to that of the State in which the company has its seat is not such as to prevent the two categories of companies from being considered, all other things being equal, as being in a comparable situation as regards the method of determining the taxable base. [para 29]

The Court concluded:

Consequently, national legislation, such as the Greek tax legislation, which for the purposes of taxing income, does not establish, as between companies having their seat in Greece and companies which, having their seat in another Member State, have a permanent establishment in Greece, any distinction such as to justify, in relation to the same taxation, a difference in treatment between the two categories of companies and which establishes a difference in treatment as regards the rate of income tax, introduces discrimination against companies having their seat in another Member State in so far as it imposes on them, irrespective of their legal form and the nature of the shares which they issue, a rate of

taxation of 40% whereas the rate of 35% only applies to companies whose seat is in Greece.

[para 30]

Finally, it is necessary to examine whether discrimination such as that in question in the main proceeding may be justified. According to settled case law, only an express derogating provision...could render such discrimination compatible with Community law.... [para 32]

Clearly, there was no question in the Court's mind that justifications under the rule of reason might be entertained in addition to the derogations set out in the relevant Treaty Article given that overt discrimination was involved.

#### **4.4.6.4 *Avoir Fiscal***

As mentioned earlier, the first challenge to the assumption that direct tax was entirely outside the ambit of the Treaties was *Avoir Fiscal*. This was an infringement action brought by the Commission against France in 1983. French tax law allowed French companies a tax credit (the *avoir fiscal*) in respect of dividends received on their shares in other French companies, which credit was offset against the recipient company's liability to tax on the dividends. The credit was only available to French resident companies, however, so if shares in a French company were owned by the French branch of a non-French company, the branch would not be entitled to a credit, even though the branch was liable to French tax on the dividends it received on those shares.

The question posed was whether the denial by France of a tax credit to French branches of companies established in other Member States was contrary to freedom of establishment for companies.

The Court upheld the Commission's contention that the French rules discriminated against branches of companies established in other Member States by comparison with companies established in France. The Court observed that the discrimination was made all the more clear by the fact that both French companies and French branches of non-French companies were both liable to French tax on the dividends [para 11].

As to the specific Treaty freedom in point, the Court stated:

...the fact that the tax rules in question are unfavourable to the branches...of foreign...companies indirectly restricts the freedom which...companies based in other Member States must have to establish themselves in France either through a subsidiary or a branch.... It constitutes an inducement to choose to set up a subsidiary so as to avoid the disadvantage resulting from the refusal to grant the benefit of the shareholders' tax credit. [para 11]

It must be stated firstly that Article 52 [now 49]...embodies one of the fundamental principles of the Community and has been directly applicable in the Member States since the end of the transitional period. By virtue of that provision, freedom of establishment for nationals of one Member State on the territory of another includes the right to take up and pursue activities...and to set up and manage undertakings under the conditions laid down for its own nationals by the law of the country where such establishment is effected. The abolition of restrictions on freedom of establishment also applies to restrictions on the setting up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State. [para 13]

Article 52 [49] is thus intended to ensure that all nationals of Member States who establish themselves in another Member State, even if that establishment is only secondary, for the purpose of pursuing activities there...receive the same treatment as nationals of that State and it prohibits, as a restriction on freedom of establishment, any discrimination on grounds of nationality resulting from the legislation of the Member State. [para 14]

No valid justifications were found by the Court.

#### **4.4.6.5 *Lasteyrie du Saillant***

This case and the following case examined (*National Grid Indus*) deal with 'exit' taxes imposed by a Member State on individuals or companies that move their residence or legal seat to another

Member State. Where a taxpayer leaves a jurisdiction and takes up tax residence in another jurisdiction on a long-term or permanent basis, the first jurisdiction will typically levy a tax charge on capital gains that have accrued but not yet been realised during the taxpayer's period of residence in that jurisdiction. The rationale behind this is unobjectionable in principle. Most jurisdictions tax residents on worldwide income and gains ('residence' basis) but non-residents only on income and gains arising in the jurisdiction ('source' basis). In such cases, if a taxpayer ceases to be resident in a jurisdiction it is likely that that jurisdiction will lose any future taxing rights over the taxpayer's income or gains, other than from sources within the jurisdiction. Where a taxpayer leaves a jurisdiction on a long-term or permanent basis, it is not unreasonable for the jurisdiction to seek to tax the element of the gain that accrued during the taxpayer's period of residence there. The principle applies to income much more rarely as, unlike capital gains, most jurisdictions tax income as it accrues rather than only when it is paid.

The facts in *Lasteyrie du Saillant* were that an individual who was French resident and owned 25% of the shares in a French company wanted to transfer his residence to Belgium. French tax law imposed in such a case a charge based on the difference between the market value of the shares at the time of emigration and their original cost. Although it was possible to defer payment of this tax charge, this was subject to very strict conditions and the provision by the taxpayer of a guarantee. After five years the debt would be waived.

The taxpayer claimed that the French tax rule breached his right of freedom of establishment.

The Court found in favour of the taxpayer. *Lasteyrie du Saillant* was the first of the Court's decisions on exit taxes. Not all of the principles referred to by the Court originated in *Lasteyrie du Saillant* itself but were derived from earlier non-tax exit cases.

The Court started by making clear that the freedom of establishment provisions applied to movements from a Member State as well as to movements to it:

Although the freedom of establishment provisions are aimed particularly at ensuring that foreign nationals are treated in the host Member State in the same way as nationals of that State, they also prohibit the Member State of origin from hindering the establishment in another Member State of one of its own nationals. [para 42]”

“A restriction on freedom of establishment is prohibited...even if of limited scope or minor importance. [para 43]

The Court then considered the application of the freedom to tax provisions:

The prohibition on Member States establishing restrictions on the freedom of establishment also applies to tax provisions. Even though direct tax does not fall within the scope of the Community’s jurisdiction, Member States must nevertheless exercise their retained powers in compliance with Community law. [para 44]

Even if the national provision in question does not actually prevent the taxpayer exercising his freedom of establishment, it is enough to engage the freedom if the effect of the provision is such that is prone to restrict the exercise of that right by having at least a dissuasive effect on taxpayers wishing to establish themselves in another Member State. [para 45]

The tax provision in question, by subjecting a taxpayer who wishes exercise his freedom to transfer his tax residence to another Member State to tax on unrealised gains, as compared to a taxpayer who remains in France and is only taxed when the assets are realised, is likely to discourage a taxpayer from carrying out such a transfer. [para 46]

Even if there is a possibility of suspension of the payment, the conditions of such suspension may have a restrictive effect if they impose strict or onerous conditions, in particular the provision of a guarantee. Such guarantees in themselves constitute a restrictive effect in that they deprive the taxpayer of the enjoyment of the assets given as a guarantee. [para 47]

In light of the above, the provision in question is liable to hinder the freedom of establishment. [para 48]

As to justifications:

A measure liable to hinder the freedom of establishment can only be justified if it pursues a legitimate objective compatible with the Treaty and is justified by imperative reasons in the public interest. Furthermore, the measure must be appropriate to ensuring the attainment of the objective and must not go beyond what is necessary to attain it. [para 49]

The measure could be justified by the aim of preventing tax avoidance, but the measure in question was not proportionate to achieving that aim. It was not targeted at purely artificial arrangements but applied generally in any situation where a taxpayer with a substantial shareholding transferred his residence outside France for whatever reason. [para 50]

The transfer of a physical person's tax residence outside the territory of a Member State does not of itself imply tax avoidance and cannot justify a measure which compromises the exercise of a fundamental Treaty freedom. [para 51]

The objective of preventing a taxpayer temporarily transferring his residence before selling securities with the aim of avoiding French tax could be achieved by measures less restrictive or coercive, for example a tax charge if the taxpayer returns to France after a relatively brief stay in another Member State. [para 54]

Diminution of tax receipts cannot be regarded as a matter of overriding general interest which may be relied on as a justification of a measure contrary to a fundamental freedom. The mere loss of tax receipts because a taxpayer has moved his tax residence to another Member State cannot in itself justify a restriction on the right of establishment. [para 59]

Whilst the cohesion of the tax system can be a valid justification in some circumstances, the Court rejected it in this case on the grounds that that the justification of coherence could only succeed where the measure in question was aimed at ensuring that there was a symmetry between the tax

treatment of receipts and payments [paras 61-67]. The fact that after five years the tax suspended would be waived ran counter to any claim by France that the measure was justified on cohesion grounds.

As regards the justification of the balanced allocation of taxing powers, the Court observed that the matter at issue did not in fact concern the allocation of taxing power between Member States at all.

#### **4.4.6.6 *National Grid Indus***

This was a landmark decision in relation to exit taxes. First, it put beyond doubt that the principles in *Lasteyrie du Saillant* also applied in the case of companies. Secondly, it was the case that prompted a raft of infringement proceedings by the Commission.

The facts in brief were as follows. National Grid Indus ('NGI') was a company incorporated under Netherlands law. It transferred its place of effective management to the UK in 2000 and, in accordance with the Netherlands-UK double tax treaty, became tax resident solely in the UK with the consequence that it would in future be taxable solely in the UK. Dutch law imposed in such cases an exit tax on unrealised gains on the company's assets, which the company challenged on the grounds that it infringed its right to freedom of establishment.

The key points from the Court's judgment were as follows.

- NGI could rely on rights under Article 49 by virtue of Article 54. [para 32]
- An exit charge was a prima facie breach of Article 49 was clear from previous case law. [para 35]
- That such a charge could be justified on the grounds of balanced allocation of taxing powers had also been established in previous cases. It was reasonable for a Member State to seek to tax unrealised gains that had accrued during the time that a taxpayer had been resident/established in that State if the taxpayer moved their residence/establishment to another Member State. [para 46]

- The Dutch exit charge was appropriate for ensuring the preservation of the allocation of powers of taxation between the Member States concerned notwithstanding that it taxed gains before they had in fact been realised. [paras 48-49]

The Court then turned to the question of proportionality.

- A distinction was made between establishing the amount of the tax and its collection. Establishing the tax at the time the company transfers its place of effective management was regarded as proportionate. [paras 51-52]
- It was not necessary from the viewpoint of proportionality for the Dutch exit tax provision to take into account decreases in the value of assets following emigration. One of the reasons given by the Court for this conclusion was that to require the former State to take into account subsequent decreases in value ran counter to the principle of the balanced allocation of taxing powers. [paras 53-64]

After a review of the pros and cons of various methods of payment and deferral, the Court concluded that:

...national legislation offering a company transferring its place of effective management to another Member State the choice between, first, immediate payment of the amount of tax, which creates a disadvantage for that company in terms of cash flow but frees it from subsequent administrative burdens, and, secondly, deferred payment of the amount of tax, possibly together with interest in accordance with the applicable national legislation, which necessarily involves an administrative burden for the company in connection with tracing the transferred assets, would constitute a measure which, while being appropriate for ensuring the balanced allocation of powers of taxation between the Member States, would be less harmful to freedom of establishment than the measure at issue.... If a company were to consider that the administrative burden in connection with deferred recovery was excessive, it could opt for immediate payment of the tax. [para 73]



As regards guarantees, which were held disproportionate in *Lasteyrie du Saillant*, the Court stated:

However, account should also be taken of the risk of non-recovery of the tax, which increases with the passage of time. That risk may be taken into account by the Member State in question, in its national legislation applicable to deferred payments of tax debts, by measures such as the provision of a bank guarantee. [para 74]

The Court gave no reason as to why it might be prepared to accept a guarantee in a case like this when it had considered a guarantee disproportionate in *Lasteyrie du Saillant*. Possibly the artificial nature of a corporate entity and the fact that it could be wound up in the same way as it was created was an influencing factor. The absence of clarity on the point leaves some doubt as to whether the Court would still find the requirement of a guarantee unacceptable in the case of an individual.

As to justifications, the Court considered observations submitted by a number of Member States that the Dutch measure could also be justified on the grounds of the coherence of the tax system [para 79]. The Court concurred with the AG's observation that the requirements of coherence of the tax system and the balanced allocation of powers of taxation coincide [para 80]. Whether this meant that they coincided in this particular case or that they should be regarded as coinciding in every case is not clear. The Court considered that whilst determination of the amount of tax liability might be justified on the grounds of cohesion of the tax system, a requirement for the immediate payment of the tax was not proportionate [paras 81-82].

As to submissions that the Dutch exit charge was justified by the risk of tax avoidance, the Court restated the principle established in previous cases that the mere fact that a company transfers its place of management to another Member State cannot set up a general presumption of tax avoidance and justify a measure which compromises the exercise of a fundamental freedom guaranteed by the Treaty.

The Court concluded that legislation of a Member State which prescribes the immediate recovery of tax on unrealised capital gains relating to assets of a company transferring its place of effective management to another Member State at the very time of that transfer is disproportionate.

Two subsequent cases in which the principles established in *National Grid Indus* were applied are *DMC*<sup>164</sup> and *Verder*<sup>165</sup>.

In *DMC*, a reorganisation involving German and Austrian entities gave rise to a tax charge in Germany on unrealised capital gains on the basis that whereas before the reorganisation a disposal of the assets in question would have been liable to German capital gains tax a disposal of the assets after the reorganisation would not. The question for the Court was whether the German tax charge on unrealised gains could be justified. The case was dealt with under Article 63 on the grounds that the legislation in question primarily concerns the transfer of assets rather than the procedure for establishment. The Court referred, *inter alia*, to its decision in *National Grid Indus*, and the principle applied therein that under the justification of the balanced allocation of taxing powers a Member State is entitled to tax the accrued but unrealised gains of a person who leaves that Member State if the Member State would lose all power to tax those gains in future. As to proportionality, the Court held that the German legislation did not go beyond what is necessary to attain the objective of preserving the balanced allocation of taxing power, and in particular that it allowed the taxpayer to opt to spread payment of the tax over five years without interest with a bank guarantee only being required where there could be shown to be actual risk of non-payment.

In *Verder*, another case involving German taxes, a German company transferred assets to a branch in the Netherlands and accrued but unrealised gains on the assets were subjected to a German tax charge, which the taxpayer could elect to pay over ten annual instalments without interest. As in *National Grid Indus* and *DMC*, the justification of the measure on the grounds of the balanced allocation of taxing powers was accepted by the Court. As to proportionality, the Court referred to

---

<sup>164</sup> Case C-164/12 *DMC Beteiligungsgesellschaft mbH v Finanzamt Hamburg-Mitte* ECLI: EU: C: 2014: 20.

<sup>165</sup> Case C-657/13 *Verder LabTec GmbH & Co KG v Finanzamt Hilden* ECLI: EU: C: 2015: 331.

its decision in *DMC* in which it had considered a five year period for payment to be proportionate, so it followed that the ten year period allowed under the legislation in question in *Verder* must also be proportionate.

The cases demonstrate in particular the rigour with which the Court examines Member States' exit tax provisions in the context of proportionality.

Finally in the context of exit taxes, it may be noted that exit taxes are one of the core areas addressed in the Anti-Tax Avoidance Directive examined in section 6.3. The provisions of the Anti-Tax Avoidance Directive on exit taxes represent a codification of the Court's case law on the subject. The Directive envisages that Member States will amend their exit tax provisions as necessary to bring them into line with the minimum standards set out in the Directive, with, presumably, the result that fewer and fewer exit tax cases will come before the Court in future.

#### **4.4.6.7 *Commission v Spain***

This case arose from infringement proceedings brought by the Commission. A Spanish tax rule that exempted individuals from income tax on winnings from lotteries, etc, organised by certain Spanish public bodies and charities but did not exempt such winnings from similar bodies established in other Member States was challenged on the grounds that it constituted a restriction on the freedom of those non-Spanish bodies to provide services in Spain, eg, the sale of lottery tickets.

Not surprisingly, the Spanish rule was found by the Court to constitute a 'discriminatory restriction' (an interesting combination of discrimination and restriction terminology) on the freedom of public bodies and charitable entities established outside Spain to provide services in Spain.

The Court limited its ruling to those non-Spanish bodies and entities that were comparable to those that qualified for the exemption in Spain (ie, those of an essentially public or charitable nature), and did not extend it as the Commission had wanted to any entities running lotteries and the like.

The court stated that:

...to the extent that a restriction, such as that at issue in the present case, is discriminatory [again note the use of restriction and discrimination language in the same sentence], it is compatible with Community law only if it is covered by an express derogating provision...namely, public policy, public security or public health. [para 37]

The Spanish government claimed that the measure fell into the Treaty derogation for the protection of public health on the grounds that it helped to combat addiction to gambling. The Court wryly observed that Spain 'had adduced no evidence capable of establishing that, in Spain, such an addiction had reached the point amongst the population at which it could be considered to constitute a danger to public health [para 40]'.

The Court might also have added that making lottery winnings tax free would if anything encourage the public's propensity for gambling rather than diminishing it.

#### **4.4.6.8 *Eurowings***

Eurowings was a German charter flight operator that leased an aircraft from an Irish company. In computing its liability to German trade tax Eurowings was obliged to include in the tax base 50% of asset lease payments plus the value of the leased asset if the lessor was not liable to German trade tax. Given that the Irish company was not liable to German trade tax, this substantially increased Eurowings' trade tax liability compared with what would have been the case had it leased the aircraft from a German lessor.

The issue before the Court was whether such a rule was contrary to the freedom to provide services.

The Court noted as a matter of settled law that the freedom to provide services confers rights not only on the provider of services but on the recipient [para 34].

The German rules were found to result in a difference in treatment based principally on the residence of the service provider, which had the effect of dissuading German businesses from leasing assets other than from German lessors [paras 36-37]. Such a difference in treatment based on the

place of establishment of a provider of services was prohibited by the freedom to provide services [para 40].

The German government claimed justification on the basis of cohesion of the national tax system, specifically that where the asset leased from a German lessor the fiscal advantage for one person (the German lessee, in not having to include the lease payments and asset value in its tax base for trade tax purposes) was offset by a fiscal disadvantage to another person (the German lessor, that had to pay trade tax). The claim was rejected by the Court on the grounds that it was settled law that for a fiscal cohesion justification to be accepted there must be a direct link between the fiscal advantage and disadvantage, ie, they must accrue to the same person, which in this case they clearly did not [paras 41-42]. Similarly, a claim that the measure was justified by the offsetting of other advantages (in this case the favourable Irish 'Shannon privileges' tax regime to which the lessor was subject) was rejected on the basis that 'it was settled case law that any tax advantage resulting for providers of services from the low taxation to which they are subject in the Member State in which they are established cannot be used by another Member State to justify less favourable treatment in tax matters given to recipients of services established in its territory and that, as the Commission had rightly observed, such compensatory tax arrangements prejudice the very foundations of the single market.' [paras 43-45].

#### **4.4.6.9 *Manninen***

An illustration of the Court's approach to direct tax and the free movement of capital (Article 63) is afforded by *Manninen*. The facts of the case are relatively simple, but as is often the case the application of the legal principles is not straightforward. *Manninen* was a Finnish resident who owned shares in a Swedish quoted company (a small portfolio investment not giving him a definite influence over the Swedish company, hence the case was considered solely in relation to what is now Article 63). The Swedish company paid dividends on the shares to *Manninen*. The Finnish tax rules were that a Finnish resident individual was liable to Finnish tax on dividends whether these were received from Finnish or non-Finnish companies, ie, in respect of dividend income he was a 'fully

taxable person' in Finland (an expression that is often employed in the Court's direct tax jurisprudence, indicating that the person is liable to tax in their jurisdiction of residence on the whole of their income, whether arising in the jurisdiction residence or overseas). However, in the case of dividends received from Finnish companies Finnish law allowed the individual to set off an 'imputation' credit against his tax liability in recognition of the fact that the Finnish company had already paid corporate tax on the profits out of which the dividends were paid. No such imputation credit was available, however, in respect of dividends received from non-Finnish companies, notwithstanding the fact that they too would have paid corporate tax in their home States on the profits out of which the dividends were paid. The result was that a Finnish individual invariably suffered a higher tax burden on dividends from investments overseas than on investments in Finnish domestic companies.

The Court firstly re-iterated the well-established principle that:

'...although direct taxation falls within their competence, the Member States must none the less exercise that competence consistently with Community law. [para 19]'

The Court recognised that the Finnish legislation had the effect of deterring fully taxable persons in Finland from investing their capital in companies established in another member State. Not only was there an impact on the Finnish investor, but the Finnish rules also had a restrictive effect as regards companies established in other Member States in that it constituted an obstacle to their raising capital in Finland, as investing in their shares would be less attractive to a Finnish investor than investing in domestic companies. [para 22-23]

It followed from the above that legislation such as that at issue constitutes a restriction on the free movement of capital which is, in principle, prohibited by Article 63. [para 24]

The Court then turned to the question of whether the restriction could be justified, bearing in mind that Article 58(1)(a) [now 65(1)(a)] permits 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...the

place where their capital is invested'. The Court noted that Article 58(1)(a) [now 65(1)(a)], as a derogation from the fundamental principle of the free movement of capital, must be interpreted strictly and cannot be interpreted as meaning that any tax legislation making a distinction between taxpayers by reference to the place where they invest their capital is automatically compatible with the Treaty and that the derogation in Article 65(1)(a) is itself limited by Article 65(3) 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. [paras 25-28]' It is in light of this very restrictive interpretation of Article 65(1)(a) by the Court that the derogations it contains are regarded by some commentators as virtually worthless.

The Court found that:

A distinction must be made between unequal treatment which is permitted under Article 65(1)(a) and arbitrary discrimination which is prohibited by Article 65(3). In that respect the case law shows that, for national tax legislation like that at issue, which in relation to a fully taxable person in the Member State concerned makes a distinction between revenue from national dividends and that from foreign dividends, to be capable of being regarded as compatible with the Treaty provisions on the free movement of capital, the difference in treatment must concern situations which are not objectively comparable or be justified by overriding reasons in the general interest, such as the need to safeguard the cohesion of the tax system. In order to be justified, moreover, the difference in treatment between different categories must not go beyond what is necessary in order to attain the objective of the legislation. [para 29]

The next step was to apply a comparability test. The comparators chosen were, not surprisingly: (1) a shareholder fully taxable in Finland who receives dividends from companies established in Finland; and (2) a similar shareholder who receives dividends from companies established in other Member States. The comparison had to be made in light of the object and purpose of the Finnish legislation, viz, to mitigate double taxation (ie, the tax paid at company level on the profits and the tax payable

by the recipient of the dividends that were paid out of those taxed profits) on dividends received. The Court found that 'In the face of a tax rule which takes account of the corporation tax paid by a company in order to prevent double taxation of the profits distributed, shareholders who are fully taxable in Finland find themselves in a comparable situation, whether they receive dividends from a company established in that Member State or from a company established in Sweden.' [paras 32-36]

The Court considered, but rejected, a number of possible justifications. To mention just one, it was claimed by the Finnish government that granting a tax credit in respect of dividends the underlying company tax on which had been paid in a different Member State undermined the cohesion of the national tax system. This caused the Court some difficulty, but it drew attention to the Court's rulings in previous cases that for the justification of coherence of the national tax system to be accepted there had to: (a) be a tax advantage which is offset by a tax levy; and (b) that, furthermore, there had to be a direct link (to be examined in light of the objectives of the legislation) between the tax advantage in question and the offsetting of that advantage. In *Manninen* there appeared to be a tax advantage (the granting of a tax credit to Manninen) and a tax levy against which the advantage could be said to be offset (the tax paid by the companies on their underlying profits). However, the Court in previous cases<sup>166</sup> had ruled that there was no direct link where the situation concerned different taxes levied on different taxpayers, so given that the facts in *Manninen* were that the tax credit had been granted to Manninen in connection with the taxation of his dividends but tax had been paid by a different taxpayer (the Swedish company) on its underlying profits, the Court found that the requirement of direct linkage was not met so the claim for justification on the basis of the coherence of the national tax system must fail. The Court ruled that there was no justifiable reason why Finland could not grant a tax credit on the dividends from Sweden in the same way as it did for the dividends received from Finnish companies. The result seems somewhat unfair on Finland and it is noteworthy that in her preliminary opinion in *Manninen* AG Kokott had suggested that in situations like this (ie, a tax credit on dividends granted to a shareholder which was intended to

---

<sup>166</sup> Eg, Case C 251/98 *C Baars v Inspecteur der Belastingen* [2000] ECR I-02787, para 41.



offset corporation tax paid by a company on its underlying profits) a fiscal cohesion argument should be admitted. Clearly her suggestion was not followed by the Court, nor has it been to date in subsequent cases on the same theme.

*Manninen* is a good illustration of how difficult it can sometimes be to judge whether a national tax provision applies different rules to objectively similar situations. Firstly, the comparator, ie, the situations being compared, is not always as easy to find as it was in *Manninen*. Secondly, if it is determined that different rules are being applied to objectively similar situations (or the same rules to different situations), the question of whether any justifications apply and if so whether they are proportionate can often be extremely difficult and finely balanced. In *Manninen* the Court's decision on justification, especially that of cohesion of the national tax system, could easily have gone the other way.

#### **4.4.6.10 *Commission v United Kingdom***

This was an infringement proceedings case brought by the Commission against UK tax rules that subjected gains made by non-UK 'close' companies (broadly, companies controlled by five or fewer shareholders or by shareholders who are also directors) to immediate taxation in the hands of UK resident shareholders, whilst no corresponding rule subjected gains made by UK close companies to immediate taxation in the hands of their UK shareholders.

The question for the Court was whether the UK legislation constituted a restriction on the free movement of capital. The legislation applied only to shareholders holding more than 10% of the shares in the foreign company and could therefore apply both to holdings which gave their holder a definite influence over the decisions of the company and holdings which did not. The Court decided to consider the case on the basis of Article 63 in the first instance, reserving the possibility of also examining it in light of Article 49 if no breach of Article 63 was found [para 17].

The Court found that the UK legislation had the effect of discouraging UK residents from investing or contributing capital to non-UK close companies. The rules also had the effect of impeding such

companies from attracting investment from the UK. Both these factors meant that the legislation was a restriction to the free movement of capital [para 20].

The UK government claimed that the legislation was justified by the objectives of combating tax evasion and avoidance, but the Court noted that it was not targeted specifically at wholly artificial arrangements but applied to all gains made by non-UK resident close companies [para 25]. For this reason the measure went beyond what was necessary to attain the objective of combating tax evasion and avoidance and could not be accepted [para 26]. The Court also observed that the legislation did not give UK shareholders a possibility of justifying to the UK tax authority that there was economic and commercial substance behind the establishment of the offshore companies, in which case the restriction went beyond what was necessary to achieve an objective of combating tax evasion and avoidance and so could not be justified [para 27]. The Court's remarks suggest that had the UK rules given taxpayers an opportunity to demonstrate that there was commercial substance behind the establishment of the non-UK close companies the Court might have accepted a justification based on an objective of combating tax evasion and avoidance even if the legislation had not been expressly directed against 'wholly artificial arrangements'.

Although the UK changed the relevant legislation in 2013 in anticipation of the Court's ruling, there is still some doubt as to whether in its current incarnation it is fully EU law compliant.

#### **4.4.7 Case law conclusions**

Absent the Member State unanimity needed to pass directives concerning direct taxes and without a fundamental structural change in the way that the EU makes law in this area, the Court is left as the only source of 'hard' law in the direct tax field (leaving to one side the Commission's application of its State aid powers). The consistent trend of the Court's judgments seems to be to extend the application of the treaty freedoms, hardly ever to restrict or rein them in.

The Commission makes no secret that one of its most fundamental roles is that of promoting European integration and the single market. A word about the Court itself as an institution is appropriate here. In an article written in 2010,<sup>167</sup> Michelle Everson wrote:

...the ECJ has historically established itself as a court with constitutional character and, in common with all constitutional courts, has always trodden a very thin line between the 'legitimate' legal-constitutional politics of the establishment of principles of social and political organisation and the 'illegitimate' personal-judicial pursuit of substantive political programmes.

The vital difference now is that whereas a cadre of European judges drawn from experienced national judiciaries was once, for all its pro-European activity, always very careful to limit the impacts of European law upon the cores of national life...today a younger, and more ruthlessly European ECJ – trained carelessly, as I was, in the supremacy of European law – seems far happier to emphasise the lowest common denominator of European legal integration: the assertion of market over social rights, or the pursuit of a neo-liberal notion of economic justice ('allocative efficiency').

One of the areas considered by Michal Bobek in a wide-ranging paper<sup>168</sup> was the legitimacy of the Court. According to Bobek 'There is hardly any other issue relating to the operation of the Court of Justice of the EU and the ECJ in particular that would give rise to such heat and passion: the legitimacy of what the ECJ has been doing and how it has been doing it'<sup>169</sup> He refers to the '...certain 'pro-Union' interpretative tendency in the reasoning of the ECJ'<sup>170</sup> and that 'Stated in very simplistic

---

<sup>167</sup> Michelle Everson, 'Is the European Court of Justice a Legal or Political Institution Now?', *The Guardian*, 10 August 2010. Available online at: <<https://www.theguardian.com/law/2010/aug/10/european-court-justice-legal-political>> accessed 17 May 2018.

<sup>168</sup> Michal Bobek, 'The Court of Justice of the European Union', College of Europe, Research Paper in Law, 02/2014.

<sup>169</sup> *ibid*, section V, para 1 at p16.

<sup>170</sup> *ibid*, section V, para 4 at p16.

terms, the ECJ is said to favour the interpretative approach and outcome that enhance further integration<sup>171</sup>.

Bobek claims that applying sweeping purposive reasoning that favours unity and effective enforcement of EU law can give rise to particularly acute problems in areas such as criminal law, tax law, or administrative sanctions where the need for clarity and foreseeability normally calls for caution and restrictive interpretation<sup>172</sup>.

He concludes that:

At the root of the social legitimacy of courts is arguably their impartiality: a court is called to decide because it is the independent third. That is why it was created and that is also why disputes keep being submitted to it. Can, however, a 'biased' institution be called a court? The legitimacy debate shifts its focus from the method to its outcomes. The chief challenge becomes not (just) that the ECJ is perceived to have stepped over the boundaries of 'proper' judicial reasoning, but that it does so instrumentally and asymmetrically in one and only one direction: to further enhance integration. [section V, para at pp 18-19]

It has been said that what matters to the European Court is not the law but to advance a 'certain idea of Europe' and nothing must stand in the way of that<sup>173</sup>. I do not think that an objective evaluation of the Court's judgments would support quite such an extreme position, but I do gain the sense that where they reasonably can the Court will promote the integrationist agenda even at the expense of occasionally sacrificing intellectual rigour and consistency.

From the early beginnings with *Avoir Fiscal* in 1986 references from national courts gathered pace through the 1990s and beyond. The Court, with the benefit of the judicial activism of a number of its judges, such as Melchior Wathelet (Belgium) and David Edward<sup>174</sup> (UK) to name but two, asserted

---

<sup>171</sup> *ibid*, section V, para 4 at p17.

<sup>172</sup> *ibid*, section V, para 7 at p17.

<sup>173</sup> Bernard Connolly, *The Rotten Heart of Europe* (Faber 2013).

<sup>174</sup> See 'The European Court of Justice – Friend or Foe?', address by Judge David Edward 18 July 1996, cited in Mark Hoskins & William Robinson (editors) *A True European: Essays for Judge David Edward* (Hart Publishing 2003) at p268.

that treaty freedoms took priority over national tax systems that discriminated between nationals and non-nationals, residents and non-residents and between domestic and cross-border transactions, which at that time most national tax systems did as a matter of course. The intrusion of EU law into the direct tax sphere forced governments to take more note of these developments, to change their tax rules where required, and generally to become more engaged with the ongoing debate within the EU as regards national tax systems and the single market.

Can it reasonably be claimed that through the application of the Treaty fundamental freedoms the Court has the weapons it needs to strike down virtually any difference between Member States' tax rules? Certainly, the Court has not shown itself backward in using what weapons it does have available to promote an integrationist agenda, but however imaginatively it were to interpret the Treaty freedoms such a claim would be going much too far. Even if one subscribed to the theory that the Court will wherever possible promote an integrationist agenda, the fact is that it is severely limited in what it can achieve, principally because:

- the Court can only address a national tax rule if a reference is made to it by a national court or as a result of infringement proceedings brought against the Member State by the Commission; and
- the Court can only consider tax provisions that potentially contravene the Treaty freedoms or prohibition against discrimination.

The first of these limitations means that even a policy of 'tax harmonisation through the back door' were being pursued by the Court it would be long, slow, haphazard and piecemeal. Striking down individual national tax measures represents 'negative' integration as opposed to the 'positive' integration that would result, for example, from the Member States agreeing to a directive adopting a common set of rules in a particular area via a directive.

Given that certain types of national direct tax provisions have been known to be vulnerable to challenge for a considerable time now, it might be seen as surprising that so many of the cases that come before the Court are blatantly discriminatory or restrictive. One might wonder why Member

States have not corrected the more glaringly incompatible provisions of their tax codes by now instead of waiting until they come before the Court.

Ideally, when a national measure has been successfully challenged before the Court, other Member States with similar provisions would amend them so that they conform without waiting to be requested to do so by the Commission or taken to court by a taxpayer. In practice this rarely happens. Even the Commission has limited resources, and the costs of litigating are such that only those with the deepest pockets will be prepared to assert Treaty rights if there is a likelihood that the matter will have to be referred to the Court. Even after the Court has made a ruling, the matter will usually be referred back to the national court, which must consider the matter in light of the Court's sometimes less than entirely helpful or clear comments, then if changes to the Member State's rules need to be made the national legislature will need to consider it. The entire process can take many years. Thus measures will often remain in place in other Member States years after they were struck down in the case of another Member State. All in all this leads to a most unsatisfactory state of affairs and creates uncertainties for both taxpayers and national legislatures as to what is permitted and what is not and how long a non-conforming measure in a Member State is likely to continue.

The Commission's watching brief over national tax measures and its ability to institute infringement proceedings contributes to making the process a little less piecemeal and haphazard than it would be if cases were brought purely by taxpayers. For example, where a type of national measure is successfully challenged, the Commission will bring infringement proceedings against Member States with similar provisions. This happened, for example, with exit taxes and cross-border loss relief provisions.

The second limitation means that many national tax measures will fall outside the Court's jurisdiction provided they do not discriminate or constitute an unjustified restriction on the exercise of a Treaty freedom. The following, for example, are completely outside the scope of the Treaty freedoms (assuming that the Member State applies them without distinction to nationals and non-nationals and that they do not discriminate):

- rates of tax that are different to those of other Member States;
- methods of determining the tax base that are different to those used by other Member States; and
- tax reliefs and incentives that are different to those of other Member States.

For there to be a harmonised tax system in any meaningful sense matters as fundamental as these would have to be aligned, or at least aligned sufficiently to leave Member States with only a limited margin of discretion. The Court, however, is essentially powerless to intervene as far as these matters are concerned.

However creative the Court might be in interpreting the Treaty freedoms and, for example, in determining what are ‘comparable situations’, there seem to be many aspects of Member States’ tax systems that are simply outside its jurisdiction. This has given rise to a view amongst some commentators that the Court’s case law in the direct tax field has reached its high water mark<sup>175</sup> and that recent cases suggest more of a willingness to entertain justifications than hitherto. Perhaps the Court feels it has pushed the envelope far enough for the time being and is now more sensitive to the repercussions of its judgments politically and for the international tax system.

Whether or not that is the case, the possibility of some surprising developments in the future should not be ruled out. The Court has consistently shown itself willing to break new ground and extend the application of the freedoms in ways and to subjects that might have seemed inconceivable when the

---

<sup>175</sup> In a review of Rosemary Healy-Rae, Frank Barry & Donal de Buitelir, *Who’s Afraid of the ECJ: Implications of the European Court of Justice Decisions on Ireland’s Corporation Tax Regime* (Institute of Taxation in Ireland 2007), Aidan Walsh, tax partner with Ernst & Young, concurred with the view expressed in the book that by the time of the *Marks & Spencer* judgment of 2005, in which contrary to all previous cases the Court accepted the UK government’s defence that its cross-border loss rules were necessary to defend coherence of its tax system and to prevent tax avoidance, the high water mark of the ECJ’s activism in the corporate tax arena had already passed [Aidan Walsh, ‘Who’s Afraid of the ECJ – Not Ireland Any More!’, *Finance Magazine*, August 2007, para 5, available online at: <[http://www.finance-magazine.com/display\\_article.php?i=7667&pi=271](http://www.finance-magazine.com/display_article.php?i=7667&pi=271)> accessed 21 May 2018. That *Marks & Spencer* marked a turning point is also the view of Miroslav Jovanovic, *International Handbook on the Economics of Integration* (Vol II, Edward Elgar Publishing 2011), pp460-461, in which he referred to some 2004 Court decisions with the comment ‘These...decisions seemed to imply that within the single market, taxpayers were entitled to relief from legal and economic double taxation on their foreign income from capital the same way as they were entitled to such relief on their domestic source income from capital. If that principle could be implemented in case law it would be an important step towards cross-border integration of tax systems’.

fundamental freedoms were first applied to direct taxes only 30 years ago. It is this judicial activism, a willingness to break new ground in pursuance of the single market agenda, which makes the question of how much the Court can contribute towards achieving direct tax harmonisation such a live and intriguing one.

In some areas the Court's case law far outstrips advances in legislation at EU level. For example in the area of cross-border loss relief, in connection with which a draft directive was published but never implemented. In the long-running *Marks & Spencer*<sup>176</sup> litigation the Court found the UK's corporate tax group relief rules that prohibited the offset by a UK company of losses incurred by its foreign subsidiaries to be contrary to the freedom of establishment. The UK amended its group relief provisions a number of times until finally the Court was satisfied with the UK's position that losses of foreign subsidiaries must be deductible against the UK parent company's profits where there was no possibility of the foreign subsidiary being able to make use of those losses either now or the future. This went well beyond what had been proposed in the draft directive.

In the last chapter of this work I consider to what extent the Court's case law might be said to have contributed towards the overall process of direct tax harmonisation.

An unintended, and somewhat ironic, consequence of all this judge-made law is as one commentator observed<sup>177</sup> that the EU's supranational legal system, originally modelled on codified Romano-Germanic systems, has come more to resemble a common law system.

---

<sup>176</sup> Case C-446/03 *Marks & Spencer plc v Halsey* [2005] ECR I-10837.

<sup>177</sup> Franco Roccasalata, in the foreword to Luca Cerioni, *The European Union and Direct Taxation* (Routledge 2015) p xi.



## **AN ALTERNATIVE TO THE NEED FOR UNANIMITY - ARTICLE 116?**

### **5.1 The imperative for an alternative legal basis**

As explained in the section on competence, there is no legal basis for EU legislative action that refers specifically to direct tax. The legal basis employed thus far for direct tax legislation has been Article 115. Article 115 is the legal basis for the approximation of Member States' laws, regulations or administrative provisions that directly affect the establishment or functioning of the internal market. By contrast Article 116 is the legal basis for eliminating Member States' laws, regulations or administrative provisions that distort the conditions of competition in the internal market.

A critical difference between the two is that Article 115 requires unanimity under a special legislative procedure whilst Article 116 only requires qualified majority voting under the ordinary legislative procedure. The difficulties that the Commission faces in obtaining the unanimity required to implement direct tax legislation under Article 115 would make Article 116 a most attractive alternative if it were legally and politically feasible.

### **5.2 Direct tax – an internal market or a competition issue?**

There is no doubt that Article 115 is the proper legal basis for EU direct tax legislation the primary purpose of which is to facilitate or improve the establishment or functioning of the internal market. Few would dispute that the subject matter of the Parent-Subsidiary and Mergers Directives, and the pending directive on double taxation dispute resolution mechanisms falls into this category. The subject matter of the Interest and Royalties Directive would also seem to fall readily into this category, notwithstanding it was introduced as part of a 2003 'package to tackle harmful tax *competition*' (my italics). Quite why the Interest and Royalties Directive was branded as a

competition measure is unclear, since in terms of content it aims to achieve broadly the same results (the elimination of double taxation) as the Parent-Subsidiary Directive did on profit distributions between subsidiary and parent companies.

The two Mutual Assistance Directives and the Savings Directives are more difficult to categorise. Their primary purpose lies in combatting tax evasion, which is not obviously a matter that “directly affects the establishment or functioning of the internal market”. Nevertheless Article 115 was used as their legal basis. Article 116 would have been an even less appropriate basis, however, as by no stretch of the imagination could the Mutual Assistance Directives be said to be addressing matters that are “distorting the conditions of competition in the internal market”.

It is doubtful to what extent the Anti-Tax Avoidance Directive and the proposed CCCTB directives deal with matters that “directly affect the establishment or functioning of the internal market”, but Article 115 was used as the legal basis for the first and is proposed to be used as the legal basis for the latter. There is an argument that these directives, perhaps particularly the CCCTB directives, are more aimed towards tackling ‘harmful’ tax competition than enhancing the establishment or functioning of the internal market and that their proper legal basis should therefore be Article 116.

Whilst it may seem a matter of semantics which legal basis is the most appropriate for a particular directive and given that directives are the appropriate form of legislation for both Articles 115 and 116, the critical difference between the two is the voting procedure.

Article 113, the legal basis for the harmonisation of indirect tax legislation, used to refer only to harmonisation necessary to ensure the establishment and functioning of the internal market.

Interestingly, the Lisbon Treaty amended Article 113 so that it now refers to harmonisation necessary to ensure the establishment and functioning of the internal market *and to avoid the distortion of competition* [my italics]. Presumably no similar change was deemed necessary to Article 115 as together with Article 116 both the internal market and competition bases are covered.

An increasing number of the Commission's pronouncements relating to direct tax over recent years have referred to the distorting effects of tax competition, especially 'harmful' tax competition. In fact concerns about the effects of direct tax disparities on competition seem to have displaced the previous emphasis on their effect on the functioning of the internal market. Significantly, the internal market was defined in the Lisbon Treaty as '...including a system ensuring that competition is not distorted'.<sup>178</sup>

As well as the Commission's comments linking tax with competition, the fact that a Member State's tax measures can distort the conditions of competition is expressly recognised in the application of the State aid provisions. Article 107(1) provides that the State aid provisions apply to aids which distort or threaten to distort competition. The State aid provisions have for some time been applied by the Commission to aid in the form of tax measures. On one view the application of the Treaty State aid provisions to tax measures may be seen as 'official' acknowledgment that tax measures can and do distort the conditions of competition.

### **5.3 Article 116 – politics or legal principles?**

Given this apparent recognition on the part of the Commission that disparities in the Member States' tax systems can and do create distortions of competition, why does the Commission not seek to apply the more appropriate legislative basis of Article 116 to at least some of its tax proposals and by doing so break the impasse (the need for unanimity) produced by its continued reliance on Article 115?

The answer is presumably more to do with politics than legal principles. Most commentators seem to see nothing in principle in using Article 116 for direct tax. For example:

There is another general legal basis for harmonisation under Article 116, which could be used for legislative action when differences in Member State laws are distorting the conditions of

---

<sup>178</sup> Protocol (No 27) on the internal market and competition [2008] OJ C115/309, annexed to both the TEU and TFEU.

competition in the internal market. Although this legislative base does not require unanimity and does not exclude direct tax measures, it has never been used for tax harmonisation purposes<sup>179</sup>.

Article 116 concerning market distortions caused by disparities, allows qualified majority adoption of directives necessary for the elimination of such market distortions. This is also true for distortions caused by disparities in national tax laws or administrative practices.

Article 116 would seem the obvious legal basis for dealing with harmful tax competition, as excessive policy competition by definition is a market distortion through deliberate creation of disparities<sup>180</sup>.

Article 116 offers another legal base for legislative action when differences between national laws distort the conditions of competition in the internal market and, unlike Article 114(2), it does not exclude tax measures. Accordingly, Article 116 provides a further base for EU legislation in the direct taxation area too, although it has not been used to date<sup>181</sup>.

Arguably, much of the Code of Conduct on Business Taxation, aimed as it is at removing competitive distortions, could and should have been the subject of a legislative proposal under the legal basis of Article 116 rather than a piece of non-binding soft law. Judging from the Commission's continuing expressions of concern about 'harmful' tax competition, it may be surmised that it is no longer very satisfied with the 'gentleman's agreement' status of the Code of Conduct. If harmful tax competition is only harmful because it distorts the conditions of competition in the internal market, surely the legally most appropriate way of dealing with it is by legislation through the Article 116 procedure. As the Commission has not itself made any statement concerning the use or non-use of Article 116 for tax measure beyond its occasional reassurances that direct tax measures require unanimity, one can only speculate as to the reasons. The most likely is that it would be too politically explosive, given

---

<sup>179</sup> Christiana Panayi, *European Union Corporate Tax Law* (Cambridge University Press 2013) p4.

<sup>180</sup> Panos Koutrakos & Jukka Snell (editors) *Research Handbook on the Law of the EU's Internal Market* (Edward Elgar Publishing 2017) p319.

<sup>181</sup> Luca Cerioni, *The European Union and Direct Taxation* (Routledge 2015) p20.

the number of reassurances the Commission has given over the years that unanimity is required for direct tax legislation (implying that Article 115 will continue to be the sole legal base). Although it probably only gave such assurances for reasons of political expediency, they are nonetheless on the record. As mentioned elsewhere, the Commission has from time to time proposed a move to qualified majority voting for direct tax measures, which has been consistently rejected by the Member States. In light of these facts, any attempt now to employ a different legal basis which requires only qualified majority voting would appear to many to be deeply cynical, however well-founded it might be from a purely legal perspective.

Notwithstanding that there seems to be no legal impediment to employing Article 116 as the legal basis for direct tax legislation that has its primary focus on the elimination of competitive distortions, there appears to have been no serious indication so far on the part of the Commission that it will attempt to use Article 116 to sidestep the impasse.

That said, it would be rash to entirely rule out the possibility. Except on matters that are relatively uncontroversial, it seems to be becoming ever more difficult to obtain the unanimous approval of 28 Member States to a legislative measure without watering it down or granting the Member States so much leeway in its implementation that its effectiveness is substantially undermined. There may well come a point at which the Commission decides that enough is enough and that the need for action has become so imperative that they will look for radical ways to break the deadlock, in which circumstances past undertakings on unanimity may count for little, whatever the temporary political fallout might be. If this seems implausible, bear in mind that the fundamental freedoms were once never thought to apply to direct tax matters yet are now applied in that area as a matter of course.

## EU LAW AND ANTI-TAX AVOIDANCE

### 6.1 Background

Until around 30 years ago, it used to be almost universally accepted that whilst tax evasion (eg, deliberate concealment of income or assets or falsification of records) was illegal and potentially criminal, any other form of tax planning was perfectly legitimate, however aggressive, contrived or artificial it was. Today, the ground rules are very different. Evasion is still illegal and usually criminal, but tax avoidance has now been divided into that which is acceptable and that which is perceived as unacceptable or abusive and thereby susceptible to being struck down, either by courts, by targeted anti-avoidance rules in domestic legislation or bilateral double tax treaties, or by general anti-avoidance or anti-abuse rules ('GAARs'), which more and more countries are introducing. There is no clear dividing line as between what is categorised as acceptable and what is abusive, and indeed that line seems to shift depending on the political and public mood at the time. When considering entering into any tax planning arrangements, however seemingly innocuous, taxpayers must try and assess where the line might be at that particular moment.

In what follows I use the term tax avoidance to cover any type of tax planning that falls short of evasion.

### 6.2 EU's attitude and response to tax avoidance

From the earliest days of the EU's activities in the field of direct tax, the Commission's attitude towards the more egregious forms of tax avoidance has been hostile. The Court, on the other hand, has steadfastly refused to intervene where a non-discriminatory tax obstacle is simply the result of the parallel exercise by Member States of their taxing power<sup>182</sup>. Indeed the Court has struck down a

---

<sup>182</sup> Eg, Case C-128/08 *Jacques Damseaux v Belgium* [2008] ECR I-7735, paras 27 and 30.

number of national tax measures which Member States sought to justify on the grounds that they sought to combat tax avoidance unless they were narrowly targeted at arrangements that were ‘wholly artificial’ in substance, the usual ground for rejection being that if the measures could apply other than to wholly artificial situations they went beyond what was necessary to achieve the purported aim of the legislation and thereby failed the proportionality test<sup>183</sup>. This attitude of the Court’s makes framing anti-avoidance measures a very difficult task for the Member States.

The two Mutual Assistance Directives (exchange of information and recovery of claims) provide valuable assistance to national tax authorities in the fight against tax evasion and avoidance. They are primarily of an administrative nature, however. The other directives on direct tax matters that had been implemented prior to the adoption in July 2016 of the Anti-Tax Avoidance Directive had little in the way of anti-tax avoidance content. The July 2016 Directive is considered below.

In 2012 in the aftermath of the financial crisis the Commission issued a Recommendation on aggressive tax planning<sup>184</sup>, which it described as those strategies aimed at “taking advantage of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability”.

The Recommendation encouraged Member States to:

- amend the terms of their bilateral double tax treaties to eliminate situations where items of income are taxed in neither jurisdiction (‘double non-taxation’), or at the least to ensure that any bilateral treaties they enter into in future are drawn up on that basis; and
- include in their domestic legislation a General Anti-Abuse Rule (GAAR) which could strike down artificial arrangements put in place essentially for the purpose of avoiding tax. GAARs enable tax planning arrangements to be challenged in cases where no specific targeted anti-avoidance provision exists.

---

<sup>183</sup> A leading case in which this principle was established is Case C196/04 *Cadbury Schweppes plc, Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue* [2004] ECR I-07995, which concerned the UK’s controlled foreign companies rules. As a result of the Court’s decision the UK made substantial changes to those rules.

<sup>184</sup> Commission Recommendation of 6 December 2012 on aggressive tax planning [2012] OJ L338/41.

The Code of Conduct for Business Taxation, considered in the section on soft law, is aimed at 'harmful' tax measures adopted by Member States rather than at tax avoidance as such.

The real spur to the EU's efforts in dealing with tax avoidance came as a result of the combined G20/OECD Base Erosion and Profit Shifting ('BEPS') project. At their meeting in June 2012 the G20 tasked the OECD with producing an action plan, which was delivered in July 2013. The backdrop to the initiative was the widespread public and political condemnation of tax avoidance (particularly by multinationals) and the tax avoidance industry following the financial crisis that had broken a few years earlier. The most widely voiced complaint against the then existing international tax regime, which had developed since the 1920s and which had hitherto been accepted with only relatively minor reservations by virtually the entire international community, was that it was no longer fit for purpose; in particular that it did not do enough to prevent artificial tax avoidance and that its principles had been drawn up decades ago and were no longer an appropriate basis for taxing transactions in a global economy and in the digital age.

'Base erosion and profit shifting' is the terminology adopted by the OECD to cover the range of tax planning strategies typically used by multinational companies that exploit gaps in and mismatches between national tax systems to more or less artificially shift profits from higher tax jurisdictions to low or no-tax jurisdictions where little or no economic activity in fact takes place and, conversely, to move expenses to jurisdictions where they are tax relieved at a higher rate. According to the OECD: "While these corporate tax strategies may be technically legal and rely on carefully planned interactions of a variety of tax rules and principles, the overall effect of this type of planning is to erode the corporate tax base of many countries in a manner that is not intended by domestic policy<sup>185</sup>".

The OECD's action plan consisted of 15 points, taking apart brick by brick virtually the whole of the international tax system and making recommendations for change. Final reports on all 15 actions

---

<sup>185</sup> OECD, 'The OECD work on Base Erosion and Profit Shifting', 4 February 2013, p2. Available online at: <https://www.oecd.org/ctp/TheOECDworkonBEPS.pdf> accessed 17 May 2018.



were delivered by the end of 2015 – a remarkable achievement in such a short space of time. BEPS is now well into the process of practical implementation, with the recommendations being implemented by a combination of unilateral action by countries that had signed up to the project and certain other recommendations that are being implemented by way of a multilateral instrument that opened for signature at the beginning of 2017.

The BEPS project without doubt marks the biggest shake up in international tax for a century. The project was led, appropriately, by the OECD as the pre-eminent international body in the field of international tax and whose model double tax treaty and commentary is by far the most widely used by the international community. The G20 added political muscle and impetus.

There is a wide overlap between the initiatives set out in the Commission's 2012 Action plan against tax evasion and earlier soft law pieces. The Commission and the OECD had expressed largely the same concerns about fighting aggressive tax planning and eliminating gaps leading to double non-taxation as well as to risks of double taxation. The EU has positioned itself as one of the most enthusiastic champions of the BEPS recommendations and has taken the lead in procuring their adoption by Member States. It justifies this role on the not unreasonable premise that tax avoidance can best be tackled through international co-ordination rather than left to individual Member States, as the latter is likely to result in just the sorts of gaps and loopholes that sophisticated tax planners can exploit.

Shortly after the OECD completed the publication of its reports on the 15 BEPS actions at the end of 2015, the Commission issued a Communication<sup>186</sup> setting out a proposed anti-tax avoidance package. The package consisted of a number of elements, including the following:

---

<sup>186</sup> Commission, 'Communication of 28 January 2016 from the Commission to the European Parliament and the Council on an anti-tax avoidance package: next steps towards delivering effective taxation and greater tax transparency in the EU' COM(2016) 23 final.

- a Recommendation on tax treaty issues, providing advice to Member States on how to reinforce their tax treaties against abuse by aggressive tax planners in an EU law-compliant way<sup>187</sup>;
- a proposed amendment to the administrative co-operation directive [2011/16/EU] to implement country-by-country reporting<sup>188</sup>;
- a Communication on an external strategy for effective taxation, concerning the approach EU Member States should take towards third countries in matters of taxation with a view to promoting good governance and compliance with international standards<sup>189</sup>.

The principal component of the package, however, was a proposed anti-tax avoidance Directive, which is examined in the next section.

### 6.3 Anti-Tax Avoidance Directive

The primary output of the Commission's efforts is the Anti-Tax Avoidance Directive ('ATAD'), adopted on 12 July 2016 and amended in May 2017 at the request of ECOFIN to extend the scope of a number of its provisions, in particular those on hybrid mismatches to include situations involving the EU and third countries.

The ATAD lays down rules against tax avoidance practices that directly affect the functioning of the internal market. It is aimed at those practices in which taxpayers act against the spirit of the law and take advantage of disparities between national tax systems to reduce their tax liabilities. It builds on the OECD's BEPS recommendations and whilst most Member States have individually signed up to implementing the BEPS recommendations unilaterally, the ATAD will be a vehicle to ensure that the main BEPS recommendations are implemented in a consistent way across the Member States, including the six Member States that are not also members of the OECD. It should be noted that the

---

<sup>187</sup> Commission Recommendation of 28 January 2016 on the implementation of measures against tax treaty abuse [2016] OJ L25/67.

<sup>188</sup> The amendment was implemented via Council Directive (EU) 2016/881 of 25 May 2016 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation [2016] OJ L146/8.

<sup>189</sup> Commission, 'Communication of 28 January 2016 from the Commission to the European Parliament and the Council on an external strategy for effective taxation' COM(2016) 24 final.

provisions set out in the Directive are a minimum standard and Member States are free to implement stricter rules if they wish. The provisions of ATAD are to come into effect from 1 January 2019, with a later start date for some of the provisions that had been subject to amendment.

Core areas addressed by the ATAD include the following.

- Interest deduction limitation rule – a company or group’s net interest deduction for tax purposes is limited to 30% of its earnings before interest, tax, depreciation and amortisation (‘EBITDA’). A *de minimis* applies such that if the company’s/group’s net interest deduction is less than €3m the whole of the interest may be deducted. Whilst the rule contained in the ATAD is derived from the OECD’s BEPs recommendations on the subject (BEPS action 4), the BEPS recommendations set out parameters of a rather broad nature whereas the ATAD provisions are quite prescriptive, with little margin left to the Member States in terms of implementation and application. In particular, the ATAD rule is mechanistic in nature with no ‘motive test’ exemption for financing arrangements with a demonstrably commercial, as opposed to tax planning, purpose.
- Exit taxation – the provisions are a codification of the Court’s exit tax case law. Exit taxes are permitted when a taxpayer transfers residence or assets to another Member State or a third country, the charge being levied on the difference between the market value of assets at the time of transfer and their value for tax purposes (normally their cost). If the taxpayer transfers their residence or assets to another Member State (including EEA members), the taxpayer must be given the opportunity to pay the tax in instalments over a five year period. Interest may be charged on the outstanding instalments but the requirement for a guarantee may only be imposed by a Member State if there is a demonstrable and actual risk of non-recovery. In the event that the assets are disposed of or the taxpayer transfers their residence to a third country that is not an EEA member the outstanding instalments become payable in full. Exit taxes were not a matter considered by the OECD in its BEPS project.

- General Anti-Abuse Rule ('GAAR') – any non-genuine arrangement, ie, one that is not put in place for valid commercial reasons which reflect economic reality, carried out for the main purpose of obtaining a tax advantage that defeats the object or purpose of the otherwise applicable tax provisions, is to be ignored for the purposes of calculating the corporate tax liability. The GAAR does not affect the application of specific anti-abuse/anti-avoidance rules. The application of the GAAR should be limited to 'wholly artificial arrangements' (this stipulation was forced upon the framers of the Directive in order to make it consistent with the Court's case law in tax avoidance cases, though in practice it will severely handicap the GAAR's application – there are few arrangements that could not be given a veneer of commercial substance sufficient to defeat a GAAR expressed in such restrictive terms). Adoption of a GAAR was not a matter considered by the OECD BEPS project. Its inclusion in a package of tax avoidance measures makes sense, however, as it is almost impossible to frame a rule so prescriptively as to eliminate all possibility of tax planning being devised to circumvent it to some extent. A GAAR acts as a weapon of last resort so that even if some tax planning defeats the specific rules and any targeted anti-avoidance provisions the tax authority has the possibility of having the planning struck down on the grounds that it constitutes an abuse. It will be interesting to see how much of a handicap the requirement imposed by the Court's case law that the GAAR can only be applied in cases of 'wholly artificial arrangements' proves to be.
- Controlled Foreign Companies ('CFC's) – the tax base of a company shall include the undistributed profits of a CFC. A CFC is defined as a company in which: the taxpayer holds a participation of more than 50%; its profits are subject to an effective corporate tax rate lower than 40% of the applicable rate in the taxpayer's Member State; the company derives more than 50% of its income from passive or financial activities or from services provided to the taxpayer or other group members; and, the company is not tax resident in a Member State or EEA State. If the CFC subsequently distributes profits to

the taxpayer, these will not be taxed if they have already been taken into account under the CFC provisions. The ATAD CFC provisions are based on the recommendations in BEPS action 3 and are largely aligned with them.

- Hybrid mismatches – where two Member States give a different legal characterisation to the same taxpayer (making it a ‘hybrid entity’) and this leads to a deduction of the same payment, expenses or losses in both jurisdictions (a ‘double deduction’), or where there is a deduction of a payment in the Member State in which the payment has its source without a corresponding inclusion of the same payment (as income) in the other Member State, the legal characterisation given to the entity by the Member State in which the payment has its source, the expense is incurred or the losses are suffered shall be followed by the other Member State. Where two Member States give a different legal characterisation to the same payment (a ‘hybrid instrument’) and this leads to a deduction in the Member State in which the payment has its source without a corresponding inclusion of the same payment (as income) in the other Member State, the legal characterisation given to the hybrid instrument by the Member State in which the payment has its source shall be followed by the other Member State. The ATAD hybrid mismatches provisions are based on the recommendations in BEPS action 2, and again are largely aligned with them.

As noted above, there is nothing in the BEPS recommendations concerning exit taxes or a GAAR, so the inclusion of provisions on those subjects in the ATAD goes beyond what would have been needed had it been the aim of the Directive solely to implement BEPS recommendations on an EU-wide basis. It will be clear from the preceding content that the EU is seeking to combat tax avoidance in its widest sense and has at no point restricted itself to following only the areas covered by the BEPS program.

Note that the ATAD does not attempt to deal with the issue of ‘double non-taxation’, which is primarily a double tax treaty issue and which was addressed in the 2012 Recommendation on aggressive tax planning.

Some Member States, the UK for example, already have provisions in their laws that cover most of the areas set out in the ATAD, and for them it will simply be a matter of amending their existing provisions to make them ATAD-compliant. Other Member States are currently in the process of drawing up and implementing the necessary legislation in time for the 1 January 2019 start date (or later in the case of ATAD provisions which were amended, such as those on hybrid mismatches). As compared with the UK, some Member States are starting from a fairly low starting point and for those States implementation of the necessary legislation within the available timeframe is likely to be more challenging. Deloitte provides a comprehensive and periodically updated online resource analysing BEPS implementation (including ATAD in the case of EU Member States) country by country<sup>190</sup>.

Although the ATAD is expressed to be complementary to the relaunched CCCTB proposals, it is interesting to note that whilst the ATAD takes the traditional approach to the matter of excessive debt funding by seeking to limit deductions for interest, the CCCTB has taken the opposite approach and would allow a deduction for notional interest on equity capital. If the full CCCTB proposal is implemented, the interplay between it and the provisions of the ATAD will be interesting, if not to say challenging.

When the draft ATAD was first published concerns were expressed that some of the proposals might not be compatible with EU law. For example, that the proposed GAAR would have applied to other than wholly artificial arrangements and would thereby conflict with the Court’s case law on Member States’ anti-avoidance measures. The draft was amended to mitigate some of these concerns, but some still remain. For example, the proposed CFC provisions might be incompatible with the Court’s

---

<sup>190</sup> Deloitte, ‘BEPS Actions Implementation by Country’, available at: <<https://www2.deloitte.com/global/en/pages/tax/articles/beps-action-implementation-matrices.html>> accessed 21 May 2018.

case law<sup>191</sup>. It has also been suggested<sup>192</sup> that the anti-hybrid rules may be contrary to the Court's case law on the grounds that they involve determining a company's tax treatment in one jurisdiction by reference to its treatment elsewhere.

The interaction of BEPS measures with EU law has been subjected to a detailed analysis by Sjoerd Douma<sup>193</sup>. He acknowledges that the view of the Court on the actions taken or proposed by the other institutions of the EU to implement BEPS measures is not yet known but raises concerns that some of the measures may infringe free movement law<sup>194</sup>. In connection with the ATAD's hybrid mismatch provisions Douma makes a similar point<sup>195</sup> to that made by Finet (n 178), that the notion of determining the tax treatment of a transaction in one country by reference to its treatment in another may be regarded by the Court as contrary to its acceptance of the general principle that the parallel exercise of taxing powers by Member States is not *per se* a restriction on free movement, ie, a Member State is not bound to draw up its tax rules on the basis of those in another Member State in order to prevent a difference in treatment. As to the ATAD's provisions on CFCs, Douma notes<sup>196</sup> the potential for conflict between the provisions in the ATAD and the Court's position on CFC provisions to the effect that they are only proportionate if they apply to wholly artificial arrangements (see for example the *Cadbury Schweppes* case cited at n 177). The ATAD provisions limiting interest deductions are especially vulnerable to challenge by the Court on free movement grounds in Douma's view as they are likely to target cross-border situations more than domestic ones<sup>197</sup>.

---

<sup>191</sup> A leading case on CFC provisions and freedom of establishment is Case C-196/04 *Cadbury Schweppes plc, Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue* [2006] ECR I-07995, in which the UK's CFC provisions were held to contravene the freedom of establishment as they were not restricted only to wholly artificial arrangements intended to escape the normally due national tax.

<sup>192</sup> See, eg, JP Finet, 'Hybrid Mismatch Rules Expected to Raise Issues for CJEU', in *Tax Notes International*, 84(3) (2016) at p244.

<sup>193</sup> Sjoerd Douma, 'BEPS and European Union Tax Law', *Cahiers de droit fiscal international*, Vol 102a, Sdu: The Hague 2017, pp65-95.

<sup>194</sup> *ibid*, section 1 at p66.

<sup>195</sup> *ibid*, section 2.5 at p72.

<sup>196</sup> *ibid*, section 3.2 at p74.

<sup>197</sup> *ibid*, section 4.4 at p77.

The ATAD was promoted by the Commission as a vehicle for the consistent implementation of BEPS recommendations across the Member States. The ATAD goes beyond BEPS, however. A GAAR has never been one of the BEPS recommendations. Neither does BEPS address the matter of exit taxes. The suspicion that the Commission has taken the opportunity to use the BEPS bandwagon to usurp the role of individual Member States in matters concerning tax avoidance may be well founded. It has been argued<sup>198</sup> that by prescribing common tax measures, the sovereignty of the Member States is further undermined, the tax competitiveness of Member States is inhibited and the “creeping harmonisation of tax law” in Europe has been furthered.

As well as a potential conflict between some of the ATAD provisions and the Court’s case law, the question arose as to whether aspects of the ATAD could be said to breach the principles of subsidiarity and proportionality and thereby represent an unlawful usurpation of Member States’ competence over direct tax matters. This concern was raised with the Commission by various Member States<sup>199</sup>. As mentioned above, there were a number of amendments of the ATAD between the initial draft and the version finally adopted, and the fact that the ATAD eventually obtained the required unanimous approval suggests that the concerns raised by Member States over subsidiarity and proportionality had been addressed to their satisfaction or otherwise mollified. The benefits of co-ordinated action to implement BEPS measures and combat tax avoidance seem to have a significant factor in persuading Member States that a legislative measure at EU level was preferable to piecemeal action by individual Member States.

## **6.4 Anti-avoidance and the tax harmonisation agenda**

The anti-avoidance measures adopted by the EU (hard law, soft law and the Court’s case law) involve elements of both positive and negative integration. There is little doubt that the EU sees the tax

---

<sup>198</sup> Joe Duffy & Tomas Bailey, ‘The Anti-Tax Avoidance Directive in Ireland: Winds of Change or an Easterly Breeze’, *Irish Tax Review* 2016, issue 4, pp106-112.

<sup>199</sup> The Czech, German, Portuguese and Romanian parliaments engaged in a dialogue with the Commission and the Maltese and Swedish parliaments submitted reasoned opinions. Links to the documentation and the Commission’s responses are available on the COM/2016/0026 document details page at: <<http://www.ipex.eu/IPEXL-WEB/dossier/document/COM20160026.do>> accessed 22 May 2018.



avoidance debate as a significant opportunity to promote a tax harmonisation agenda, though this is not publicly stated. In this connection the fact that the ATAD was passed despite some initial Member State reservations that it breached the principles of subsidiarity and proportionality may encourage the Commission to try and promote further tax measures by emphasising an anti-tax avoidance character, since the adoption of the ATAD suggests that Member States have accepted that in principle anti-avoidance measures are best dealt with at EU level.

Ideally, of course, anti-avoidance measures would eliminate the conditions for tax avoidance *ex ante* rather than tackling the symptoms *ex post*. The Court's judgments are necessarily *ex post*. The elimination of the conditions for tax planning *ex ante* is a feature of the CCCTB proposal, which is covered elsewhere in this work. The CCCTB involves a strong anti-avoidance component which would go a considerable way towards ensuring that multinationals pay their 'fair' share of tax in each jurisdiction in which they operate by apportioning their aggregate profits between Member States on the basis of a formula designed such that profits are taxed on the basis of their actual economic activity in each jurisdiction.

## STATE AID AND DIRECT TAXES

### 7.1 Background

If the Court was a relatively late starter (in the mid-1980s) in terms of establishing its jurisdiction in matters of direct tax, the widespread application by the Commission of its State aid powers is an even more recent development.

The principal Treaty provisions on aids granted by States are set out in Articles 107 to 109.

Article 107(1) sets out the fundamental principle that:

...any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.

Article 108 tasks the Commission, in cooperation with the Member States, with keeping all systems of State aid in constant review. Article 108(2) allows the Commission to in effect block aid it deems incompatible with the internal market, and if the Member State concerned does not comply with the Commission's decision it may be referred to the Court. Under Article 108(3), Member States are obliged to inform the Commission of any plans to grant or alter an existing aid, and the Commission is empowered to block any proposals it considers not compatible with the internal market.

### 7.2 Application to direct taxes

That the Commission considered tax measures were in principle within the ambit of the State aid provisions was made clear in a Commission Notice in 1998<sup>200</sup>. Article 107 refers to aid "in any form

---

<sup>200</sup> Commission Notice on the application of the State aid rules to measures relating to direct business taxation [1998] OJ C384/3.

whatsoever”, and there was no reason to suppose that aid in the form of tax measures should fall outside this deliberately broad definition.

Further guidance on the application of the State Aid rules to tax was published by the Commission in 2016<sup>201</sup>, which substantially expands on (though does not supersede) that set out in 1998.

The Commission’s view is that fiscal measures that discriminate between taxpayers in a similar factual and legal situation constitute, in principle, State aid<sup>202</sup>. If a State aid is found to be incompatible with the internal market, the consequences for the Member State concerned can be draconian. It may be required to recover the aid from its recipients up to ten years after it was given.

There are many examples of tax reliefs and tax favoured regimes for the treatment of income or expenditure that constitute notifiable State aids. For example, enhanced tax reliefs for research and development expenditure and tax reliefs on venture capital scheme investment schemes. Member States seek Commission approval as a matter of course when introducing such reliefs or changing existing ones, as they are required to do under Article 108(3).

The application of the State aid rules to tax measures like these has been relatively uncontroversial, though involving a great deal of extra work for Member States’ tax authorities in making the case why the measures are justified and do not amount to significant distortions of competition. What really caught the public eye (and focused Member States’ attention) was the extension of State aid provisions to tax rulings and settlements, as the investigations launched by the Commission involved some of the world’s best known companies. The catalyst for this was that since 2013 the Commission’s Directorate General for Competition has been carrying out an inquiry into tax ruling practices from a State aid perspective<sup>203</sup>. The Commission does not question the principle of

---

<sup>201</sup> Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union [2016] OJ /C262/1.

<sup>202</sup> The principal is referred to in almost all the Court’s judgments in State Aid cases, eg, Case C-88/03 *Portuguese Republic v Commission of the European Communities* [2006] ECR I-07115, para 54.

<sup>203</sup> ‘DG Competition working paper on State aid and tax rulings’, Background to the high level forum on State aid of 2 June 2016. Available online at:

granting advance tax rulings by Member States' tax authorities. It recognises the value of advance rulings as a tool to providing taxpayers with legal certainty. What does give it grounds for concern, however, are rulings that grant a selective advantage to specific undertakings or groups of undertakings.

To facilitate the inquiry, all Member States were asked to provide information about their tax ruling practices and the legal framework underlying those rulings, together with a list of rulings given between 2012 and 2013.

The inquiry led to the launch in mid-2014 of three high profile formal State aid investigations on tax rulings granted by Ireland (to Apple), by Luxembourg (to Fiat) and by the Netherlands (to Starbucks). Amongst other high profile investigations that have been opened subsequently are those into rulings granted by Luxembourg (to Amazon, McDonalds and GDF Suez) and by Belgium (under their Excess Profit Scheme).

As a result of these investigations the Commission ruled against the aid given to Starbucks, Fiat and under the Belgian Excess Profit Scheme. On 30 August 2016 the Commission also ruled against Ireland in the Apple case<sup>204</sup>. Ireland's response was vigorous. In an application lodged with the General Court on 9 November 2016 the Commission was accused of attempting to rewrite the Irish corporation tax rules in a manner inconsistent with Member State sovereignty in the area of direct taxation. The application claims that:

The Commission infringed the principles of legal certainty and legitimate expectations by invoking alleged rules of EU law never previously identified. These are novel and their scope and effect are wholly uncertain.... The Commission has exceeded its powers and interfered with national tax sovereignty. The Commission has no competence, under State aid rules, unilaterally to substitute its own view of the geographic scope and extent of the Member

---

<[http://ec.europa.eu/competition/state\\_aid/legislation/working\\_paper\\_tax\\_rulings.pdf](http://ec.europa.eu/competition/state_aid/legislation/working_paper_tax_rulings.pdf)> accessed 18 May 2018.

<sup>204</sup> Commission Decision of 30.8.2016 on State aid implemented by Ireland to Apple C(2016) 5605 final.

State's tax jurisdiction for those of the Member State itself. The purpose of the State aid rules is to tackle State interventions which confer a selective advantage. The State aid rules by their nature cannot remedy mismatches between tax systems on a global level.

Apple has also lodged its own appeal. Commentators expect that resolving the cases could take upwards of five years<sup>205</sup>, which in the meantime will leave businesses, national tax authorities and Member States alike in a state of complete uncertainty.

Other Member States are likely to have similar grounds for appealing against the Commission's rulings in their own cases, and there are indications that other Member States subjected to similar Commission investigations may support Ireland's case. This seems to make a great deal of sense as many of the fundamental points at issue are *prima facie* common to all.

I do not intend to examine individual cases in any detail as the facts in most of them are extremely complex. They almost all involve rulings on transfer pricing, the common theme being that the rulings, allegedly, gave the companies a more favourable tax treatment (in terms of taxation of income or deduction of expenses) than would have been justified had the internationally accepted 'arm's length' principle been applied.

### **7.3 Tax settlements and rulings**

The 2016 Commission Notice<sup>206</sup> contained a section (5.4) on specific issues concerning tax measures. Of particular interest are the comments on tax amnesties and tax rulings and settlements, which helpfully clarify the Commission's position on these matters.

According to the Commission, tax amnesties are acceptable provided that: (i) they are open to all undertakings without favouring any pre-defined group of undertakings; (ii) that they do not indirectly

---

<sup>205</sup> Institute of Chartered Secretaries & Administrators, 'The EU, tax and the Apple of its Ire', 10 November 2017, states that 'Five years is being touted as the likely timeframe to resolve the appeal against the August 2016 decision'. Article available online at: <<https://www.icsa.org.uk/knowledge/governance-and-compliance/indepth/technical/eu-tax-apple-legal-case>> accessed 19 May 2018.

<sup>206</sup> Commission Notice on the notion of State aid as referred to in Article 107(1) of the TFEU [2016] OJ C262/1 ('2016 Notice').

entail any selectivity in favour of certain undertakings or groups of undertakings; and (iii) that the tax administration's action is limited to administering the implementation of the tax amnesty without any discretionary power to intervene in the in granting of the measure<sup>207</sup>.

Tax rulings may confer a selective advantage on their recipients where: (i) the ruling misapplies national tax law and this results in a lower amount of tax; (ii) the ruling is not available to undertakings in a similar legal and factual situation; and (iii) the administration applies a more 'favourable' tax treatment compared with other taxpayers in a similar legal and factual situation, which might be the case where the tax authority accepts a transfer pricing arrangement which is not at arm's length<sup>208</sup>.

Tax settlements may entail a selective advantage where: (i) in making disproportionate concessions to a taxpayer, the administration applies a more 'favourable' discretionary tax treatment compared to other taxpayers in a similar factual and legal situation; or (ii) the settlement is contrary to the applicable tax provisions and has resulted in a lower amount of tax outside a reasonable range, which might the case where established facts should have led to a different assessment of the tax on the basis of the applicable provisions but the amount of tax due has been unlawfully reduced<sup>209</sup>.

What becomes clear from these pronouncements is that any significant degree of discretion on the part of tax authorities can easily be construed as selectivity. As a result, many Member States have amended their tax administrative practices to make them more transparent and less reliant on discretion on the part of the tax authorities.

Not only are Member States required to inform the Commission of any tax rulings they grant but from 1 July 2017 they have been required to share those rulings amongst themselves. According to Pierre Moscovici, Commissioner for Economic & Financial Affairs, Taxation & Customs:

---

<sup>207</sup> *ibid*, para 166.

<sup>208</sup> *ibid*, para 174.

<sup>209</sup> *ibid*, para 176.

“We have broken new ground on tax transparency, by pushing Member States to commit to more openness, both on their own tax practices and those of multinationals. On 1 July, just two days from now, Member States will for the first time begin to share information about tax rulings with each other, finally tearing down the wall of secrecy around the tax arrangements they grant to businesses and companies. As a Commissioner, I am in favour of anything that contributes to competition<sup>210</sup>, but I will never oppose competition to transparency, I think that is a wrong idea and a wrong way of thinking. I am not fighting this or that profession, but I think that secrecy is no more what we must achieve in today's world<sup>211</sup>”.

## **7.4 Methodology: advantage and selectivity**

Article 107(1) refers to aid “...which distorts or threatens to distort competition by favouring certain undertakings...”. This requires the existence of two key elements; an advantage, and that the advantage is conferred selectively.

The recommended methodology for assessing these factors is set out in the 2016 Commission Notice. Note that references to case law are given throughout the 2016 Notice to support the propositions advanced therein.

### *Advantage*

Section 4 of the 2016 Notice addresses advantage. Paragraph 66 states that “An advantage within the meaning of Article 107(1) of the Treaty, is any economic benefit which an undertaking could not have obtained under normal market conditions, that is to say in the absence of State intervention”.

Paragraph 74 states the principle that “Economic transactions carried out by public bodies (including public undertakings) do not confer an advantage on its counterpart, and therefore do not constitute

---

<sup>210</sup> With the exception, one assumes, of tax competition.

<sup>211</sup> Pierre Moscovici, Speech to the Commission’s Tax Fairness Conference, 28 June 2017, SPEECH/17/1828 available on European Commission Press Release Database.

aid, if they are carried out in line with normal market conditions". The Commission considers that a 'market economy operator' (MEO) test is the relevant method to assess whether economic transactions carried out by public bodies take place under normal market conditions and, therefore, whether they involve the granting of an advantage (which would not have occurred in normal market conditions) to their counterparts [para 75]. The purpose of the MEO test is to assess whether the State has granted an advantage to an undertaking by not acting like a market economy operator with regard to a certain transaction [para 76].

The Notice then goes on to give guidance as to how the MEO test can be applied. Where the same transactions are also carried out on the same terms by private operators (referred to as 'pari passu' transactions), or the transaction was the subject of a competitive tender process, compliance with market conditions can be directly established [section 4.2.3.1]. In other cases, either a benchmarking process should be employed or other assessment methods used [section 4.2.3.2].

Benchmarking in the context of advantage involves the assessment of a transaction in light of the terms under which comparable transactions carried out by comparable private operators have taken place in comparable situations [para 98].

Other assessment methods may be appropriate provided they are based on "...a generally accepted, standard assessment methodology" [para 100].

### *Selectivity*

Fundamental to the application of the State aid provisions is the principle that a measure or action is only susceptible to challenge if it confers a selective advantage. For the avoidance of doubt, a measure can only be 'selective' for State aid purposes if it treats persons in the same Member State differently. Thus if, for example, a Member State had an exceptionally low rate of corporation tax compared with that of other Member States and this rate applied to all its corporate taxpayers, it would not be vulnerable to challenge as a State aid as there was no selectivity within the Member State. This was confirmed by Max Lienemeyer, the State aid Head of Unit for Tax Planning Practices,



DG Competition, when he spoke in London during 2017, who added that whilst the State aid provisions could not apply in such a case differences between Member States' tax regimes that amounted to harmful tax practices would fall within the scope of the Code of Conduct on Business Taxation<sup>212</sup>. State aid is mainly concerned with (positive) discrimination within the same Member State, whilst the Code of Conduct is mainly concerned with excessive cross-border tax policy competition. Some national tax policy measures may be caught by both sets of rules, however. For instance, the Commission's State aid interventions have led to the discontinuation of several 'harmful' national tax regimes, such as the 10% tax rate under the Irish International Financial Services Centre regime<sup>213</sup>, the Belgian coordination centre regime<sup>214</sup>, and the Netherlands group financing regime<sup>215</sup>. These arguably fall more within the ambit of the Code of Conduct on harmful tax practices than under the ambit of State aid, but the latter of course enables the Commission to tackle the measures with hard law rather than the non-binding soft law of the Code of Conduct.

Selectivity is addressed in section 5 of the 2016 Notice. The basic principle is set out in paragraph 117: 'To fall within the scope of Article 107(1) of the Treaty, a State measure must favour "certain undertakings or the production of certain goods". Hence, not all measures which favour economic operators fall under the notion of aid, but only those which grant an advantage in a selective way to certain undertakings or categories of undertakings or to certain economic sectors'.

Paragraph 118 goes on to say: 'Measures of general application which do not favour certain undertakings only or the production of certain goods only do not fall within the scope of Article 107(1) of the Treaty. However, the case law has made it clear that even interventions which, at first appearance, apply to undertakings in general may be selective to a certain extent and, accordingly, be regarded as measures designed to favour certain undertakings or the production of certain goods.'

---

<sup>212</sup> Joint Chartered Institute of Taxation and King's College, London seminar 'State aid and taxation', 14 March 2017 (attended by writer).

<sup>213</sup> Commission Decision of 17 February 2003 on aid scheme – Ireland – foreign income [2003] OJ L204/51.

<sup>214</sup> Commission Decision of 17 February 2003 on the aid scheme implemented by Belgium for coordination centres established in Belgium [2003] OJ L282/25.

<sup>215</sup> Commission Decision of 17 February 2003 on the State aid implemented by the Netherlands for international financing activities [2003] OJ L180/52.

Neither a large number of eligible undertakings (which can even include all undertakings of a given sector), nor the diversity and size of the sectors to which they belong, provide grounds for concluding that a State measure constitutes a general measure of economic policy, if not all economic sectors can benefit from it’.

The approach to be taken in most cases when assessing selectivity involves three steps [para 128] as follows.

1. Identify the ‘system of reference’. A ‘system of ‘reference’ is composed of a consistent set of rules that generally apply – on the basis of objective criteria – to all undertakings falling within its scope as defined by its objective [para 133]. Examples of systems of reference are given in paragraph 134, including a corporate income tax system and a VAT system.
2. Determine whether the measure in question constitutes a derogation from that system insofar as it differentiates between economic operators who, in light of the objectives intrinsic to the system, are in a comparable factual and legal situation. If the measure in question does not constitute a derogation from the reference system it is not selective. If it does constitute a derogation, the third step of the test must be applied.
3. Determine whether the derogation is justified by the nature or general scheme of the reference system. A measure may be justified if it derives directly from the intrinsic basic or guiding principles of the reference system or where it is the result of inherent mechanisms necessary for the functioning and effectiveness of the system [para 138].

The number of Commission Decisions and appeals to the Court by Member States in the field of State Aid and tax measures would suggest that there is a considerable underlying lack of definition and clarity regarding the practical application of the principles outlined above. Especial difficulties appear to arise as regards the boundaries of the ‘nature or general scheme of the system’ justification and with measures that *prima facie* appear to apply to all undertakings but might be said

to be indirectly selective<sup>216</sup>. An example of the latter can be seen in the *Santander* case<sup>217</sup>, which as if to underline the difficulties of interpretation and practical application was initially decided in the taxpayer's favour by the EGC but in the Commission's favour by the Court on appeal. Following its investigation into a Spanish tax provision under which Spanish companies were allowed a tax deduction for the goodwill element of the cost of acquisitions of shares in non-Spanish companies, whilst no such deduction was allowed in the case of the acquisition of shares in domestic Spanish companies, the Commission ruled that the provision conferred a selective advantage on certain Spanish companies compared with their Spanish competitors in breach of the State aid rules. Spain took the matter to the EGC, which ruled against the Commission. The EGC found that to constitute State aid it was necessary to specify a particular category of undertakings that benefit from the measure in question, and that in its view the Spanish tax provision was not aimed at any particular category of undertaking and did not exclude any category of undertaking from taking advantage of the regime. In the EGC's opinion, by failing to prove that the tax measure had benefitted a particular category of undertakings, the Commission had failed to establish the selective nature of the measure and, therefore, it could not be considered State aid. The Commission in turn appealed the matter to the Court, which ruled in its favour<sup>218</sup>, with the likely result that Spain will have to recover the aid. The Court held that in determining whether a measure is selective for the purposes of the State aid rules it is not necessary to identify a specific category of undertakings that benefit exclusively from the measure. The appropriate standard for establishing the selectivity of a measure is whether the measure benefits certain undertakings as compared to other undertakings, or applies different

---

<sup>216</sup> A recent examination of EU State aid as applied to taxation with a focus on the underlying case law is Christopher Bobby, 'A Method Inside the Madness: Understanding the European Union State Aid and Taxation Rulings', *Chicago Journal of International Law*, Volume 18, Number 1, Article 5 pages 186-215, 7 January 2017. The analysis of the case law on selectivity, advantage and the reference system (pages 204-212) is of particular interest. The author claims (page 207) that a careful analysis of relevant cases refutes the US Treasury Department's claim that the Commission has purposefully conflated the terms advantage and selectivity. Certainly the terms are dealt with separately in the Commission's 2016 Notice.

<sup>217</sup> Case T-399/11 *Banco Santander and Santusa v Commission* ECLI: EU: T: 2014: 938.

<sup>218</sup> Joined cases C-20/15 P *European Commission v World Duty Free Group SA and Others* and C-21/15 P *Commission v Banco Santander SA and Santusa Holding SL* ECLI: EU: C: 2016: 981.

treatment to undertakings that are in comparable factual and legal situations, unless the treatment can be justified by the nature of the tax regime. *This is the case even if, in principle, the beneficial measure is available to all companies* [my italics]. On this basis, the Spanish tax provision was selective even though all Spanish multinationals could have benefitted from it as wholly domestic companies could not achieve similar benefits.

A result of the lack of definition and clarity regarding the application of State Aid to tax measures is that Member States are unsure where the boundary lies as between their general competence over direct tax matters and the Commission's competence over State Aid matters. This inevitably causes a degree of friction. As matters stand it is not easy to see how this could be remedied, however<sup>219</sup>.

## **7.5 Is State aid the right tool for the job?**

The great advantage for the Commission of employing its State aid powers as opposed to seeking to legislate is that the Treaty vests competence in matters of State aid entirely in the Commission (subject to the right of Member States to appeal to the EGC or Court against adverse Commission rulings). No support is required from the Member States and the Commission's actions require no votes. The Commission can effectively operate independently from everyone else, especially the Member States. It may be said that in State aid matters it is master of the game.

A former Commissioner for Competition, Neelie Kroes, considers that State aid is not the right tool to fight tax avoidance, and that rather than pursuing companies such as Apple for what they did in the past, the EU should be focusing on shaping a fair tax system for the future. She recognises that there

---

<sup>219</sup> Tax selectivity in the EU State Aid context is the subject of Claire Micheau, 'Tax Selectivity in European Law of State Aid: Legal Assessment and Alternative Approaches', *University of Luxembourg Law Working Paper Series*, Paper number 2014-06, July 2014. In contrast to the article by Christopher Bobby referred to above, the author does not review the jurisprudence of the Court to any great extent but focuses on a number of alternative approaches to the current selectivity test that have been suggested. The author concludes, however, that none of these alternatives appear to be entirely satisfactory and that the likelihood is that the Commission and Court will continue to develop and refine the existing methodology. She rightly notes (page 32) that tax selectivity is made all the more complex because it crosses boundaries between the different fields of tax law, EU law and competition law.

is a widespread feeling that multinationals do not pay enough taxes and that they are using mismatches between national tax laws to lower their tax burden. But in her view State aid is not suited to deal with such mismatches. Rather it is a tool to address instances where a Member State has made an exception to its own rules and given a specific company an advantage. She writes<sup>220</sup>:

EU Member States have a sovereign right to determine their own tax laws. State aid cannot be used to rewrite those rules. However, the current State aid investigations into tax rulings appear to do exactly that, by suggesting a radical new approach to so-called transfer pricing rules that determine where profits shall be allocated. By doing so, the Commission risks undermining the important work carried out within the OECD through its Base Erosion and Profit Shifting ('BEPS') project.

She goes on to note concerns expressed by the United States (which sees the Commission's use of the State aid provisions as particularly aimed at US multinationals<sup>221</sup>) that it is expanding the Commission's role beyond the enforcement of competition and State aid law under the Treaty into that of a supra-national tax authority. She is particularly concerned by the retrospective nature of the State aid provisions:

...you cannot change the rules of the game through *ad hoc* State aid enforcement and then seek retroactive recovery for unpaid taxes. Doing so would be fundamentally unfair and would harm competition, growth and tax income in Europe. And it raises serious questions about legal certainty and the rule of law. It is a fundamental principle of tax law that changes will not apply retroactively. Companies (as individuals) should know what their fiscal obligations are up front and should be able to plan with them. When tax rules change, they do so for the future only, and there are strict limits to the re-opening of tax assessments for the past. With the application of State aid rules, this changes, as the Commission may order

---

<sup>220</sup> Neelie Kroes, 'Why EU State Aid is Not the Right Tool to Fight Tax Avoidance', *The Guardian*, 1 September 2016.

<sup>221</sup> Robert Stack, the US Treasury official responsible for international tax policy, in testimony before the US Congress, accused the Commission of disproportionately targeting US companies.

the recovery of any State aid deemed illegal for 10 years into the past. This could happen in a situation in which neither the company nor the Member State have violated any tax rules nor had any reason to believe that the tax assessment was illegal.

I have made the point elsewhere in this work that the best way of tackling tax avoidance is to remove the conditions that give rise to it *ex ante* rather than trying to deal with the manifested symptoms *ex post*.

Bill Dodwell, a former President of the UK's Institute of Taxation, is also of the view that the State aid provisions are not the right tool for the job of tackling tax avoidance:

The overarching problem for the EU, some of its Member States, and many businesses, is that State aid inquiries are a poor way to raise questions about tax systems. Whilst there is public concern in Europe at untaxed profits, State aid inquiries shouldn't lead to taxing profits left low taxed or untaxed by other countries<sup>222</sup>.

If the application of the State aid rules in this way leads to large numbers of cases coming before the EGC or Court under which Member States challenge the Commission's rulings and the EGC/Court is in effect having to act as arbitrator in highly complex transfer pricing matters, this will be a far from ideal situation.

Clearly, action taken against Member States under the State aid provisions constitutes a 'negative' form of integration.

---

<sup>222</sup> Bill Dodwell, 'Building Blocks: the Application of State Aid Rules in Recent Incidents', *Tax Adviser*, October 2016, p14.

## THE EU VAT REGIME – A MODEL OR A WARNING?

### 8.1 Background to the VAT regime

The focus of this work is on direct taxes, so it is not the aim of this section to consider the EU VAT regime in any detail. The purpose of this chapter is to illustrate the benefits and potential drawbacks of implementing an EU-wide direct tax regime by way of directives using the VAT regime as a model.

Article 113, the legal basis for legislative measures on indirect taxes, permits the adoption of 'provisions', without specifying what form these should take. It would consequently have been open to the Commission to have proposed that the VAT system be introduced via directly effective regulations rather than directives to be implemented by the Member States. Even if regulations were a theoretical alternative, it is unlikely that they were seriously entertained in the case of the VAT regime if for no other reason than that Member States were to be given a considerable degree of latitude as regards VAT rates and numerous other elements which would be almost impossible to incorporate in a single set of regulations. This latitude was not only to apply to the initial setting up of the system but for the future as well, which again militates against any idea of a single set of rules changes to which could only be made by going through a cumbersome process of amending legislation at EU level.

Unless the Treaty is amended, the question of whether regulations or directives are used is in any event academic as far as direct tax is concerned, since directives are the only form of legislation permitted under the two legal bases most appropriate for direct tax legislation, viz, Articles 115 and (in principle if not yet in practice) Article 116. Putting the fact that regulations would not appear legally possible in direct tax matters to one side, would regulations be a practical means of implementing an EU-wide tax system? Regulations are by their nature suited to measures that apply uniformly to all Member States, a one size fits all approach. They are not suited to legislation under

which Member States are permitted a latitude of treatment in various ways. If legislation were made by way of regulations, changes could only be made to the regime by amending legislation at EU level, which would be a very cumbersome procedure when frequent or regular changes are needed.

Implementation through directives allows a degree of discretion to be granted to the Member States which, within margin of that discretion, enables them to tailor the system to their particular domestic circumstances and to make changes as and when needed in response to changes in those circumstances. A system governed by regulations would tend to need total control at the centre, which for a tax system would be politically unacceptable to the Member States even leaving aside the matter of practicability.

Some of the advantages of permitting the Member States some flexibility in implementation have been alluded to above. Flexibility in setting tax rates is an important factor, as Member States with relatively low rates of corporate and personal tax may choose to set higher rates of VAT than Member States with high corporate and personal tax rates. The current EU VAT regime stipulates a minimum standard rate of 15%<sup>223</sup> with no maximum laid down. The imposition of a single VAT rate with no flexibility would result in taxpayers in some Member States facing a disproportionately high tax burden.

Measures to harmonise Member States' indirect tax systems had been envisaged since the earliest days of the Community, which then consisted of only six members. Free movement of goods and services, ie, without the imposition of cross-border tariffs and the like, was clearly fundamental to the establishment and functioning of the internal market so it is no surprise that considerable emphasis was placed at an early stage on devising a solution for harmonising the various different indirect tax systems hitherto employed by the Member States. The first Directive on VAT, setting out the broad overall principles, was introduced in 1967<sup>224</sup> and the substantive rules were introduced the

---

<sup>223</sup>Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [2006] OJ L347/1, Article 97.

<sup>224</sup> First Council Directive 67/227/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes [1967] OJ English special edition: Series 1 Volume 1967 p14.



same year in the Second VAT Directive<sup>225</sup>. The Second VAT Directive was replaced by the Sixth VAT Directive in 1977<sup>226</sup>, which was in turn recast in 2006<sup>227</sup>.

In contrast to the limited number and the limited scope of the directives thus far issued in relation to direct taxes, the harmonised EU-wide VAT system has been in place for over 40 years. Over this period practical issues and problems arising from its implementation have emerged. Those issues and problems have proved not insignificant.

## 8.2 The VAT system and its problems

That there were problems with the VAT regime was recognised fairly early on. The European Parliament's Directorate General for Research observed that "One of the most serious defects of the...VAT system is its complexity: the scope it allows for varying national interpretations of VAT law. The basis system established under the Sixth Directive is riddled with derogations, exemptions options and special regimes<sup>228</sup>". It was also noted that most of the many types of derogating measures are "permanently temporary", ie, theoretically temporary but in practice permanent. It was recognised that these derogations, exemptions, etc, have a potentially distorting effect on competition within the Community, increase legal uncertainty, increase compliance costs and make it increasingly difficult for a trader established in a Member State to ascertain the VAT rules applicable in another Member State. Globalisation and the increased levels of international and intra-community trade have amplified the negative consequences of a deficient EU VAT system<sup>229</sup>.

---

<sup>225</sup> Second Council Directive of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes [1967] OJ English special edition: Series 1 Volume 1967 p16.

<sup>226</sup> Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment [1977] OJ L145/1. (This was subsequently recast as the Council Directive of 28 November 2006 on the common system of value added tax – see n 214.)

<sup>227</sup> Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [2006] OJ L347/1.

<sup>228</sup> 'Tax coordination in the European Union', European Parliament, Directorate General for Research, ECON 125 EN, 12-2000, at 29. Available online at:

<[http://www.europarl.europa.eu/workingpapers/econ/pdf/125\\_en.pdf](http://www.europarl.europa.eu/workingpapers/econ/pdf/125_en.pdf)> accessed 18 May 2018.

<sup>229</sup> Guido De Wit, 'The European VAT experience', *Tax Notes International* (1995) 10(2), pp49-54.

In 2011 the Commission issued a Communication on the future of VAT<sup>230</sup>. This was a wide-ranging review drawing on the experience of the past 40 years, the sub-title of which was ‘Towards a simpler, more robust and more efficient VAT system tailored to the Single Market’. The Communication followed a public consultation launched in 2010 to take a critical look at all aspects of the EU VAT system. The document also drew on discussions with the Member States and the EU’s own institutions. The more than 1,700 responses to the consultation were overwhelmingly of the view that there was certainly a need for such a debate.

The general conclusions included the following<sup>231</sup>:

There is a general feeling amongst stakeholders that the fragmentation of the common EU VAT system into 27 national VAT systems is the main obstacle to efficient intra-EU trade and thus prevents citizens from reaping the benefits of a genuine single market. Internationally active businesses consider that the price they actually pay for this lack of harmonisation comes in the form of complexity, extra compliance costs and legal uncertainty. SMEs do not always have the necessary resources to deal with this and therefore refrain from engaging in cross-border activities.

These shortcomings have an impact on commercial behaviour which may prevent the most effective business decisions being taken. When tax rules influence the decision on where to buy or sell goods and services, the economic neutrality of VAT is no longer guaranteed and the functioning of the single market is severely undermined.

Several contributors even pointed out that, as a result, doing business with non-EU partners is becoming ever easier and more profitable than doing business with EU firms.

As a preliminary point before addressing these concerns, the Communication noted that an average of around 21% of Member States’ tax revenues were generated from VAT, which meant that

---

<sup>230</sup> Commission, ‘Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee: on the future of VAT – towards a simpler, more robust and efficient VAT system tailored to the single market’ COM(2011) 851 final.

<sup>231</sup> *ibid*, section 2, paras 1-4.

Member States would be prepared to consider only gradual change and then only when the risks, benefits and costs to them were clear, well understood and fully assessed.

In light of the issues and concerns raised during the consultation, the Communication made the following points.

- The original intention when the VAT Directives were implemented was for a system under which VAT would normally be charged by the Member State in which goods or services had originated (the 'origin' system). Member States, and indeed the European Parliament, now recognise that the origin system, whilst theoretically the most attractive choice, is, for various reasons, politically unachievable and the preference now is to move to a system under which the norm will be that VAT is charged on goods or services in the Member State where the good or services are consumed (the 'destination' system). The notion that a greater share of tax should be levied on transactions in the country in which goods or services are consumed has gained wide currency and support from the public, as a result of the perception that businesses, especially large multinationals often sell large volumes of goods and services to a Member State whilst paying what seems like very little tax in that jurisdiction; this is a significant factor behind the assertion that the retention of a primarily origin based VAT system is politically unacceptable. One of the main demands coming out of the consultation is that a definitive set of rules to achieve the necessary transition should be put in place. The Commission has agreed that the original plan for the universal application of the origin system to both goods and services should be abandoned and the called-for rules to achieve a transition to system based more fully on the destination principle should be brought forward. I would mention that the need for this change in direction does not indicate that the system as originally implemented was defective; rather it is the result of changes over a long period of time to methods and patterns of doing business<sup>232</sup>.

---

<sup>232</sup> *ibid*, section 4.1 'An EU VAT system based on the destination principle'.

- The VAT system should be made simpler, so that a business active across the EU should be faced with a single set of clear and simple VAT rules: an EU VAT Code. A business should only have to deal with the tax authorities of a single Member State (a ‘one-stop-shop’ approach, which parallels the proposals of the CCCTB for corporate direct tax). Divergent practices at national level were increasingly being highlighted as a frustrating burden<sup>233</sup>.
- The VAT system should be efficient and neutral. This would involve a broader tax base (ie, transactions on which VAT is chargeable) with the charge being made at the standard rate, rather than the present system under which numerous categories of goods and services are completely exempted from VAT, or else charged at a reduced or zero percent rate. A broader base with fewer exemptions would generate more revenue at less cost, or allow the standard rate to be reduced. ‘Neutrality’ would require equal rules and much less scope for differences in implementation as between Member States. The present system allows for considerable differences both in taxable base, exemptions and reliefs and rates<sup>234</sup>.
- The VAT system should be robust and fraud-proof<sup>235</sup>.

The Commission followed up with an action plan to try and address some of these issues, but I will not consider these ongoing legislative proposals further. The point I wished to draw out is that whilst VAT is conceptually a very simple tax, it has been vastly complicated by the derogations, exemptions, special regimes, options, reduced rate schemes and so on. Their cumulative effect is that where they exist VAT ceases to be a tax on final consumption as it is in principle intended to be. There are also significant differences between the Member States as regards their administrative procedures. The result is significant distortions in decision making by businesses, competition between VAT-exempt and non-exempt businesses and between different EU countries, and an increase in compliance and administrative costs. Reducing the number of these exemptions, etc, would produce extra VAT revenues for Member States which they could use to reduce the rate of VAT or for other purposes.

---

<sup>233</sup> *ibid*, section 4.2 ‘A simpler, more efficient and robust VAT system’.

<sup>234</sup> *ibid*.

<sup>235</sup> *ibid*.

### 8.3 VAT regime as a model for a direct tax system?

In light of all the above, would the VAT system be a good model for an EU-wide direct tax system to follow? That is to say follow in the sense of directives setting out the overarching principles but leaving Member States to set their own tax rates (perhaps with a minimum rate stipulated to limit tax rate competition) and leaving Member States with a considerable latitude in determining the tax base. The comments made above suggest that the VAT system suffers from a serious lack of neutrality, produces obstacles and market distortions, is complex and involves high costs of compliance which fall disproportionately on smaller and medium sized businesses. These facts alone would be enough to recommend caution in following a similar model for a direct tax system.

But I believe that the problems could be even more pronounced in a direct tax system than they are under the VAT system. This is because a possibly crucial difference between the VAT system and a direct tax system is that a 'fully taxable' business (ie, one that is VAT registered and is not a wholly or partially VAT-exempt business) is generally indifferent to the rate of VAT, as any input VAT it incurs on purchases can be offset against the output VAT it charges on its sales. For such a fully taxable business VAT is by and large a matter of cash-flow and does not represent a real cost. VAT is a real cost to the end user (usually an individual) that is not itself a VAT-registered business. Such end users, however, typically do not have the mobility to relocate to a jurisdiction with a lower VAT rate. Differing corporate tax rates, on the other hand, can be a real cost to a business operating in more than one jurisdiction. If a company established in a country with a corporate tax rate of, say, 20%, wishes to carry on activity in another country whose corporate tax rate is 30%, then if it needs to set up a branch or agency in that other country any profits from business the company carries on in that other country will be taxed at 30%, representing a real additional cost of 10% compared with the tax rate that would have applied had the company conducted all of its business from its country of residence. Clearly, this represents a disincentive to the Company to set up business in the other country – if at all possible it would prefer to sell its products or services to customers in the other country but without sufficient physical presence there to render the profits from those sales liable to

tax in the other country. In some circumstances of course this is simply not a practical proposition and the only way the company can make sales in the other country it to set up a branch or agency and accept the fact that the profits it makes on those sales is taxed at 30%. At first thought, the higher tax rate would seem to represent an impediment to the exercise of the company's right of freedom of establishment. Indeed it is, but the Court has long accepted that Member States are free to allocate their taxing powers as they see fit provided the allocation reasonably approximates to international tax practice, and that the fact that a person might be subject to a higher tax rate if they exercise a freedom to move to or carry on activities in another Member State is not a matter to which the Treaty provides any remedy.

The purpose of this rather lengthy digression is to illustrate the point that allowing Member States a significant latitude under the VAT Directive as to their VAT rate and exemptions, etc, is, leaving aside the compliance costs of dealing with the administrative complexities, of relatively little concern to most businesses as it is not they that bear the real cost of VAT, and most end users are not in a position to relocate to another Member State simply to reduce their VAT burden. If a directive for corporate tax harmonisation were passed, which allowed Member States a substantial degree of latitude in setting tax rates and the tax base comparable to that afforded to them under the VAT Directive<sup>236</sup>, the risk would be that significant distortions remain. Such distortions could be avoided by substantially reducing, or even eliminating entirely, the degree of Member States' discretion under the hypothetical corporate tax regime. But the less latitude is allowed to the Member States

---

<sup>236</sup> For example, the standard rate of VAT set by the VAT Directives is currently a minimum of 15% (Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [2006] OJ L347/1, Article 97) with no maximum. As of January 2017 the lowest standard rate of any of the Member States was 17% (Luxembourg) and the highest was 27% (Hungary) [Commission, 'VAT rates applied in the Member States of the European Union – Situation as at 1 January 2017' Taxud.C.1 (2017)]. By contrast, as of March 2017 the lowest corporate tax standard rate amongst Member States was 9% (Hungary) and the highest was 35% (Malta) [KPMG, 'Corporate tax rates table 2017', available online at: <<https://home.kpmg.com/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online/corporate-tax-rates-table.html>> accessed 19 May 2018]. Note that Hungary has both the lowest corporate tax rate and the highest VAT rate; clearly end users of products and services bear a higher share of the tax burden in Hungary than do businesses, to which VAT is not generally an irrecoverable cost.

the more difficult will be the task of persuading them to agree to implement such a regime. That is the political balancing act that the Commission would have to grapple with.

A corporate tax harmonisation directive allowing Member States a significant degree of latitude and discretion might be a more realistic way to go forward. From the Member States' point of view they could claim to be retaining a significant degree of sovereignty over their direct tax affairs which should make it easier to sell to their electorates, and from the Commission's point of view it would be a start, certainly better than the existing position of 28 different and uncoordinated systems, and the amount of latitude allowed could over time gradually be reduced. Whilst some larger multinationals might not welcome a curbing of their ability to exploit differences in tax systems and to play one off against the other, it is likely that most businesses operating cross-border within the EU would welcome the greater certainty and stability that a more harmonised corporate tax system would bring. In fact there would be no need for such a directive to be limited to corporate taxes. A similar approach could be taken to harmonising personal taxes. A proposal for tax harmonisation across the board would seem to be far too ambitious at this stage, however. In any event the corporate tax system is clearly the Commission's immediate target, and rightly so as businesses, having greater mobility than most individuals, are more likely to exploit any discrepancies between different tax systems, thereby reducing Member States' tax revenues. By comparison, the personal tax system is much less of a priority. A proposal for a corporate tax harmonisation directive would certainly be a way the EU might choose to try and move forward. What the Commission is actually promoting in the corporate tax field at the moment is somewhat different. This is the Common Consolidated Corporate Tax Base ('CCCTB'), which is considered elsewhere in this work.

The point should be made, though it also arises to a lesser extent where legislation is in the form of regulations, that where legislation takes the form of directives requiring separate implementation some differences are always likely to arise because language issues give rise to differences in definitions, interpretation or emphasis, some of which can be significant.

## CONCLUSIONS

### 9.1 Where are we now?

The EU has now been grappling with the issues of direct taxation for more than 50 years, yet it is still far from settled whether the future trend will be towards more harmonisation or towards Member States reasserting their sovereignty. Neither is there a common view as to whether competition between Member States in matters of tax is bad thing or a good thing. If competition is in principle a good thing, leading to innovation, efficiency, reduced costs and benefits for consumers, as acknowledged by Commissioner Moscovici in a speech quoted earlier, why should it be a different when it comes to tax? And if tax competition is a bad thing, where is the dividing line between what is 'fair' competition and 'harmful'?

The current position was succinctly summarised by Malcolm Gammie, a British barrister and tax tribunal judge with extensive experience of EU tax litigation:

The basic parameters set by the case law within which Member States can legislate in the corporate tax field are now relatively clear. With only limited hard law in place and without political agreement on the role and direction for corporate taxes within Europe that might facilitate further legislative measures at EU level, Member States are left to try and strike the right balance between those matters still within their competence, even assuming it is entirely clear which those might be. Progress in the corporate tax sphere is no longer glacial but it is spasmodic and can hardly be described as coordinated. We are, however, a very long way away from being in a position to describe and analyse a single European corporate tax system<sup>237</sup>.

---

<sup>237</sup> Malcolm Gammie, in foreword to Christiana Panayi, *European Union Corporate Tax Law* (Cambridge University Press 2013) p xiii.



The aim of this work was to consider the question: are the existing mechanisms and instruments available to the institutions of the EU sufficient to achieve effective harmonisation of Member States' direct tax regimes? In order to answer this, it is first necessary to consider what 'effective harmonisation' would involve. At the beginning of this work I set out a working definition of tax harmonisation as the elimination of differences, in particular the equalisation of corporate income tax rates and the standardisation of corporate income tax bases within the EU, ie, that tax reliefs, exemptions and the way in which taxable income is calculated is broadly the same across all Member States.

'Harmonisation' is as distinct to 'tax co-ordination' which I defined as the process of governments reaching agreements over some specific aspects of corporate taxation, such as agreements to reduce or remove special regimes that apply reduced corporate tax rates to certain activities.

That tax harmonisation would have a number of significant objective benefits, and what the nature of those benefits would be, was made clear in the 1962 Neumark Committee Report<sup>238</sup>, the Commission's 1967 'Programme for the harmonisation of direct taxes'<sup>239</sup> and the 1990 Ruding Committee Report<sup>240</sup>, all of which are examined in section 4.1. The fact that the Member State unanimity required to implement harmonisation on a large scale was not achieved and resulted in the Commission adopting a more piecemeal and limited approach does not negate the potential benefits of harmonisation that had been identified in these earlier works.

It has been said that 'harmonisation does not mean the uniformization [sic] of taxes<sup>241</sup>' and this has been a view fairly consistently expressed in the various policy documents on direct taxes over the years. For example, the 1962 Neumark Committee Report concluded that any attempt to completely unify the structures of national tax systems was both undesirable and bound to fail. In the Committee's view, '...complete unification of the tax systems of the Member States – even if it is

---

<sup>238</sup> n 6.

<sup>239</sup> n 9.

<sup>240</sup> n 31.

<sup>241</sup> Daniela Pirvu, *Corporate Income Tax Harmonization in the European Union* (Palgrave Macmillan 2012) p25.

held...that it is politically achievable – would not be considered as necessary from the aspect of integration policy, since experience proves that on many grounds moderate differences limited to the nature and to the rate of taxes do not hinder the free play of competition<sup>242</sup>. Similarly, the 1992 Ruding Committee was of the view that Community action does not mean uniformity; the Community should set a minimum Community-wide ‘floor’ for the tax base and rates but Member States would be free to impose higher taxes than the minimum prescribed by the floor<sup>243</sup>.

Elena Gonzalez Sanchez<sup>244</sup> questions whether harmonisation is even needed in the EU:

Notwithstanding all the tax harmonisation euphoria encouraged by the European Commission, this book has sought to establish that full harmonisation of corporate tax laws in the EC is not needed for the achievement of the EC Treaty objectives.” And: “...tax decentralisation is not an obstacle to the EC internal market.

She cites the example of Spain, which has a quasi-decentralised tax system that produces minimal tax obstacles to their internal market.

If by ‘full harmonisation’ she means total uniformity, with all rule changes made from the centre, then I would agree that it is neither necessary, desirable nor practicable.

The EU VAT system can reasonably be said to be a harmonised one, but Member States are allowed a degree of latitude. The harmonisation of the VAT system was achieved via a series of directives, which set out the core principles and a range of acceptable VAT rates, but left detailed implementation to the Member States. The flaws in that model that 40 years of experience have exposed have been highlighted in the previous chapter.

---

<sup>242</sup> Neumark Report (n 6), p102 at para 6.

<sup>243</sup> Ruding Committee Report (n 31), pp209-210.

<sup>244</sup> Elena Gonzalez Sanchez, *Corporate Tax Harmonisation in the European Union* (Universidad del Pais Vasco 2005) p203.

Although it is commonly accepted that harmonisation does not require total uniformity, it must in my view involve a very substantial degree of uniformity as between Member States' tax systems if it is to be meaningful.

An evaluation as to what progress has been made towards the harmonisation of direct taxes might perhaps best be carried out by comparing the current position with the specific goals and aspirations that have been set out by the Commission itself. The Commission's 2006 Communication 'Co-ordinating Member States' direct tax systems in the internal market'<sup>245</sup> set out three key objectives:

- eliminating discriminations (which can be taken as including obstacles/restrictions as well as direct and indirect discrimination) and double taxation;
- eliminating unintended double non-taxation and abusive practices; and
- reducing compliance costs associated with being subject to more than one tax system.

Further objectives were set out in subsequent documents:

- promoting good governance in tax matters<sup>246</sup>;
- removing cross-border tax obstacles for EU citizens (ie, natural persons)<sup>247</sup>;
- combatting tax fraud and tax evasion<sup>248</sup>; and
- tackling aggressive tax planning<sup>249</sup>.

---

<sup>245</sup> Commission, 'Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – coordinating Member States' direct tax systems in the internal market' COM(2006) 823 final.

<sup>246</sup> Commission, 'Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – promoting good governance in tax matters' COM(2009) 201 final.

<sup>247</sup> Commission, 'Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – removing cross-border tax obstacles for EU citizens' COM(2010) 769 final.

<sup>248</sup> Commission, 'Communication from the Commission to the European Parliament and the Council on concrete ways to reinforce the fight against tax fraud and tax evasion including in relation to third countries' COM(2012) 351 final; Commission, 'Communication from the Commission to the European Parliament and the Council – an action plan to strengthen the fight against tax fraud and tax evasion COM(2012) 722 final.

<sup>249</sup> Commission Decision of 17 June 2015 establishing the Commission Expert Group 'Platform for Tax Good Governance, Aggressive Tax Planning and Double Taxation' and replacing Decision C(2013) 2236 [2015] OJ C206/5.

If it may be assumed that if all of the above objectives were achieved the Commission would consider that Member States' tax systems had been successfully co-ordinated. But they could hardly be said to have been harmonised as well. For example, none of the above objectives preclude in principle differences in Member States' tax systems, their tax rates, tax base methodologies, tax reliefs and incentives. At present, inter-jurisdictional tax competition between Member States is only moderated by unenforceable soft law measures such as the Code of Conduct for Business Taxation.

Even assessed against the 'benchmark' objectives set out above, which fall well short of harmonisation, the combination of the limited positive integration achieved through the directives implemented so far, the negative integration through the Court's case law, soft law, the application of State aid provisions and, it might also be added, through the competitive pressures of market forces, has not succeeded in achieving the desired results. The conflict at the heart of this failure to achieve the objectives more fully (let alone to achieve meaningful harmonisation) is between the ostensible tax sovereignty of the Member States and the Treaty freedoms, which if interpreted literally could result in almost any direct tax provision of a Member State being construed as a restriction on free movement. It is only the fact that the Court has decided that certain matters (eg, the parallel exercise of taxing powers by Member States) fall outwith the Treaty freedoms, combined with its development of 'unwritten' justifications, that prevents Member States' tax provisions being attacked wholesale as restrictions on free movement.

As matters stand, substantial gaps and differences between Member States' direct tax systems still remain, with consequent distortions and opportunities for sophisticated tax planners (mainly larger multinational businesses) to exploit.

The elimination of double taxation was identified as an objective at a very early stage. Although the Parent-Subsidiary and Interest and Royalties Directives have been instrumental in eliminating double taxation in a large number of cases, these directives only apply to corporates and then only where one of the corporates holds at least, respectively, 10% or 25% of the shares in the other. The directives do not eliminate double taxation where the shareholding is smaller. Double taxation of

interest (but not dividends) received by individuals is eliminated under the Savings Directive. The double taxation problem is still far from solved.

The fundamental freedoms are at the heart of the entire European project. Since the Court established the principle that Member States' competence in matters of direct tax had to be exercised consistently with those freedoms, it (aided by the Commission in bringing infringement proceedings) has made a substantial contribution towards eliminating discriminatory and restrictive national tax Measures, and has by doing so made a notable contribution towards harmonisation and integration, albeit in a 'negative' and necessarily piecemeal and un-coordinated way. Given the significance of its contribution and the impact its rulings have had on national tax systems I have considered it appropriate to consider the Court's case law and methodology at some length.

But what of the Court's contributions towards the other objectives listed by the Commission? There, its contribution has been at best limited, since the subject matter of those objectives are simply not within its competence. The Commission has on occasion appeared to suggest that in its view the Court could do more and that some of the limitations the Court has placed upon itself are needless. For example, as regards double taxation the Commission voiced its frustration at the failure to eliminate it in its Communication 'Double taxation in the single market'<sup>250</sup>, in which it cited some of the Court's judgments that had allowed double taxation on the grounds that it represented a parallel exercise of taxing powers by Member States and, absent a general harmonising measure at EU level dealing with the matter, was thereby outside the scope of the Treaty freedoms. It has been pointed out<sup>251</sup> that the Court's approach in double taxation cases of confining itself to the tax position in a single country is inconsistent with its approach in cases like *Schumacker* (deductions for personal and family circumstances) and *Marks & Spencer* (offsetting cross-border losses), where it followed a 'global' approach and took the whole of the taxpayer's position into account. Had the Court adopted

---

<sup>250</sup> Commission, 'Communication from the Council to the European Parliament, the Council and the European Social and Economic Committee – double taxation in the single market' COM(2011) 712 final.

<sup>251</sup> Luca Cerioni, *The European Union and Direct Taxation* (Routledge 2015) p146.

a similarly 'global' approach in double taxation cases, the Parent-Subsidiary and Interest and Royalties Directives might not have been necessary and the double taxation problem solved.

The Court's acceptance, rightly or wrongly, of the principles that the parallel exercise of taxing power is not susceptible to Treaty challenge and that there is no Treaty right guaranteeing that a person moving from one Member State to another will not be subject to any higher tax burden than they were in the first State has had the result that differences between Member States' tax systems *per se* are not a matter for the Court. Cases in which the Court has been willing to act have been almost entirely the result of distinctions made by Member States on the grounds of nationality or residence.

If implemented by all Member States, the CCCTB would mark a major step towards the achievement of the objectives. Assessing CCCTB against the objectives listed above, it would eliminate the problems of tax discriminations and distortions at a stroke, eliminate double taxation of both the juridical and economic varieties, eliminate 'double non-taxation' and abusive tax planning strategies, it would certainly reduce the compliance costs associated with being subject to more than one tax system (as the group would have to file only one consolidated tax return), and the effect of automatic consolidation and a standardised tax base would remove the possibility of exploiting differences between Member States' tax systems upon which many of the forms of aggressive tax planning depend.

CCCTB would not of course be a universal panacea. It would only apply to those corporate bodies participating in the scheme. To the extent that CCCTB is adopted by only a number of Member States, or made optional for companies, the problems would still remain. CCCTB would be of no application to non-corporates.

From the point of view of the functioning of the internal market, the ideal scenario would be a situation where discriminations and distortions created by direct taxation in the functioning of the internal market no longer exist, and where free movement rights would be exercised for economic and market-related reasons, not for tax saving reasons. The notion that direct taxation should be as neutral as possible within the internal market has been an aspiration since as early as the 1960s. It

has not, however, been put into practice. According to the Court's case law, neutrality in the direct taxation area is not one of the Treaty objectives of the EU. The Court has accepted that 'forum shopping' for the most advantageous tax regime does not of itself constitute abuse of Treaty freedoms, and that the Treaty does not guarantee that a person transferring to another Member State will find themselves in a neutral situation as regards taxation, since disparities in the tax legislation of the Member States are merely instances of the parallel exercise of their taxing powers by Member States and outside the scope of the Treaty. The position the Court has taken on these matters does not necessarily mean that neutrality in the direct taxation area should not be an objective of the EU in the future. Statements in the Court's judgments along the lines of 'given the relevant disparities in the tax legislation of the Member States' indicate that whilst the Court has taken account of the current situation in the EU, where national tax laws do contain many disparities as between one Member State and another, there is no suggestion that the Court would necessarily oppose the Commission (or the Member States themselves if they were so minded) from seeking either through coordination or harmonisation a convergence between national direct tax systems. The proposed cooperation between France and Germany towards harmonising their tax systems referred to in the section on the CCCTB is an example of Member States taking the initiative themselves. If the Court's statements should be interpreted as meaning that neutrality of direct taxes has been neither an EU objective in the past nor should it be in future, this is not reconcilable with clear statements to the contrary that the Commission has made over many years (whether phrased in terms of harmonisation or coordination) highlighting the need to overcome distortions arising from a lack of sufficient tax neutrality.

One particular problem is that the fundamental principles of the internal market, above all the non-discrimination principle and the fundamental freedoms, are incompatible with the principles underlying the current international tax framework. Given that the EU's direct tax legislation thus far has addressed only limited and specific areas, the international tax system is still the foundation upon which the tax regimes of the Member States are based, and the Court in its case law has been forced to a large extent to accept the principles of the international tax system and try and reconcile

them with the principles of non-discrimination and the fundamental freedoms as best it can. If the reasoning in some of the Court's judgments sometimes looks doubtful, it is not entirely surprising given that it is trying to reconcile two sets of principles that are to a large extent fundamentally opposed. The current non-achievement of many of the benchmark objectives is the result of the very incomplete nature of the EU's legislation on direct tax and the Court's not always successful or coherent attempts to reach a compromise between the principles laid down in the Treaty and those of the international tax system.

Although the measures taken by the EU in both hard and soft law form, together with the case law of the Court, have gone some way to eliminating tax obstructions and distortions, many still remain and under the existing state of EU legislation and case law are not susceptible to challenge. In addition, the acceptance, albeit probably reluctantly, by the Commission of the concept of 'fair' tax competition<sup>252</sup> (as opposed to 'unfair' or 'harmful' tax competition which is to be discouraged or suppressed) means that Member States are still free to encourage businesses into their territory by offering a more attractive tax regime. The borderline between 'fair' and 'unfair' tax competition is unclear and is likely to vary according to the political weather. Notwithstanding it may be 'fair', this tax competition still creates significant distortions in the internal market. Without a convergence between the essential features of national direct tax regimes, or the imposition of more stringent boundaries as to what constitutes 'fair' tax competition these distortions will continue to arise. Just one striking illustration of how wide differences between Member States' tax systems can be whilst still being regarded as 'fair' is that Hungary's corporate tax rate is 9%, whilst that of Malta is 35%.

Aggressive tax avoidance strategies typically feature the segregation of taxable income (so that it is taxed in the lowest-tax jurisdictions) from the activities that create it (the costs of which are borne in higher tax jurisdictions so as to obtain a tax deduction). The OECD, in its 2013 Action Plan against Base Erosion and Profit Shifting ('BEPS'), stressed that, "No or low taxation is not *per se* a cause of

---

<sup>252</sup> The positive effects of fair tax competition were expressly acknowledged in the recitals to the Resolution adopting the Code of Conduct (Resolution of the Council on a code of conduct for business taxation [1997] OJ C2/1)



concern, but it becomes so when it is associated with practices that artificially segregate taxable income from the activities that create it<sup>253</sup>". In other words, what creates tax policy concerns is that, due to gaps in the interaction of different tax systems, and in some cases because of the application of bilateral tax treaties, income from cross-border activities might go untaxed anywhere, or be only lowly taxed. The proposed CCCTB would overcome these strategies by allocating profits based on the production factors and sales made in each Member State.

The acceptance of 'fair' tax competition means that national tax legislators will have to keep a close eye on the legislation of other Member States to ensure they are not 'undercut', as multinational companies will as a matter of course seek the lowest effective tax rate on their profits. Moral and fairness considerations aside, were they not to do so they might be accused of failing in their duty to act in the best interests of their shareholders. The uncertainties surrounding aspects of the Court's case law on fundamental freedoms and the seemingly progressive erosion of their tax sovereignty have been persuading many Member States that the most effective way to protect their national tax revenues lies not through cooperation with the other Member States but in designing a competitive direct tax system capable of attracting inward investment, resulting in a vicious (or virtuous depending on your viewpoint) circle; one Member State undercuts another causing the other Member State to lose tax revenues as businesses shift activity or residence to the more tax-attractive jurisdiction, the other Member State retaliates, etc, etc. Whether the result of this so-called 'race to the bottom' is that all the Member States ultimately lose revenues remains to be seen. The more disparities that fair tax competition creates between Member States the better the tax planners will like it. Indeed there is an argument that 'fair' tax competition is one of the primary roots of aggressive tax planning strategies. If 'fair' tax competition gets too much out of hand the EU institutions must surely consider reining back what is currently deemed to be acceptable, even if at present they can only seek to do this through soft law.

---

<sup>253</sup> OECD, 'Action Plan on Base Erosion and Profit Shifting' (OECD Publishing 2013), p10, para 2.

A secondary point is that if Member States are in reality pursuing a policy of tax competition with other Member States rather than cooperation, the measures adopted to enhance cooperation such as the Mutual Assistance Directives must seem rather incongruous. After all, why help a competitor? That Member States should regard each other suspiciously and as competitors is not likely to be conducive to the smooth progress of the European project.

Making a distinction between tax competition which is 'fair' and that which is 'unfair' or 'harmful' is a cornerstone of the EU's position on direct tax<sup>254</sup>. Where is the dividing line? Is the distinction a specious one? Businesses will take advantage of tax planning opportunities if there is a significant benefit to be gained and a reasonable likelihood of the planning not being challenged, though the uncertainties as to what in tax planning is still regarded as fair game and what is not is causing more and more taxpayers (both businesses and individuals) to avoid anything but 'plain vanilla' planning. With countries under pressure to raise tax revenues to plug spending deficits, a range of methods are being employed in order to do so. I would specifically mention a few of them. Firstly, a change of attitude by national tax authorities, which since the 2008 global financial crisis are taking a much more aggressive line in challenging tax planning that would have been considered perfectly acceptable only a few years earlier, before tax avoidance became divided, as explained in section 6.1, into that which is deemed acceptable and that which is deemed unacceptable by virtue of being 'abusive' or 'aggressive'<sup>255</sup>. Second, the amendment by tax authorities of certain reliefs and exemptions to include 'targeted' anti-avoidance rules to the effect that they will not apply in, broadly, situations that are deemed abusive, for example lacking in commercial substance and/or structured in an artificial way so as to benefit from the relief or exemption. Thirdly, the introduction

---

<sup>254</sup> See section 4.3.2 above on the Code of Conduct for Business Taxation and the increased resources allocated to the Code of Conduct Group, in particular to enable it to react more efficiently to cases of harmful tax competition, and its work in drawing up the EU's 'blacklist' of non-cooperative jurisdictions. These initiatives are an example of the Commission's use of soft law to achieve what is to all intents and purposes hard law.

<sup>255</sup> Taking the UK as an example, see HM Treasury/HM Revenue & Customs, 'Tackling Aggressive Tax Planning in the Global Economy: UK Priorities for the G20-OECD Project for Countering Base Erosion and Profit Shifting', Policy Paper published 19 March 2014, which refers to 34 separate measures passed by the UK since 2010 to clamp down on tax avoidance (p3, para 3) and the additional resources being allocated to HM Revenue & Customs to investigate the tax arrangements of multinationals (p3, para 3). The same pattern is being followed by tax authorities worldwide, not just in the EU.

by some tax authorities of a general anti-abuse (or anti-avoidance) rule ('GAAR'), typically (and quite deliberately) phrased in very broad terms and giving the tax authority the power to strike down any tax planning that smacks of abuse or artificiality and which is not susceptible to a targeted anti-abuse rule in the particular tax provision concerned. Typically both TAARs and GAARs give the tax authority more powers than they really need, and the tax authority then draws up a 'white list' of situations which they will not attack. Fourth, some tax authorities, for example the UK with its Advance Payment Notice scheme, have introduced a regime under which taxpayers employing certain types of tax avoidance schemes, generally of the more 'aggressive' variety, have to pay tax up-front as if they had not employed the scheme at all, then once the scheme has been litigated to its ultimate conclusion the tax will be refunded to the taxpayer in the event that they win: this has removed one of the main attractions of entering into tax avoidance schemes, which was not that the taxpayer necessarily expected to win at the end of the day but that they would be able to hold onto their money whilst the scheme was litigated, which could often take ten years or more, and only had to pay up if they finally lost the case. All these developments taken together have produced a highly uncertain and unsatisfactory situation, but it is undoubtedly the case that the availability of these anti-avoidance rules coupled with a much greater readiness on the part of tax authorities to use them has frightened many taxpayers into attempting nothing more than the most risk-free tax planning. In a real sense this represents a success for national tax authorities and the EU in their attempts, sometimes coordinated, sometimes not, to crack down on the more aggressive and egregious forms of tax planning. But is this 'climate of fear' a healthy one?

My own perspective is that of a tax practitioner, many of whose clients are businesses engaged in cross-border activity in both Member States and elsewhere in the world. From my own experience of talking to these clients, large as well as small, I have no hesitation in saying that what most of them want above all from the tax systems in which they operate is certainty and stability so that they can make long-term investment decisions. Business people are renowned for their optimism and willingness to embrace as opportunity what most of us would be more likely to see as a risk or problem. Certainly there are some in the business community who see this time of uncertainty as a

time of opportunity and relish the challenges, but my own experience suggests that these are very much a minority and that the great majority of business clients find the current situation extremely disquieting and inhibiting of their ability, and sometimes willingness, to make investment decisions for the long term.

There is also a definite issue with regard to the mixed messages coming from the EU itself. On the one hand there are reassuring statements such as those made by Stephen Quest (cited below) that corporate tax rates will remain a matter within Member States' sovereignty. On the other hand there are statements such as those recently made by Pierre Moscovici, the European Commissioner for economic and financial affairs, in a speech on 28 June 2017<sup>256</sup> at the Commission's Tax Fairness conference, where he claimed that: "Fairness in taxation should rest on...ensuring a level playing field, so that all taxpayers...are on an equal footing...". In the same speech he said in connection with the proposed CCCTB: "I do not think that we can reach a minimum rate – some might like it, but the rule of unanimity forbids it...". He concluded his speech by stating that, "I believe that we need more, not less, Europe in taxation".

Whatever mechanisms are employed to achieve it, a single market and monetary union surely demand in the long run a tax system that is more harmonised than merely co-ordinated. Would a federal system such as applies in countries such as the United States, Switzerland and Germany be a model, with a centrally imposed primary tax system with some discretion at the margins for Member States to impose limited and localised taxes, maybe at a regional level? Such a system has not been proposed by the Commission and the idea that the EU itself should have tax raising powers is anathema to most Member States (witness the controversy over the proposed Financial Transactions Tax).

The purpose of this work was to evaluate whether the existing mechanisms available to the EU were sufficient to achieve effective harmonisation of direct taxes. If the question is limited to whether the

---

<sup>256</sup> Pierre Moscovici, Speech to the Commission's Tax Fairness Conference, 28 June 2017, SPEECH/17/1828 available on European Commission Press Release Database. .

legal instruments passed thus far, and allowing for a degree of additional negative integration through future Court judgments and application of the State aid rules, have achieved effective harmonisation, the answer is emphatically not. If the question is whether the mechanisms available to the EU are sufficient to achieve such harmonisation if the Member States agreed to it, then the answer is an equally emphatic yes. It would be perfectly possible for directives to be passed providing for the complete harmonisation of Member States' tax systems, both as they apply to corporates, individuals and other taxpayers.

But is this likely to happen? As matters stand it seems inconceivable that the Member States would unanimously agree to such a move. The possibility that the Member States voluntarily decide to harmonise their direct tax regimes without intervention of any kind from the EU can be dismissed as fantastic. Is there likely to be a sudden outbreak of consensus between the Member States that total harmonisation is agreed to be the most principled and sensible way forward such that they all clamour to sign up to an EU directive? There is nothing to suggest that this is on the horizon. Would another economic downturn make Member States more willing to agree to large scale harmonisation? I would suggest that it would make them if anything all the more determined to retain control over their tax systems in order to try and undercut their Member State competitors.

Perhaps there will be no 'big bang' solution and the future will lie in the continuation of the creeping process of coordination and harmonisation premised on tackling tax abuse, avoidance and 'harmful' tax competition, coupled with the Court's efforts in removing discriminatory or restrictive tax measures, and an increasing use of State aid powers, until there comes a point when Member States' effective sovereignty over direct tax matters has been eroded to such an extent that it becomes obvious to everyone that it has become little more than an illusion and Member States actually come to welcome handing the whole troublesome business over to Brussels.

If both proposed stages of the revised CCCTB proposal are implemented, it would address a great many of the tax obstacles and distortions that the Commission has identified, but aside from the very large multinationals for whom it would be mandatory, it would only apply to those companies and

corporate groups that opted to participate. It would not apply at all to individuals or other taxpayers. At the present time there seems little likelihood of the CCCTB gaining the unanimous support of the Member States. It may very well be that there will be enough countries supportive of the proposal to adopt it under the enhanced cooperation procedure. If an attempt is made to obtain unanimous support by making concessions and allowing Member States a greater degree of flexibility in implementation, this may well bring some additional countries on board but may at the same time anger those countries who want less flexibility, not more, on the grounds that more concessions would undermine some of the central goals of the CCCTB, ie, consistency and certainty. As noted earlier, adoption under the enhanced cooperation procedure is intended to be a measure of last resort and would represent very much a second best outcome. Having some Member States participating and some not would add an additional layer of complexity to the operation of the scheme: for example, how would it apply where a multinational group has companies in both participating and non-participating Member States? Also as previously noted, leaving Member States free to set their own corporate tax rates would leave open the possibility of tax rate competition, which of itself can produce major distortions in the internal market. Corporate tax rates in the Member States currently vary from 9% to 35%<sup>257</sup> (though it must be said that 'headline' tax rates can be very misleading – Member States with low 'headline' tax rates are likely to apply them to very broad tax bases, and conversely those with high tax rates are more likely to apply them to relatively narrow tax bases, the result being that the effective tax rates across the Member States are likely to be within a much narrower range than the headline tax rates might suggest).

There is no indication, at least publicly, that the Commission intends to restrict Member States in the setting of their own corporate tax rates. On the contrary, Stephen Quest, Director General of the EU's Directorate-General for Taxation and Customs Union has stated in an article<sup>258</sup> that '...there is

---

<sup>257</sup> KPMG, 'Corporate Tax Rates Table 2017', available online at: <https://home.kpmg.com/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online/corporate-tax-rates-table.html> accessed 19 May 2018.

<sup>258</sup> Stephen Quest, 'Next Steps in Corporate Tax Policy: an EU Perspective', *Tax Journal*, 26 October 2016, Issue 1327, at penultimate section on 'Respecting national sovereignty', paras 1-3. Available online at:

one area which the CCCTB will not touch, *now or in the future* [my italics]. Tax rates remain an area of national sovereignty and Member States are free to decide their own rate for companies, both inside and outside the CCCTB structures. The Commission is highly vigilant as regards the fine balance between Member States' national sovereignty in tax matters and the need for EU action. This balance is further protected by the fact that EU tax rules are decided by unanimity'. He went on to make the interesting observation that '...I believe that Member States are gradually coming to realise that the real threat to their sovereignty does not lie in European level action. Rather, it comes from unrestrained tax competition and corporate avoidance, which erode their tax bases and destabilise their tax frameworks. It comes from mismatches between one national tax regime and another, which create legal uncertainty and administrative burdens for companies they are trying to attract. It comes from 28 uncoordinated approaches to taxation undermining the single market and the benefits it offers. In this respect, it can be argued that EU coordination on tax matters actually reinforces Member States sovereign rights in this area, rather than erodes it. It provides Member States with a collective strength and security, which allows them to focus on tax policies that truly meet their national needs.

Of course there are arguments to the contrary, that EU action undermines rather than reinforces the Member States sovereign rights. The statements just cited are of especial interest though, coming as they do from someone currently at the heart of EU policy making in this area.

As to whether the ability for Member States to set their own corporate tax rates will lead to a convergence or a race to the bottom, there is no consensus on which is the more likely outcome, so time will tell.

Businesses, particularly larger ones, will take advantage of tax planning opportunities if they are available, just as they would take advantage of other commercial opportunities in the marketplace. But above all most would prefer certainty and stability. The current situation possesses neither of

---

<<https://www.taxjournal.com/articles/next-steps-corporate-tax-policy-eu-perspective-12102016>> accessed 20 May 2018.

these attributes. Instead, there is what seems like almost constant change and tinkering by national tax authorities with their tax regimes as they respond with what seems like increasing desperation to each changing political wind that blows. Taxpayers operating cross-border in EU Member States (or their advisers) need to monitor not only changes in their own domestic tax systems but hard and soft law coming from the EU and developments in the Court's case law. Add to this the unprecedented shake-up of the international tax system currently being undertaken via the OECD/G20 BEPS programme and it is clear that businesses operating across-borders have never experienced such a period of uncertainty.

## 9.2 A radical, but flawed, solution?

A radical solution to these problems has been proposed by Luca Cerioni, to which he devotes almost half of his book *The European Union and Direct Taxation*, which is subtitled 'A solution for a difficult relationship'<sup>259</sup>.

Cerioni's bold approach would be to do away altogether with the current 'residence'-based tax system (ie, under which tax is charged on worldwide income by the jurisdiction in which a taxpayer is resident) and instead tax income only in the place in which it is generated. To the extent that Cerioni's notion is that tax should be charged in the jurisdiction in which a business's customers are located, on the basis that sales are the real origin of corporate income, this was widely mooted in the wake of the public revelations regarding the tax affairs of the likes of Amazon, Starbucks and Google. These multinationals were criticised for not paying enough tax in the jurisdictions in which they were making sales and thereby earning profits. Whilst Cerioni's proposal seems unobjectionable in principle, I believe it is based on some dangerous oversimplifications. Supposing a company in Member State A makes a product in its factory located in Member State A, and a customer in Member State B buys that product by placing an online order. Where is the 'sale' made in this case? Would it be right for the profit made on the sale to be taxed entirely in Member State B, where the

---

<sup>259</sup> Luca Cerioni, *The European Union and Direct Taxation* (Routledge 2015) p33.



company has had no activity or presence whatsoever? In the example I have just given what would Member State A say to the proposition that although a profit generating activity had been carried out entirely within its jurisdiction it has no right to tax any of the profit? It is a nonsense. A 'sale' is not necessarily generated where the customer happens to be located. Many of those who advocate taxation solely on a 'destination' basis, ie, where the customers are located, are confusing turnover with the activity that generated that turnover. Neither is turnover (ie, gross sales) synonymous with profit and, unlike VAT, corporate tax is levied on profits not gross turnover. A destination based approach for direct tax would suffer from a fundamental lack of symmetry between the income generated and where the costs are incurred to generate it, which is a principle the Court has shown its intention to safeguard through the justification of cohesion of Member States' tax systems.

If a purely destination based direct tax system were adopted it would be akin to a destination based VAT system. In any event, tax is charged by the country in which a business's customers are located: it is called VAT. That applying a destination based system to direct taxes rests on a number of fundamental misapprehensions does not seem to have registered with the general public (or, regrettably, a great many politicians).

Cerioni names his proposed regime the 'European Regime for Tax Compliance Simplification' ('ERTCS'). It would be a measure implemented at EU level and hence 'supranational'. Its cornerstone is a new concept of 'European tax resident', which would displace or override national tax residence. The EU would be treated as one jurisdiction for tax residence purposes; effectively EU residents would have a one-stop shop for tax purposes. Member States would no longer subject persons resident in their particular jurisdiction to taxation on their worldwide income. Taxpayers participating in the scheme would make a single tax return to a 'European One-Stop Shop' (EOSS) office, which would be independent of any Member State. A single unified tax return form would be submitted by the taxpayer to the EOSS. The form would show the categories of taxable income and the Member States in which the income arose, and include a determination of the amount of tax due to each Member State. The EOSS office would deal with the checking of the return, the collection of

payment from the taxpayer and the distribution of that payment as between the relevant Member States. Capital gains would presumably be reported and taxed in the same way. Cerioni is silent as to whether under the ERTCS each Member State would be free to set their own tax rate to apply to the income apportioned to it (as under the CCCTB).

The ERTCS would have many of the benefits that the CCCTB would bring for companies, except that the ERTCS would apply to other types of taxpayer. Compliance costs would be reduced for those taxpayers currently subject to tax in more than one Member State, double taxation eliminated and residence jurisdiction shopping rendered pointless except to the extent that tax competition would still exist in the form of tax rate differentials (assuming the ERTCS permitted the Member States to set their own rates).

Cerioni admits that the ERTCS would be a challenge to the current international tax order (which is something of an understatement), but so to a large extent would the CCCTB. Cerioni sees the ERTCS as complementary to the CCCTB, envisaging that the CCCTB could apply to companies whilst the ERTCS applied to other taxpayers, or, alternatively, that the ERTCS could be adapted to cater for companies as well as other taxpayers in which case there would be no need for a separate CCCTB.

Cerioni makes the claim, which at first sight might appear counter-intuitive, that far from eroding the sovereignty of the Member States in direct tax matters, the ERTCS would in fact safeguard it from further erosion. The basis for this claim is that the current national residence-based tax system is increasingly unable to protect Member States' tax revenues from erosion by tax competition and tax-related distortions in the internal market. By replacing the national residence based system with one in which income is taxed where it arises, tax competition and distortions would largely fall away, with the result that Member States' tax revenues are stabilised and not continually eroded by a race to the bottom in terms of tax competition. It appears to me, however, that not all countries would necessarily stand to benefit from the ERTCS to the same degree. For example a Member State might lose more revenue by no longer subjecting resident companies to worldwide taxation than it gains by being able to tax non-resident companies on income or profits arising in its jurisdiction; this is

particularly the case since even under the current residence based system of taxation most if not all Member States tax profits generated in their jurisdiction through a branch of a foreign company, and levy tax (by way of withholding taxes) on passive income such as interest and dividends that arises in the jurisdiction. A country like the UK, for example, would not gain much under the ERTCS as it already taxes non-residents on profits or other income that arises in its jurisdiction, but it could lose a lot by no longer being able to subject UK companies to taxation on their worldwide income and gains. No Member State would sign up to such a proposal unless it had been rigorously costed. Given that the international tax system already permits a jurisdiction to tax non-residents on profits and income arising in the jurisdiction, it seems to me that Cerioni rather overestimates the significance of residence; certainly it is the most significant nexus for the imposition of tax, but it is by no means the only one.

Cerioni proposes that the ERTCS would be optional, at both Member State and taxpayer levels. As with an optional CCCTB, the same tax problems would continue to exist for those Member States and taxpayers not participating, and Member States' tax compliance costs would increase through having to continue running their existing tax regime in parallel with their contributions towards the costs of running the EOSS.

Cerioni's proposal is certainly a bold one, but if the CCCTB is proving difficult enough to sell to the Member States, his ERTCS scheme seems altogether too left field to be taken seriously. At least the CCCTB confines itself to corporate tax, whereas the ERTCS would apply to all taxes and all types of taxpayer. This is simply far too ambitious to achieve in a single step. In addition, having the tax system administered through a supranational EOSS instead of through Member States' own tax authorities would make it extremely hard for Member States to convince their voting public that they had not to all intents and purposes simply given up on tax sovereignty.

On a more general point, Cerioni considers that distortions and lack of tax neutrality are a reason for Euroscepticism. An alternative view might be that a cause of Euroscepticism is the fact that Member States are being prohibited from being as competitive as they might ideally like to be on taxes

because they would be accused of indulging in ‘harmful’ tax practices. Why is competition generally seen as a good thing and Member States that try to suppress competition in other fields are likely to face proceedings by the Commission, but competition in the tax field is to be frowned upon? The Commission needs to come up with a convincing explanation.

### **9.3 Can direct tax harmonisation be achieved through the existing mechanisms and instruments?**

This thesis set out to address the question “Are the existing mechanisms and instruments available to the institutions of the EU sufficient to achieve effective harmonisation of Member States’ direct tax regimes?”

It is clear that we do not have an effectively harmonised direct tax system at the present time.

Are the existing mechanisms and instruments available to the EU sufficient to achieve effective harmonisation in the future? Without unanimous Member State agreement to facilitate legislation, then in my opinion no. The Court’s jurisprudence is of application in only limited areas. The same can be said of the State aid provisions, despite the Commission’s evident ambitions in this area. It will be interesting indeed to see what the result of Ireland’s appeal in the Apple case is and whether it curbs these ambitions or fuels them. Soft law is of its nature unenforceable. Such contributions as any of these mechanisms make towards harmonisation are necessarily piecemeal and negative in nature. As to the positive hard law so far implemented, it covers only limited and specific areas. None of it can be said to amount to the basis of a comprehensive tax regime. The CCCTB will be a big step forward if it is ever implemented in its present form, which remains to be seen though current indications do not seem promising.

Does Europe need more tax harmonisation? In my opinion, yes. The existence of 28 different national tax systems, with a degree of coordination that despite what the Commission and the Court has so far managed to achieve can at best be described as limited, gives rise to too many disparities, mismatches and obstacles, which adversely affect the functioning of the internal market and distort

the conditions of competition within the internal market. The primary gainers are the sophisticated tax avoiders who can exploit the differences and mismatches. The loser is the EU taken as a whole through the overall loss of tax revenues that results from tax avoidance.

BEPS will cut some of the ground from under the tax avoiders' feet, but again the BEPS measures are necessarily negative in terms of their influence on integration, and anti-avoidance measures are no substitute for a coherent positive tax regime.

#### **9.4 Is there a way forward?**

Do I see a realistic way forward? Yes. I believe that a common EU wide direct tax system is a realistic possibility provided it is designed with a view to Member States' sensibilities on tax sovereignty. I certainly believe that most EU businesses operating cross-border will welcome such a system. Truth be told it tends to be only the largest multinationals that employ the types of tax avoidance scheme that so vex the Commission. I believe that most businesses would welcome a common tax system if it leads to stability, certainty and significant savings in their tax compliance costs. The problem for the Commission is not in persuading businesses of the merits of a common tax system, but in persuading governments.

A common EU-wide tax system would in my view have to incorporate the following key features.

- It would be limited to corporate and business taxes. This is by far the biggest priority and to try and introduce a new scheme covering all types of taxes and taxpayer would make it far too complicated and make the task of obtaining Member States' agreement much harder.
- It would have to be introduced through binding hard law.
- It would not involve total harmonisation, which is neither necessary nor desirable. A degree of latitude should be permitted to Member States both as regards tax rates and the tax base.
- Implementation through directives would be more practical than through regulations (in any event directives are the only legal instruments available under the Article 115 or 116 legal bases).

- A minimum rate of corporate tax should be set but no maximum. Failure to set a minimum rate could lead to significant distortions through aggressive tax rate competition.
- It would involve a common corporate tax base. The latitude allowed to Member States in determining the tax base should be strictly limited to avoid tax base competition. In this regard the VAT system with its host of derogations, exemptions, and special regimes does not constitute a model to be followed.
- The Scheme must be easy to understand and easy to administer. This of itself would result in significant compliance cost savings. Again, the VAT system would not be a model to follow in this regard.

How would such a system compare with the proposed CCCTB? The most significant difference is that whilst both involve a common tax base with only limited scope for Member State discretion, a scheme along the above lines would not require the second part of the CCCTB proposal, ie, a consolidation of group profits and a formulary apportionment of those profits as between the Member States in which the group operates. Admittedly, this aspect of the CCCTB could result in significant cost savings which would not be replicated in the scheme outlined above. However, the consolidation and formulary apportionment aspect is what is frightening a number of Member States about the CCCTB proposal. A common tax base combined with much more convergence on tax rates as proposed under the above scheme would still largely remove the conditions for tax avoidance *ex ante* without the need for consolidation and formulary apportionment. Apart from harmonising the tax base and setting a minimum corporate tax rate, the above scheme would not affect the current tax compliance system. Companies would continue to be tax resident in their home Member State, make tax returns in every country in which they do business and they would have to continue to apply transfer pricing to their intra-group transactions. Despite the potential compliance costs foregone as compared with the CCCTB, retaining the existing tax compliance system virtually intact could actually be seen as a positive feature of the alternative scheme, as Member States, tax authorities and businesses are all used to it. Moving straight to a common tax base and a

consolidation and formulary apportionment system would on the other hand be a leap in the dark for all concerned.

A scheme along these lines would virtually eliminate harmful tax base competition in the EU.

Allowing the Member States to set their own corporate tax rates would allow for an element of tax rate competition, but setting a minimum rate would limit this and should ensure that competitive distortions are kept within manageable proportions.

Ideally unanimous Member State agreement would be obtained for such a scheme, in which case Article 115 could be used as the legal basis. Failing unanimity, consideration could be given to using Article 116, whilst though it appears legally unobjectionable would be fraught with political difficulties. If at least nine Member States support the proposal, it could as a last resort be implemented by those Member States through the enhanced cooperation procedure. In the event that the scheme proves a success and participating Member States' corporate tax revenues are shown not to have been reduced, other Member States might be persuaded to join in.

At the present time, any proposal involving direct tax must enable Member States to retain at least a semblance of sovereignty over their tax affairs if it is to have any chance of implementation. If Member States were to agree to a common tax base but retain the right to set their own tax rates, perhaps subject to a minimum rate, would this be enough for them to be able to claim to have retained a meaningful degree of sovereignty over direct taxes? Possibly.

The issue of sovereignty is clearly a sensitive one, as many believe that the European 'project' requires an inexorable erosion of the Member States' sovereignty over their tax affairs. But isn't the reality that the Member States abandoned that sovereignty to the markets long ago?

As to Brexit, the nature and extent of the UK's future engagement with the EU VAT and Customs systems is clearly of huge importance to businesses, both in the UK and other Member States, which engage in cross border trade. At the time of writing there is very little clarity as to what form those future arrangements might take.

In the direct tax context, Luca Cerioni in a recent article<sup>260</sup> identified two interconnected questions that Brexit throws up. One is the extent to which the UK will continue to be bound by EU direct tax legislation and case law as part of any deal with the EU, or by any other agreements or undertakings the UK may enter into with the EU, for example to refrain from 'harmful' tax competition. The other question is whether Brexit makes it more likely that the remaining Member States will more readily accept tax harmonisation measures, and especially the revised CCCTB proposal, given that the UK had been one of the most consistent opponents of tax harmonisation. For the present the answer to both questions can only be that it remains to be seen.

Though not referred to in Cerioni's article, there is perhaps a third question which Brexit poses, namely, whether Brexit will have any influence on the Commission's general direction of travel, not just in the tax field. Might it feel that its best policy is to press for deeper and faster integration on as many fronts as possible so as to make it almost a practical impossibility for other Member States to leave? Or might it feel that the opposite approach, ie, less integration, would be more advisable to defuse the pressure that Member States have come under from disgruntled voters. It will be fascinating to see which direction the Commission takes.

---

<sup>260</sup> Luca Cerioni, 'Brexit and Direct Taxation: A Turning Point for EU Tax Law?', 20 December 2017, Edinburgh Europa Institute, available online at: <<http://www.europeanfutures.ed.ac.uk/article-5719>> accessed 19 May 2018.



# BIBLIOGRAPHY

## Books

- Barents, R *Directory of EC Case Law on Direct Taxation* (Wolters Kluwer 2009)
- Barnard, C & Scott, J *The Law of the Single Market: Unpacking the Premises* (Hart Publishing 2002)
- Bobek, M *The Court of Justice of the European Union* (College of Europe, Research Paper in Law, 02/2014)
- Bond, S et al (contributors) *Corporate Tax Harmonisation in Europe: a Guide to the Debate* (Institute for Fiscal Studies 2000)
- Brokelind, C (editor) *Towards a Homogenous EC Direct Tax Law* (IBFD 2007)
- Cerioni, L *The European Union and Direct Taxation: a Solution for a Difficult Relationship* (Routledge 2015)
- Cerioni, L *EU Corporate Law and EU Company Tax Law* (Edward Elgar Publishing 2007)
- Connolly, B *The Rotten Heart of Europe* (Updated edition, Faber 2013)
- Cotrut, M (managing editor) *ECJ Direct Tax Compass 2017* (IBFD 2017)
- Dahlberg, M *Direct Taxation in Relation to the Freedom of Establishment and the Free Movement of Capital* (Kluwer 2005)
- Dourado, A, da Palma Borges, R *The Acte Clair in EC Direct Tax Law* (IBFD 2008)
- Easson, A *Taxation in the European Community* (Athlone Press 1993)

- Ernst & Young *The Future of Corporate Income Tax in the European Community* (Kogan Page 1992)
- Essers, P, de Bont, G, Kemmeren, E *The Compatibility of Anti-Abuse Provisions in Tax Treaties with EC law* (Kluwer 1998)
- Ghosh, J *Principles of the Internal Market and Direct Taxation* (Key Haven 2007)
- Gonzalez Sanchez, E *Corporate Tax Harmonisation in the European Union* (Universidad del Pais Vasco 2005)
- Gormley, L *EU Taxation Law* (Oxford University Press 2005)
- Gribnau, H *Legal Protection Against Discriminatory Tax Legislation* (Kluwer 2003)
- Heidenbauer, S & Stuerzlinger, B *The EU's External Dimension in Direct Tax Matters* (Linde Verlag 2010)
- Helminen, M *EU Tax Law – Direct Taxation* (IBFD 2009)
- Hindelang, S *The Free Movement of Capital and Foreign Direct Investment: the Scope of Protection in EU Law* (Oxford University Press 2009)
- Hoskins M & Robinson W (editors) *A True European: Essays for Judge David Edward* (Hart Publishing 2003)
- Jansen, S (editor) *Fiscal Sovereignty of the Member States in an Internal Market: Past and Future* (Wolters Kluwer 2011)
- Jovanovic, M *International Handbook on the Economics of Integration, Vol II* (Edward Elgar Publishing 2011)

- Koutrakos, P & Snell, J *Research Handbook on the Law of the EU's Internal Market* (Edward Elgar Publishing 2017)
- Lang, M *Direct Taxation: Recent ECJ Developments* (Kluwer 2003)
- Lang, M & Pistone, P *The EU and Third Countries – Direct Taxation* (Kluwer 2008)
- Lang, M, et al (contributors) *ECJ – Recent Developments in International Taxation* (Linde Verlag/Kluwer 2006)
- Lang, M, et al (editors) *Introduction to European Tax Law: Direct Taxation* (3<sup>rd</sup> edition, Spiramus Press 2013)
- Meussen, G (editor) *The Principles of Equality in European Taxation* (Kluwer 1999)
- Micheau, C *Tax Selectivity in European Law of State Aid: Legal Assessment and Alternative Approaches* (University of Luxembourg Law Working Paper Series, Paper number 2014-06, July 2014)
- Mullan, R & Brown H *The Interaction of EU Treaty Freedoms and the UK Tax Code* (Key Haven 2011)
- Panayi, C *Double Taxation, Tax Treaties, Treaty Shopping and the European Community* (Kluwer 2008)
- Panayi, C *European Union Corporate Tax Law* (Cambridge University Press 2013)
- Pinto, C *Tax Competition and EU Law* (Kluwer 2003)
- Pirvu, D *Corporate Income Tax Harmonisation in the European Union* (Palgrave Macmillan 2012)

- Pistone, P *The Impact of Community Law on Tax Treaties: Issues and Solutions* (Kluwer 2002)
- Radaelli, C *The Politics of Corporate Taxation in the European Union* (Routledge 1997)
- Richelle, I, Schoen, W & Traversa, E *State Aid Law and Business Taxation* (Springer-Verlag 2016)
- Stevens, L (editor) *Harmonisation of Company Taxation in the European Community* (Kluwer 1992)
- Teixeira, G *Business Taxation in the European Union* (Wiley Chancery 1994)
- Terra, B & Wattell, P *European Tax Law* (6<sup>th</sup> unabridged edition, Wolters Kluwer 2012)
- Terra, B & Wattel, P *European Tax Law* (Abridged edition, Wolters Kluwer 2012)
- van Raad, K (editor) *Materials on International and EU Tax Law, Volume 2* (12<sup>th</sup> edition, Leiden, International Tax Center 13)
- Van Thiel, S *EU Case Law on Income Tax* (IBFD 2001)
- Van Thiel, S *Free Movement of Persons and Income Tax Law: the European Court in Search of Principles* (IBFD 2002)
- Weber, D *Tax Avoidance and the EC Treaty Freedoms* (Kluwer 2005)
- Weber, D (editor) *The Influence of European Law on Direct Taxation: Recent and Future Developments* (Kluwer 2007)
- Williams, DW *EC Tax Law* (Longman 1998)

## Articles

Stephen Coleclough 'Getting Stuck In!', *Tax Adviser Magazine* June 2013, p4

Stephen Coleclough 'Incoming CIOT', *Tax Adviser Magazine*, June 2013, pp18-20

Joe Dalton, 'ECJ's Ruling on Spanish Exit Tax Creates Uncertainty for MNCs', *International Tax Review* June 2013, p6

Guido De Wit, 'The European VAT experience', *Tax Notes International* (1995) 10(2), pp49-54

Bill Dodwell, 'Building Blocks: the Application of State Aid Rules in Recent Incidents', *Tax Adviser*, October 2016, p14

Sjoerd Douma, 'BEPS and European Union Tax Law', *Cahiers de droit fiscal international*, Vol 102a, Sdu: The Hague 2017, pp65-95

Joe Duffy & Tomas Bailey, 'The Anti-Tax Avoidance Directive in Ireland: Winds of Change or an Easterly Breeze', *Irish Tax Review* 2016, issue 4, pp106-112

Michelle Everson, 'Is the European Court of Justice a Legal or Political Institution Now?', *The Guardian*, 10 August 2010

JP Finet, 'Hybrid Mismatch Rules Expected to Raise Issues for CJEU', *Tax Notes International*, 84(3) (2016), p244

Hans Gribnau, 'Soft Law and Taxation: EU and International Aspects', [2008] *Legisprudence* Vol 2 No 2, pp67-117

Conor Kennedy, 'Exit Taxes – the New Dimension', *Irish Tax Review* November 2009, pp65-68

Neelie Kroes, 'Why EU State Aid is Not the Right Tool to Fight Tax Avoidance', *The Guardian*, 1 September 2016

Michael McGowan, 'European Commission v Portuguese Republic: Implications for Exit Taxes in the EU', *British Tax Review* 2013, 1, 15-21

Tom O'Shea, 'Portuguese Exit Taxes Successfully Challenged by European Commission', *Tax Notes International* January 28 2013, pp371-374

Christiana Panayi, 'Exit Taxation as an Obstacle to Corporate Emigration from the Spectre of EU Tax Law', [2011] *Cambridge Yearbook of European Legal Studies*, pp245-281

Christiana Panayi, 'National Grid Indus BV v Inspecteur van de Belastingdienst Rijnmond/Kantoor Rotterdam: Exit Taxes in the European Union Revisited', *British Tax Review* 2012, 1, 41-49

Stephen Quest, 'Next Steps in Corporate Tax Policy: an EU Perspective', *Tax Journal*, 26 October 2016, Issue 1327

Franz Vanstendael, 'The Ruding Committee Report: A Personal View', *Fiscal Studies* Vol 13, No 2, May 1992

Melchior Wathelet, 'The Influence of Free Movement of Persons, Services and Capital on National Direct Taxation: Trends in the Case Law of the Court of Justice', *Yearbook of European Law*, Vol 20, issue 1, 1 January 2001 pp1-33

Jeanette Zaman, 'Exit Taxes: an Infringement Deferred?', *Tax Journal* 1 February 2013, pp17-18

## **Material published online**

### **Articles**

Luca Cerioni, 'Brexit and Direct Taxation: A Turning Point for EU Tax Law?', 20 December 2017, Edinburgh Europa Institute, available online at: <<http://www.europeanfutures.ed.ac.uk/article-5719>>

The Hon. Sir Launcelot Henderson, 'Forty Years On: is the EU Tax Tide Still Rising', The 2013 Chartered Tax Adviser Address for the Chartered Institute of Taxation

Institute of Chartered Secretaries & Administrators, 'The EU, tax and the Apple of its Ire', 10 November 2017, available online at: <<https://www.icsa.org.uk/knowledge/governance-and-compliance/indepth/technical/eu-tax-apple-legal-case>>

Adelina Marini, 'The Second CCCTB Proposal Seems Also Headed for a Failure', 12 June 2017, <<http://www.euinside.eu/en/news/the-second-ccctb-proposal-seems-to-be-headed-for-another-failure>>

Agata Uceda, 'Norway Modifies Exit Tax Rules to Comply with ECJ Ruling', DLA Piper 26 June 2012. [www.dlapiper.com](http://www.dlapiper.com)

Agata Uceda & Sirathorn Dechsakulthorn, 'In Wake of ECJ Ruling, EU Member States Amend Exit Tax Regimes', DLA Piper 21 March 2013. [www.dlapiper.com](http://www.dlapiper.com)

Unattributed, 'ECJ Rules Against Spanish Exit Tax' Ernst & Young, 26 April 2013. [www.ey.com](http://www.ey.com)

Unattributed, 'Exit Tax in Portugal – In Which Direction it Should Go [sic]?', Inside Tax Reform, 30 March 2013. [www.insidetaxreform.blogspot.co.uk](http://www.insidetaxreform.blogspot.co.uk)

Unattributed, 'CJEU: Danish Exit Taxation is Contrary to EU Law', Kromann Reumert, 22 July 2013. [www.kromannreumert.com](http://www.kromannreumert.com)

Unattributed editorial, 'Spotlight on the EU Code of Conduct Group', 4 July 2017. Available online at: <[https://www.tax-news.com/features/Spotlight\\_On\\_The\\_EU\\_Code\\_Of\\_Conduct\\_Group\\_\\_574446.html](https://www.tax-news.com/features/Spotlight_On_The_EU_Code_Of_Conduct_Group__574446.html)>

Aidan Walsh, 'Who's Afraid of the ECJ – Not Ireland Any More!', Finance Magazine, August 2007, available online at: <[http://www.finance-magazine.com/display\\_article.php?i=7667&pi=271](http://www.finance-magazine.com/display_article.php?i=7667&pi=271)>

### ***Other online material***

Deloitte, 'BEPS Actions Implementation by Country', available at:

<<https://www2.deloitte.com/global/en/pages/tax/articles/beps-action-implementation-matrices.html>>

OECD, 'The OECD work on Base Erosion and Profit Shifting', 4 February 2013. Available online at:

<https://www.oecd.org/ctp/TheOECDworkonBEPS.pdf>

Unattributed, 'ECJ: Exit Charges Allowed but Company Must be able to Defer Payment', Practical Law

12 January 2012. [www.uk.practicallaw.com](http://www.uk.practicallaw.com)

Unattributed, 'Corporation Tax: Exit Tax: Deferred Payment Option', Practical Law 25 January 2012.

[www.uk.practical law.com](http://www.uk.practical law.com)

Unattributed, 'Commission Challenges UK Corporate Exit Charges', Practical Law, 27 March 2012.

[www.uk.practicallaw.com](http://www.uk.practicallaw.com)

Unattributed, 'ECJ: Advocate General Further Considers Exit Charges', Practical Law, 9 July 2012.

[www.uk.practicallaw.com](http://www.uk.practicallaw.com)

Unattributed, 'ECJ Holds Portuguese Exit Charges Contrary to EU Law', Practical Law, 7 September

2012. [www.uk.practicallaw.com](http://www.uk.practicallaw.com)

Unattributed, 'Deferring Payment of Corporate Exit Charges: Draft Finance Bill 2013 Provisions and

Consultation Document', Practical Law, 27 December 2012. [www.uk.practicallaw.com](http://www.uk.practicallaw.com)

Unattributed, 'Deferral of Payment of Exit Charge: Finance Bill 2013', Practical Law, 16 April 2013.

[www.uk.practicallaw.com](http://www.uk.practicallaw.com).

Unattributed, 'ECJ Direct Tax Cases: Where Are They Now?', Practical Law, maintained resource.

[www.uk.practicallaw.com](http://www.uk.practicallaw.com)