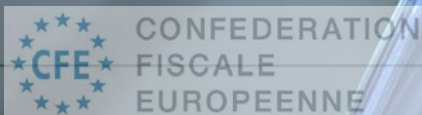


*The ATOZ Chair for European and International Taxation
welcomes you to:*

TIME AND TAX

TAX TREATIES, EU LAW AND CONSTITUTIONAL ASPECTS



RUL | RESEARCH UNIT
IN LAW



Conference Programme

- 08:30

Registration
- 09:00

Opening of the Conference
- 09:15 - 10:15

Time and Tax Treaties: Allocation rules
Chair: Pasquale Pistone

Time and Distributive Rules in Tax Treaties
Georg Kofler, JKU Linz
&
Alexander Rust, WU Wien

Temporal Aspects of Passive Income
Daniel Smit, Tilburg University

Coffee Break

10:45 - 12:15

Time and Tax Treaties: Relieving Provisions
Chair: Werner Haslehner

Time and Double Taxation Relief
Joanna Wheeler, University of Amsterdam

Entry into Force and Termination of Tax Treaties
Mario Tenore, Maisto e Associati

Timing Disadvantages and Tax Treaty Non-Discrimination
Niels Bammens, University of Leuven

Walking Lunch

13:30 - 15:00

Time and EU Tax Law I
Chair: Eric Kemmeren

An Ever-closer Union? Evolution, Revolution and the Value of Precedents in EU Tax Law
Ieva Freija, Court of Justice of the EU

Temporal Aspects of ECJ Judgments
Alfredo García Prats, University of Valencia

Tax Deferral and EU Freedoms: Exit Tax, Recapture, and Neutralization
Karoline Spies, WU Wien

Coffee Break

15:30 - 17:00

Time and EU Tax Law II
Chair: Georg Kofler

Temporal Aspects of EU Tax Legislation
Dennis Weber, University of Amsterdam, Loyens & Loeff

Time, Tax, and the Fiscal Merger Directive
Frederik Boulogne, PWC & VU Amsterdam

The Evolution of the Internal Market and the Application of State Aid Law to Tax Rules
Edoardo Traversa, University of Louvain &
Alice Pirlot, University of Louvain (FNRS)

Coffee Break

17:15 - 19:00

Time, Constitutional Law, and Tax Policy
Chair: Alexander Rust

Effective Legal Remedies and Fair Trial in Tax and Time
Katerina Pantazatou, University of Luxembourg

Constitutional Limits to Retroactivity in Tax Law
Serge Schroeder, Cour Administrative de Luxembourg

Timing Taxation: Constitutional and Economic Perspectives
Werner Haslehner, University of Luxembourg

19:00

Closing of the conference

TIME AND DISTRIBUTIVE RULES IN TAX TREATIES



Georg Kofler/Alexander Rust

OVERVIEW

■ Time and Treaty Application

- ☐ Entry into Force, Termination
- ☐ Arts 28, 70 VCLT

■ Time in Distributive Rules, e.g.,

- ☐ Art 5 OECD-MC → “fixed”, “more than twelve months”, “habitually”
- ☐ Art 10 OECD-MC (new) → “throughout a 365 day period”
- ☐ Art 13(4) OECD-MC (new) → “at any time during the 365 days preceding the alienation”
- ☐ Art 15 → “183 days in any twelve month period”
- ☐ Art 18 → “consideration of past employment”
- ☐ Art 20 → “immediately before”

■ Accrual versus Realization versus Payment

- ☐ Subsequent Income
- ☐ Preceding Income
- ☐ Gain in Taxing Rights
- ☐ Loss in Taxing Rights
- ☐ Entry and Exit / Triangular Cases

ARTICLE 15: SUBSEQUENT INCOME

Residence State



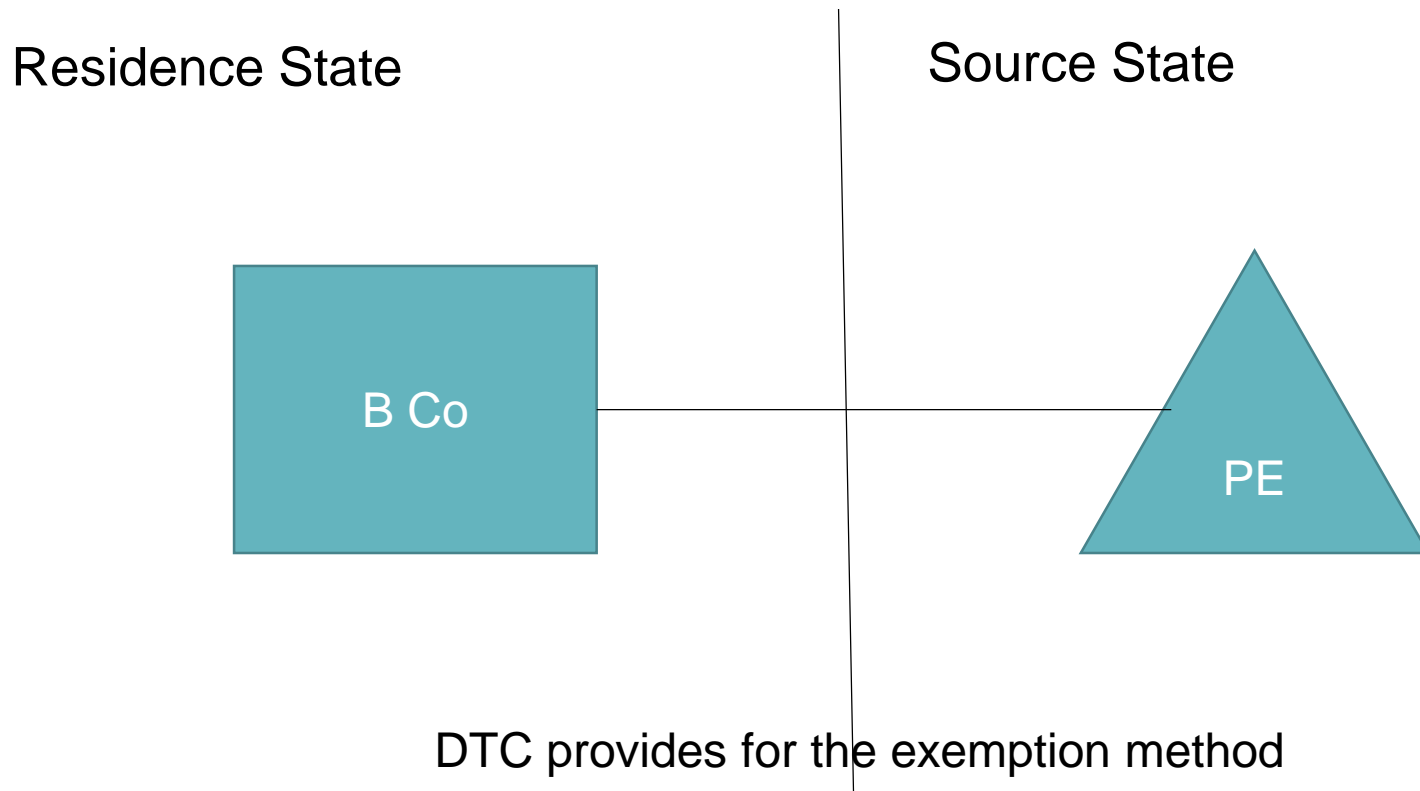
Source State

Taxpayer worked for more than 183 days in Source State

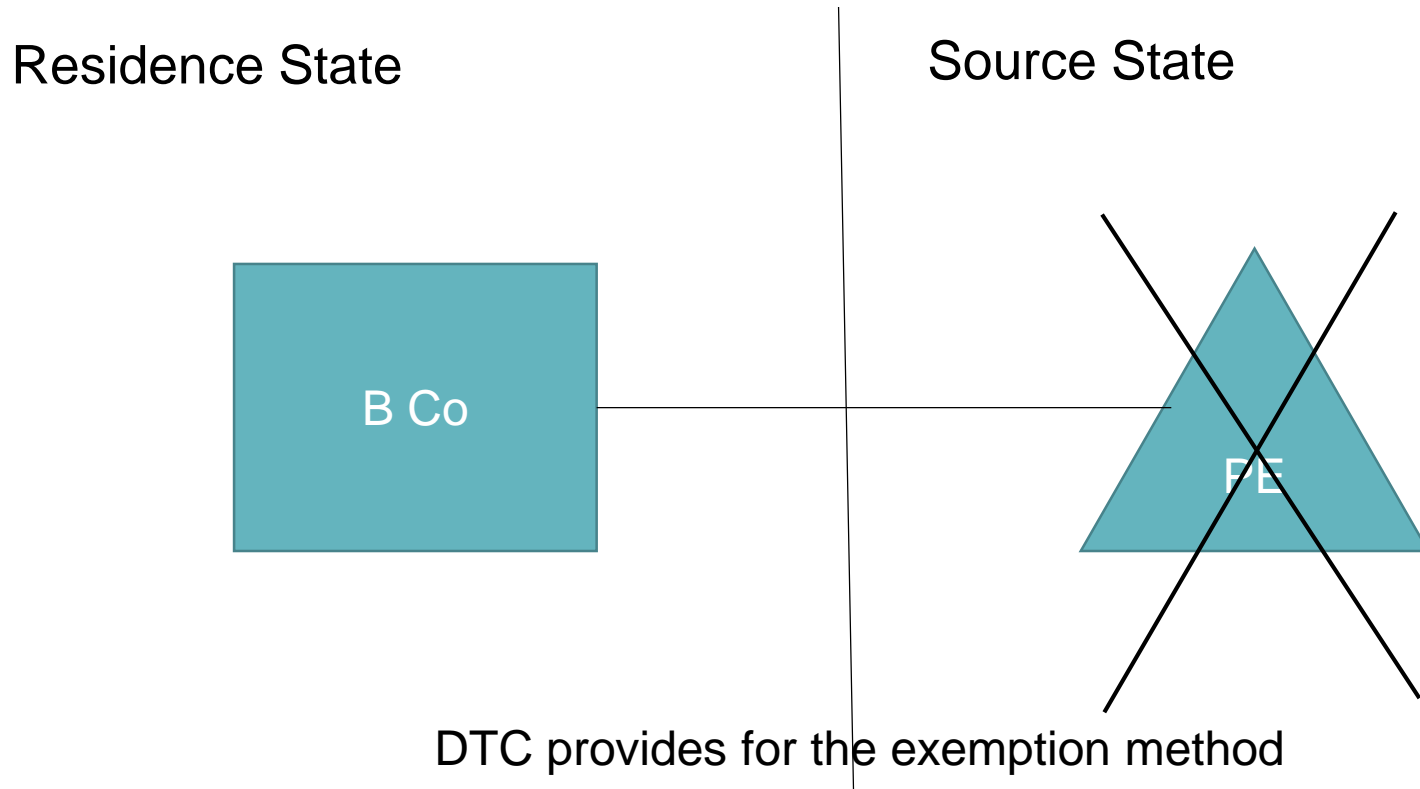
OECD Commentary Article 15 par. 2.4:

Any remuneration paid after the termination of employment for work done before the employment was terminated (e.g. a salary....) will be considered to be derived from the State in which the relevant employment activities were exercised.

ARTICLE 7: SUBSEQUENT INCOME



ARTICLE 7: SUBSEQUENT INCOME



ARTICLE 7 SUBSEQUENT INCOME

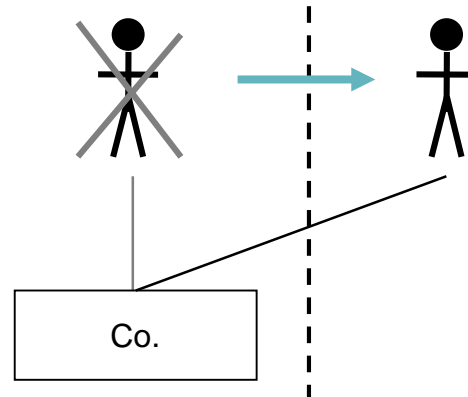
- **Wording:** “carries on” business through a
pe situated in the other Contracting State
- **Principle of causation**
=> Exemption in Residence State / limited tax
liability in the Source State.

ARTICLE 7 PRECEDING INCOME

- **Expenses** made before the permanent establishment is set up.
- **Principle of causation?**
- **Linked** to a future permanent establishment.
- What if permanent establishment never comes into being? **Intention** sufficient?
- Domestic law: preliminary assessment.

GAIN IN TAXING RIGHTS

■ Example 1: Immigration with Shares



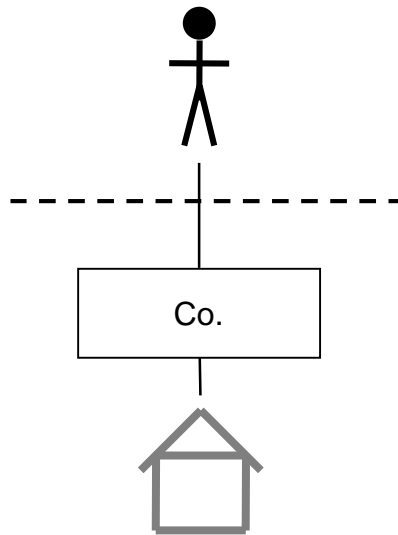
- Does Art 13 OECD MC preclude taxation of “imported” capital gains, e.g., through immigration or conclusion of a new treaty? → Art 13 No 3.1 OECD MC Comm. (and also, e.g., Austrian EAS 2955):

Also, where the Article allows a Contracting State to tax a capital gain, this right applies to the entire gain and not only to the part thereof that has accrued after the entry into force of a treaty (subject to contrary provisions that could be agreed to during bilateral negotiations), even in the case of a new treaty that replaces a previous one that did not allow such taxation.

- No step-up required → E.g., Nos 65-67 BEPS Final Report on Action 7 (2015) and Art. 23 Nos 4.1-4.3 OECD MC Comm.; BFH, 30 March 1993, VIII R 44/90

GAIN IN TAXING RIGHTS

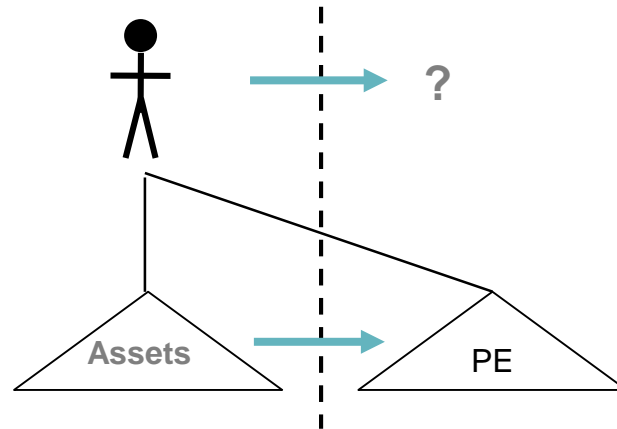
■ *Example 2: Change of Facts (e.g., “land richness”)*



- ☐ Does Art 13(4), (5) OECD MC prohibit Source State taxation of those capital gains that accrued before the company became “land rich”?

LOSS IN TAXING RIGHTS

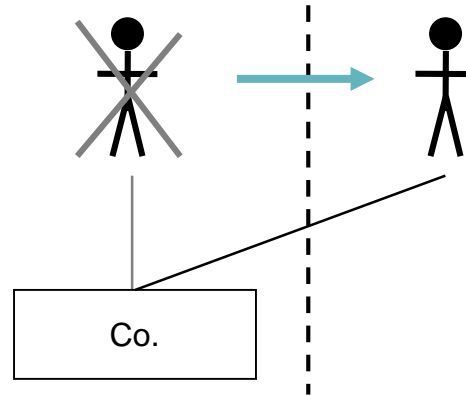
■ Example 1: Transfer of Assets or Permanent Establishments



- ☐ Does Art 13(2) OECD MC permit taxation of hidden reserves that accrued before the transfer? → See BFH 17 July 2008, I R 77/06; BFH 28 October 2009, I R 99/08; BFH 28 October 2008, I R 28/08
- ☐ Tax Base?
- ☐ What about exit taxation?
 - Not prohibited by Art 7, 13 or 18 (Nos 65-67 BEPS Final Report on Action 7 (2015)), because „provisions of tax treaties do not govern when income is realised for domestic tax purposes”
 - Different, e.g., South African Supreme Court of Appeal, 8 May 2012, *Commissioner for the South African Revenue Service v Tradehold Ltd* (132/11) [2012] ZASCA 61

LOSS IN TAXING RIGHTS

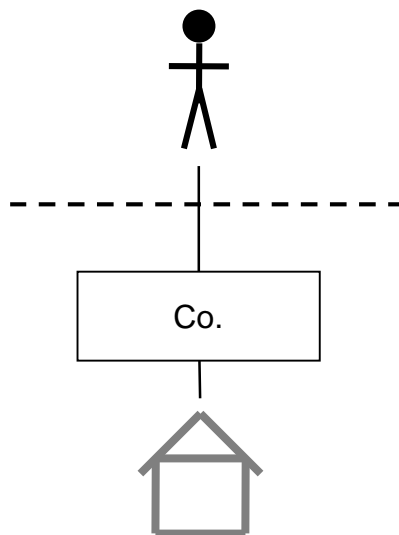
■ *Example 2: Emigration with Shares*



- ☐ Does Art 13 OECD MC prohibit taxation of “exported” capital gains, e.g., through emigration or conclusion of a new treaty?

LOSS IN TAXING RIGHTS

■ *Example 3: Change of Facts (e.g., “land richness”) or Conclusion of New Treaty*



- ☐ Does Art 13 OECD MC prohibit Residence State taxation of those capital gains that accrued before the company became “land rich”? Or before the tax treaty was concluded?
- ☐ Art 13 No. 32.1 OECD MC Comm. (and, e.g., Austrian EAS 3293):

Observation on the Commentary

32.1 With respect to paragraph 3.1, Austria and Germany hold the view that when a new tax treaty enters into force, these countries cannot be deprived of the right to tax the capital appreciation which was generated in these countries before the date when the new tax treaty became applicable.

☐

TRIANGULAR CASES

Old Residence State

Source State



New Residence State

TRIANGULAR CASES

Old Residence State



Source State

New Residence State

Is New Residence State
restricted by DTC Old
Residence State / Source
State?

TIME AND DISTRIBUTIVE RULES IN TAX TREATIES



Thank you for your attention!



Temporal Aspects of Passive Income

Luxembourg, 26 January 2017,
Time & Tax" Conference
Prof.dr. D.S. Smit

Temporal Aspects of Passive Income: General Introduction

- Typically, timing issues under DTCs – both for passive and passive income – may arise when:
 - A new DTC rule becomes applicable as a result of a legal change of the DTC;
 - A new DTC rule becomes applicable as a result of a change in the factual situation of the taxpayer

Temporal Aspects of Passive Income under Dutch (Domestic) Law: Compartmentalization Doctrine

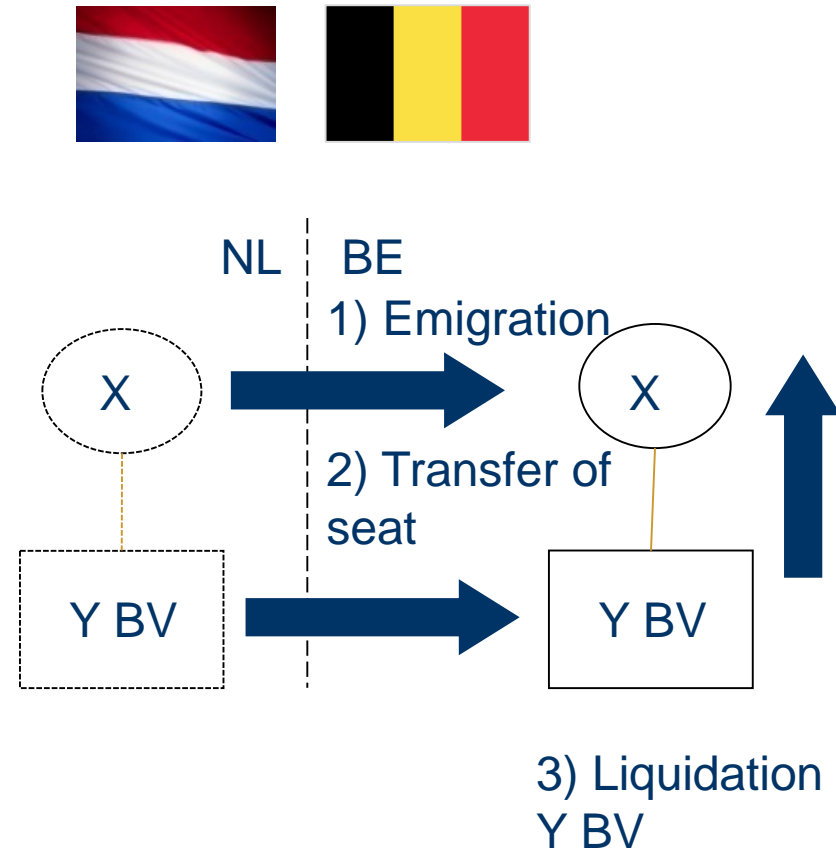
- Dutch compartmentalization doctrine as developed by the Dutch SC in the context of the Dutch participation exemption regime:
 - “Labelling” of accrued capital gains in “exempt” and “non-exempt” in case of leaving/entering the regime
 - Changes in the facts: no specific provision required; based on reasonable interpretation (e.g. *BNB 1986/305*)
 - Changes in the law: specific provision required (*BNB 2013/177*)

Application of the Dutch Compartmentalization Doctrine at DTC Level? Examples based on Dutch Case Law

- Example 1: (factual) relocation of the source of (passive) income to the other DTC country

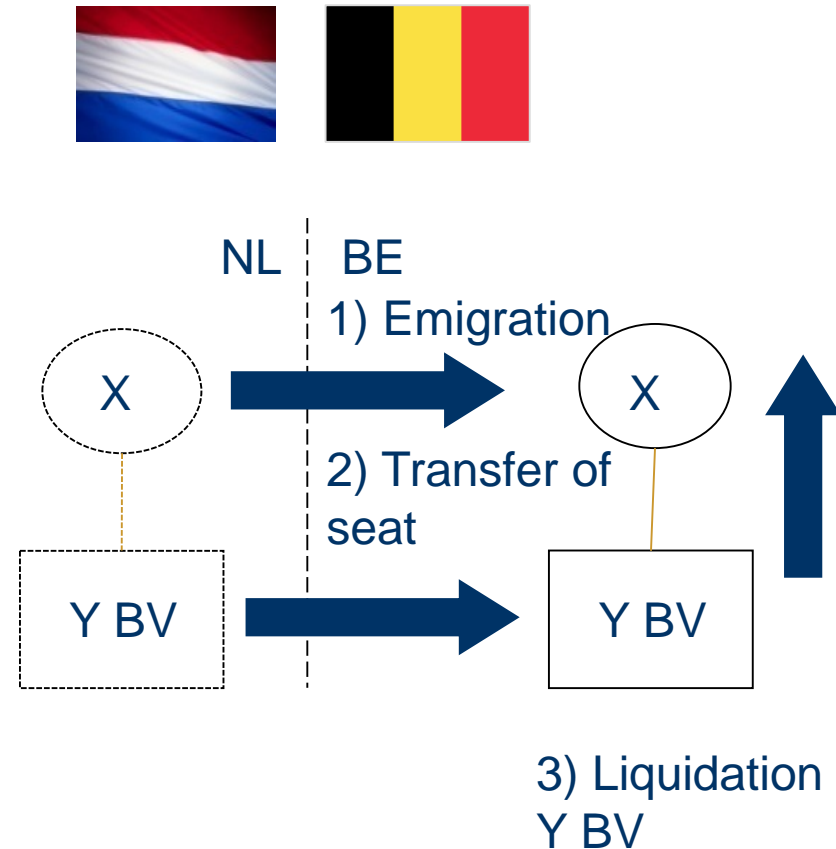
Example 1: Dutch SC 12 May 2006, BNB 2007/36 (1/3)

- X moves to Belgium on 15 October 1996
- POEM of Y BV (cash box) is transferred to Belgium on 30 October 1996
- Afterwards Y BV is liquidated and pays liquidation payments to X on 27 December 1996 and 31 August 1997
- Question: is the Netherlands still allowed to tax the liquidation payments under the NL/BE DTC?



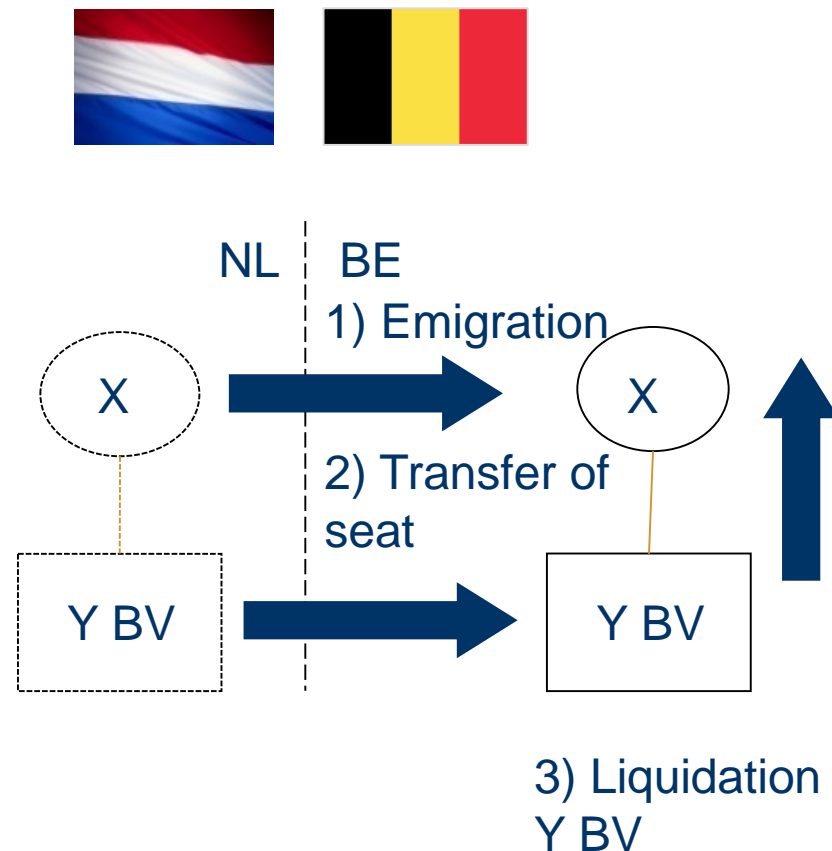
Example 1: Dutch SC 12 May 2006, BNB 2007/36 (2/3)

- High Court of Appeal Den Bosch 18 December 2002:
 - Based on a *reasonable tax treaty application*, the liquidation must be considered as being sourced in the Netherlands



Example 1: Dutch SC 12 May 2006, BNB 2007/36 (3/3)

- Dutch SC BNB 2007/36:
 - On 30 October 1996, Y BV became a tax treaty resident of Belgium
 - NL/BE DTC recognizes the consequences of a transfer of seat
 - Motive for transfer of seat are not relevant when determining tax treaty residence of Y BV
 - Hence, the Netherlands no longer allowed to tax
- Question: exit tax upon emigration shareholder tax treaty override as well? Dutch SC 20 February 2009, BNB 2009/261: no



Application of the Dutch Compartmentalization Doctrine at DTC Level? Examples based on Dutch Case Law

- Example 2: legal shift from residence-state-based to source-state-based-taxation as a result of the entry into force of a new DTC

Example 2: Dutch SC 12 July 2002, BNB 2002/402 (1/3)

- NL/UK DTC (until 6 April 1981): exclusive residence state taxation for capital gains on the disposal of Dutch located real estate
- NL/UK DTC (per 6 April 1981): exclusive source state taxation for capital gains on the disposal of Dutch located real estate

Example 2: Dutch SC 12 July 2002, BNB 2002/402 (2/3)



- Capital gain realized under new, but partly accrued under old DTC (figures are fictitious): is the Netherlands allowed under the new DTC to tax the full capital gain?

Example 2: Dutch SC 12 July 2002, BNB 2002/402 (3/3)

- Dutch Supreme Court BNB 2002/402:
 - Netherlands is only allowed to tax the capital gains accrued after the date of entry into force of the new DTC
 - Analogy with non-resident taxpayer that transfers asset from foreign head-office to NL branch → valuation at FMV at the moment of transfer for Dutch tax purposes(step-up)
- Prevailing view in literature:
“compartmentalization”/step-up based on Dutch domestic tax law (and therefore not based on DTC)

Application of the Dutch Compartmentalization Doctrine at DTC Level: Examples based on Dutch Case Law

- Example 3: (factual) relocation of the taxpayer's place of residence to (the other) DTC country

Example 3: Dutch SC 6 December 2013, BNB 2014/38 (1/1)

- Immigration of independent researcher from UK(or BE) to NL receiving pre-immigration income from research previously carried out in the UK
- Article 14 DTC NL/UK: exclusive residence state taxation, unless profits attributable to fixed base in other Contracting State
 - Dutch Supreme Court: taxpayer had carried out its research activities through a fixed base located in the UK for purposes of the NL/UK DTC
 - The link with the UK territory had the result that the right to tax the pre-immigration income was allocated to the UK
 - NL must therefore provide relief for double taxation

Evaluation & conclusion

- Typically, depending on the wording of the allocation provision in question...
 - Either the moment of actual payment (e.g. dividends); or
 - The moment on which the income has accrued (e.g. income from personal services)
- ... is the decisive factor when applying the allocation rule at stake
- Case law examples 1 & 3 are in line with this and case law example 2 is not in conflict with this



Temporal Aspects of Passive Income

Luxembourg, 26 January 2017,
Time & Tax" Conference
Prof.dr. D.S. Smit

Time and Double Tax Relief

Joanna Wheeler, IBFD, University of Amsterdam

- ▶ **Measurement over time**
- ▶ **Timing of a tax liability**
 - ▶ Change in the applicable law
 - ▶ Change in the facts

- ▶ **DTR is primarily domestic law**
- ▶ **Timing of tax liability is not a treaty issue**
 - ▶ C1(22.1)
 - ▶ C15(2.2 and 12.3)
 - ▶ BEPS 6 Final Report, para. 66
- ▶ **Treaty obligations re DTR**
- ▶ **DTR - The devil is in the detail**

- ▶ **Income recognition**
 - ▶ Zero-coupon bonds
 - ▶ Instalment sales

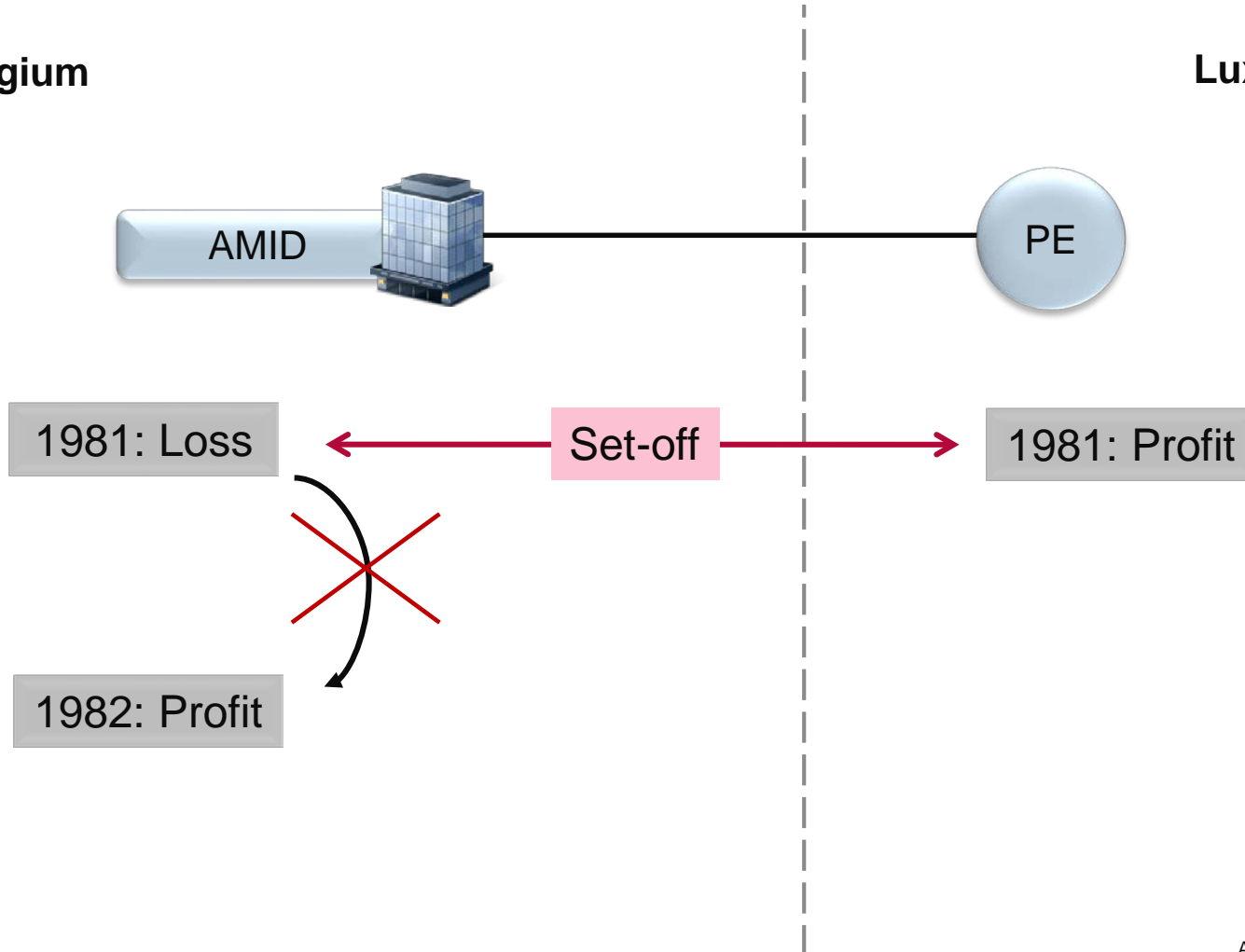
- ▶ **Deductions**
 - ▶ Depreciation and amortization

- ▶ **DTR involves two states - mismatches!**

European Court of Justice, Case C-141/99

Belgium

Luxembourg



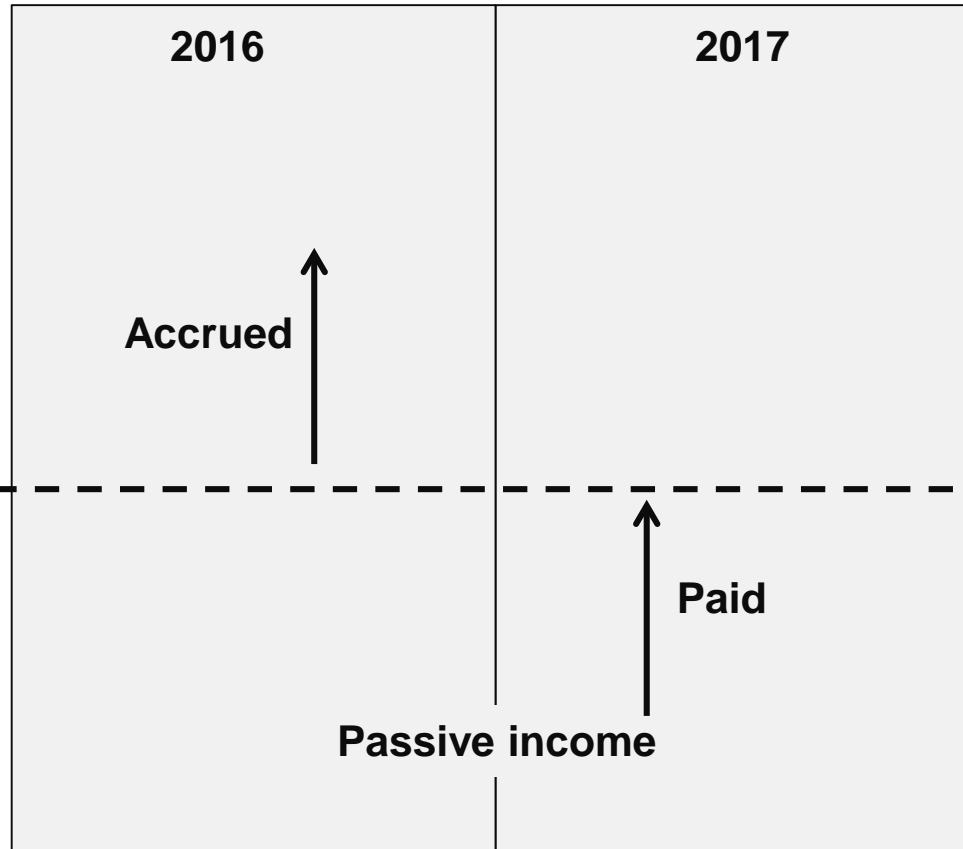
► **Losses**

- Computation of DTR over time

► **Excess credits**

- Carry-forward or carry-back of credits
- Carry-forward or carry-back of credit space
- Ordering of credits/credit space carried over

State R



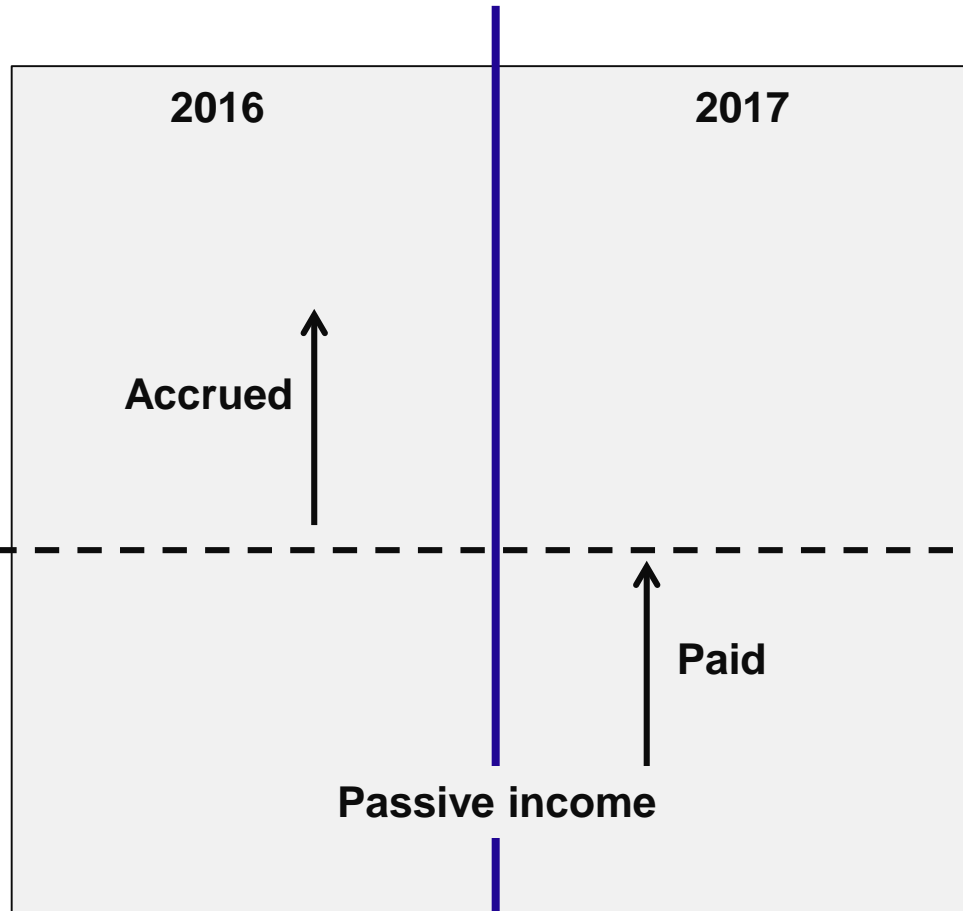
State S

- ▶ **OECD Partnership Report**
 - ▶ C23(69.3)
 - ▶ cited in UN Commentary

- ▶ **OECD Stock Options Report**
 - ▶ C15(2.2 and 12.3)
 - ▶ C23(32.8)
 - ▶ cited in UN Commentary

Timing of Tax Liability

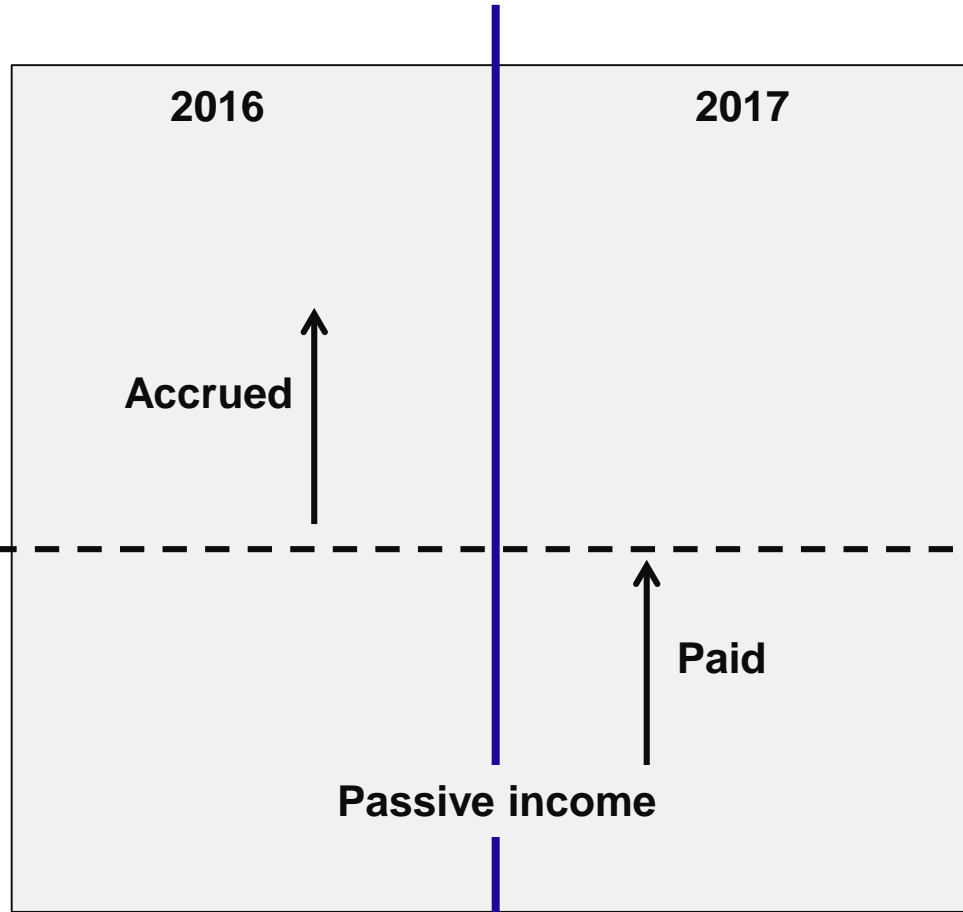
State R



State S

Change in facts

State R

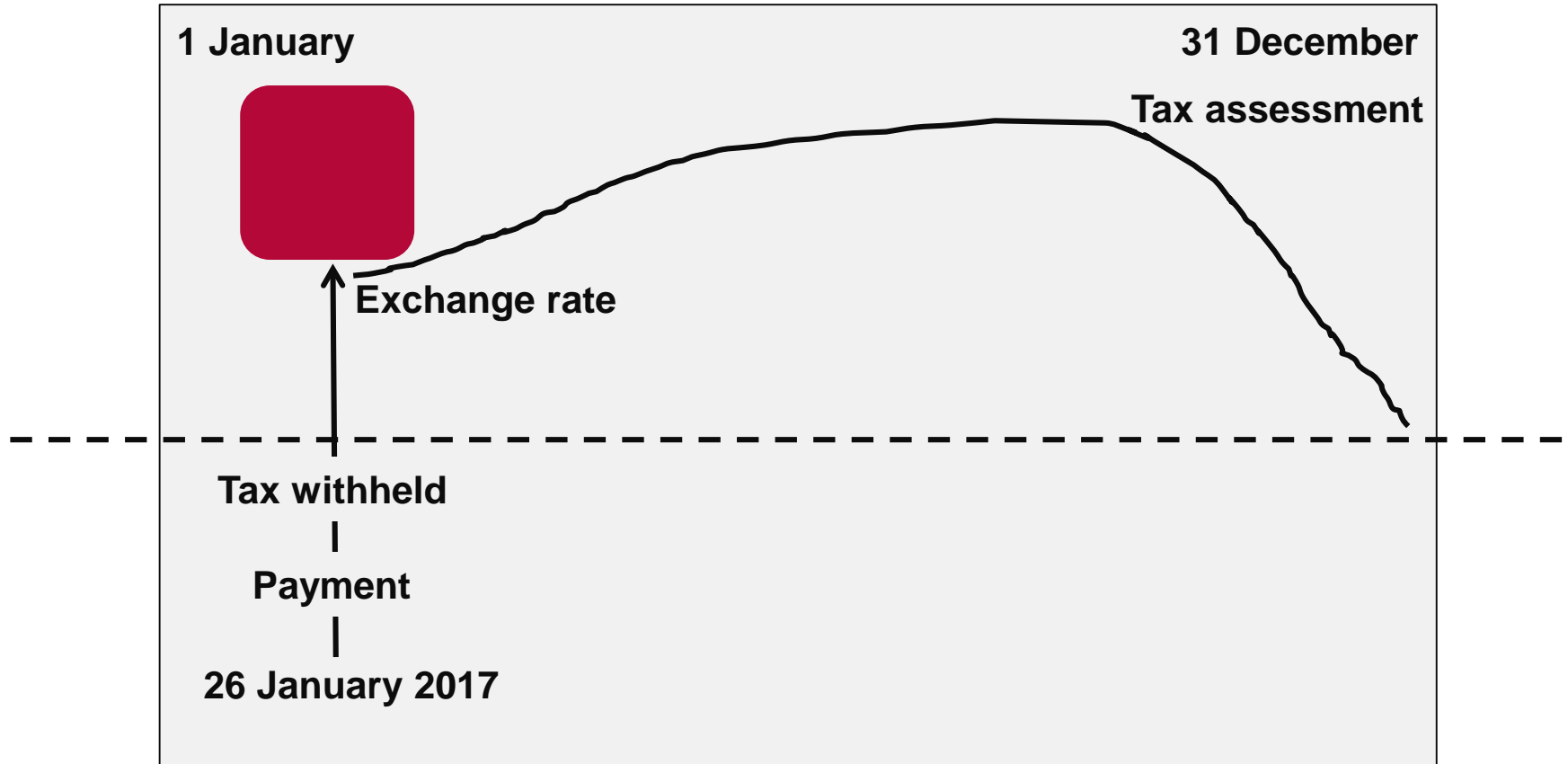


State S

Timing of tax liability

Timing of Tax Liability

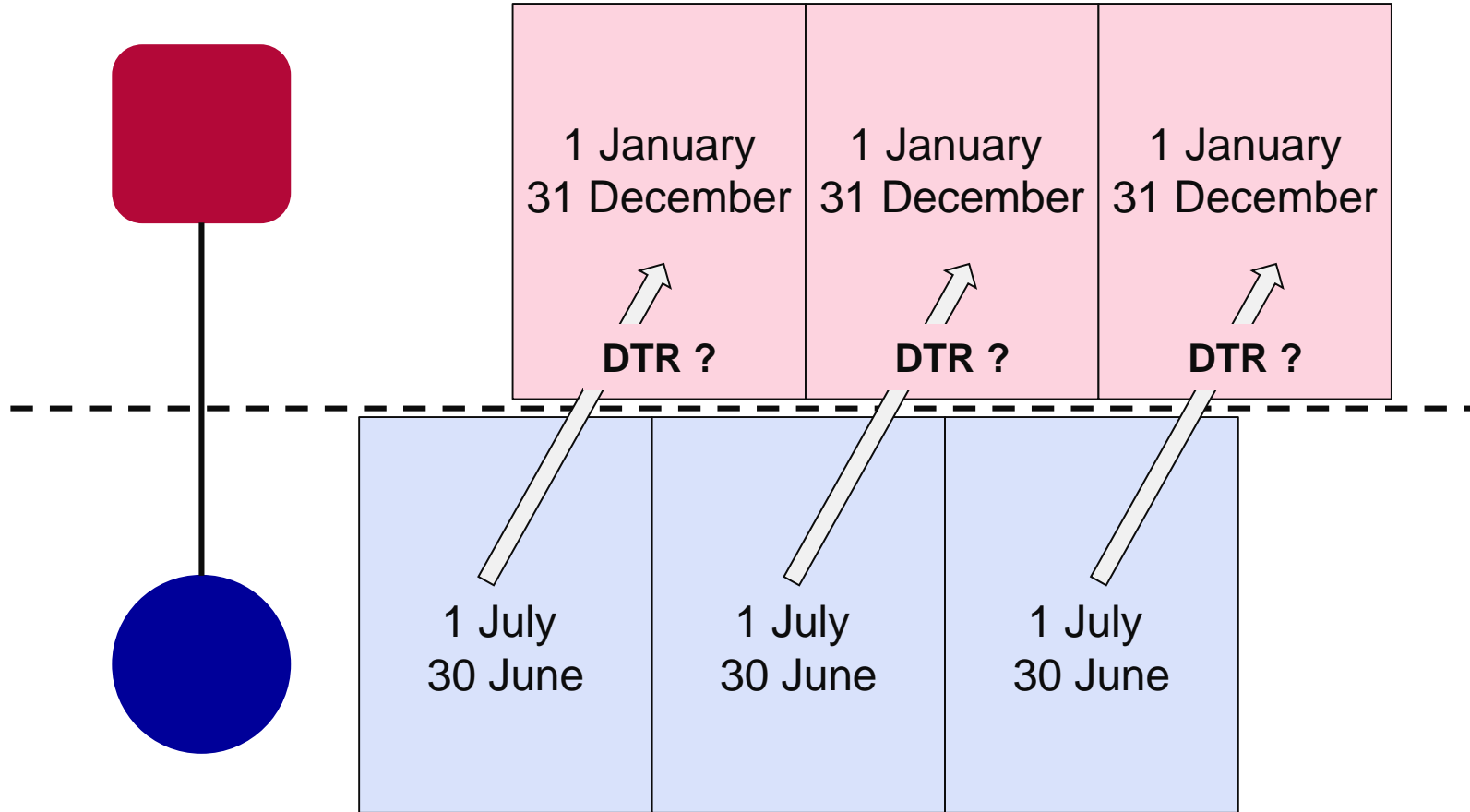
State R



State S

Timing of Tax Liability - Business Profit

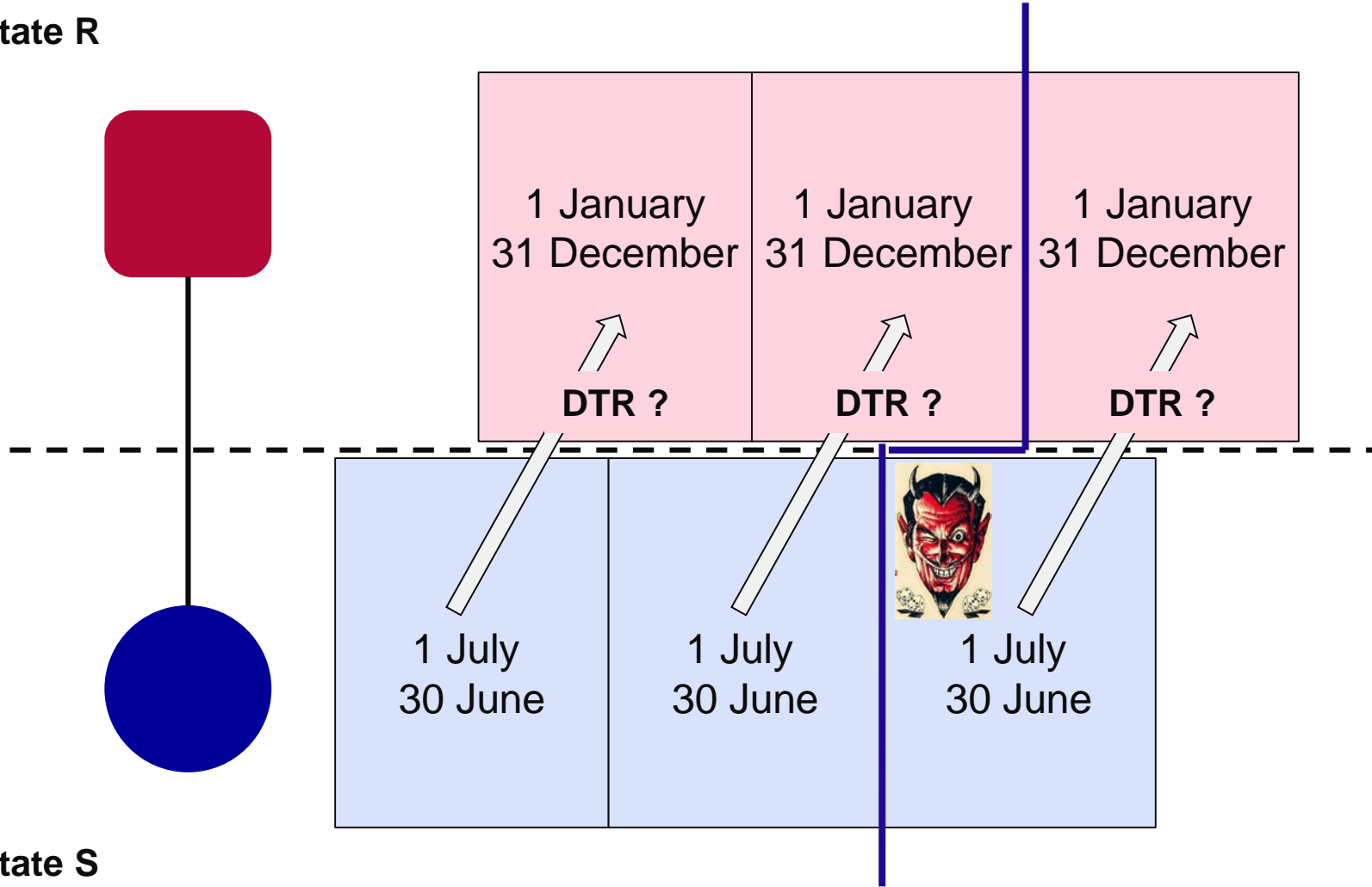
State R



State S

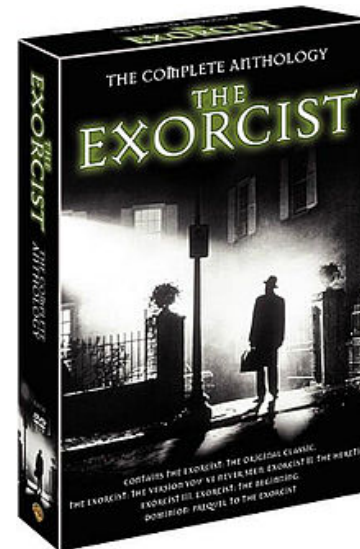
Timing of Tax Liability - Business Profit

State R



State S

Treaty takes effect



Time and Tax

Entry into Force and Termination of Tax Treaties

General questions

- Entry into force and termination of tax treaties
 - When does a tax treaty apply?
 - When is the tax treaty in effect?
- Relevant provisions:
 - Article 30 OECD MC – Entry into force
 - Article 31 OECD MC - Termination

Possible scenarios

- Entry into force of a new DTC
 - No prior existing DTC
 - Prior DTC is replaced
- Termination of a DTC
 - No prior existing DTC
 - New DTC enters into force
- Distributive TT rules (Art. 7 to Art. 22 OECD MC)
- Procedural TT rules (Art. 25 to Art. 27 OECD MC)

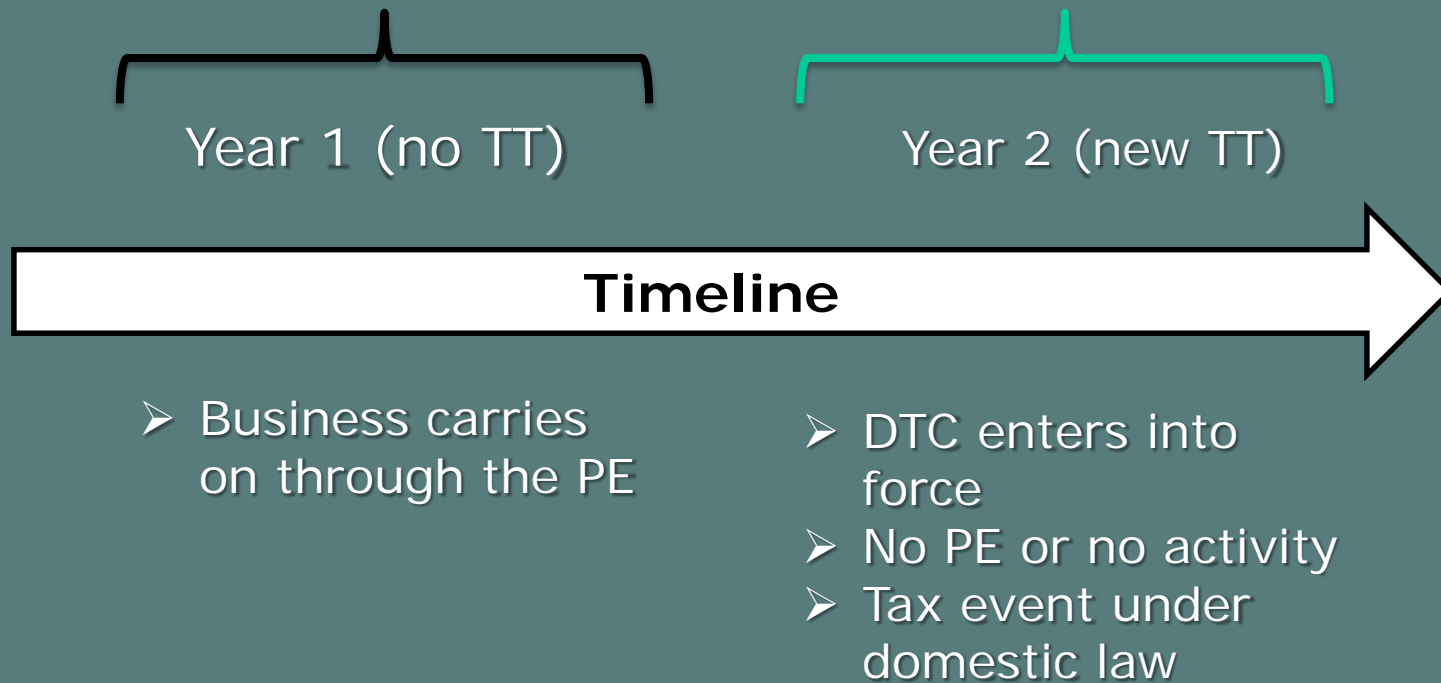
Italy – Luxembourg (1981)

Art. 30 Entry into force

1. This Convention shall be ratified and the instruments of ratification shall be exchanged at Rome as soon as possible.
2. This Convention shall enter into force upon the exchange of instruments of ratification and its provisions shall have effect:
 - a) in respect of taxes withheld at source, on income paid or payable on or after 1 January 1978;
 - b) in respect of other taxes, to fiscal periods ending on or after 1 January 1978.

Case 1:

New DTC/No prior DTC



Focus on business profits

- OECD MC, Art. 7 (Business profits):
 - “[...] If the enterprise carries on a business, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment”
- Canada – Luxembourg (1999), Art. 7 reads:
 - “If the enterprise carries on or **has carried on business** as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment”

Case 1:

New DTC/No prior DTC

- Entry into force
 - When is Art. 7 in effect? → reference to the tax period
 - Year 2 would be covered
- But the facts relevant for the application of Art. 7 are not occurring in same tax period (i.e. Year 2) in which the DTC enters into force

Case 1:

New DTC/No prior DTC

- Source State exemption should be denied
 - Would be against the very same object and purpose of the DTC
- Art. 28 VCLT calls for immediate temporal effect, but non-retroactivity is the rule

Case 1:

New DTC/No prior DTC

- Swiss case on exchange of information
- 2002 decision of the Swiss Federal Court of appeal (Case BGE 2A.551/2001):
Information requested by the IRS in respect of bank accounts in the name of individuals X and F for taxation years 1990 to 1997.
 - The 1996 tax treaty entered into force in 1997 and applied to taxes for the periods after 1 January 1998
 - Court concluded in favor of applicability of Art. 26 of the 1996 treaty

Case 1:

New DTC/No prior DTC

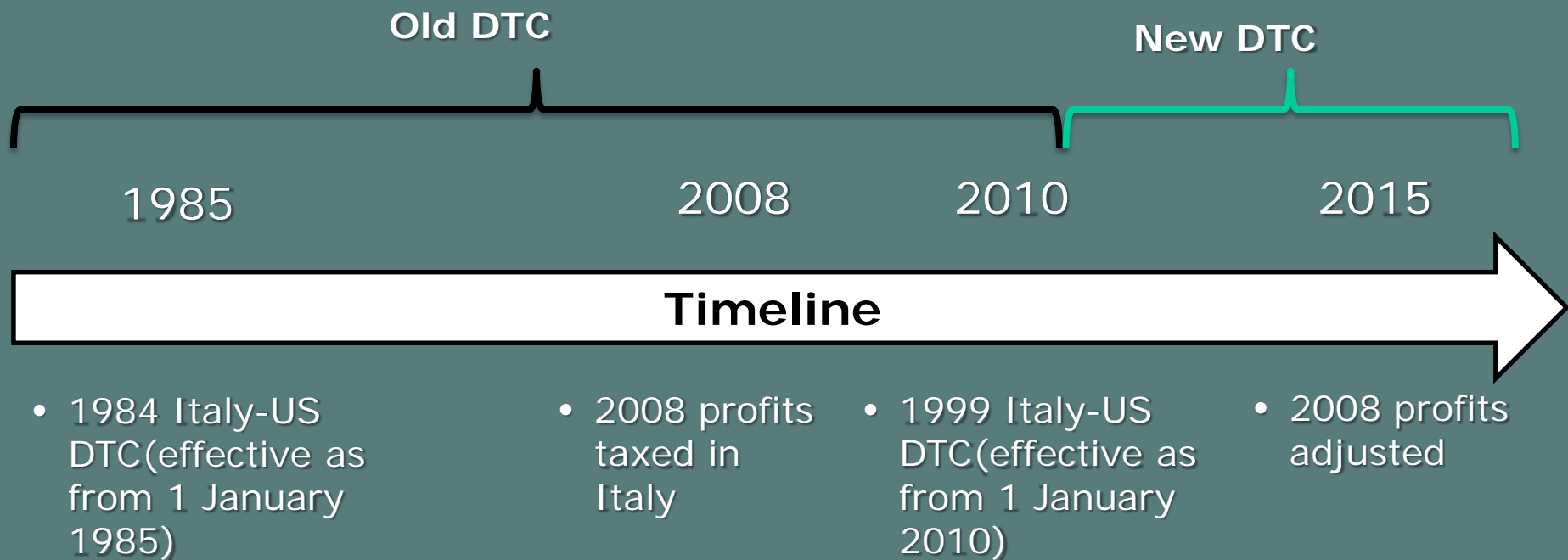
- Decision of the Court:
 - Taxes for the years 1990-1997: out of the scope of the treaty
 - Entry into force article does not apply to procedural provisions
 - the exchange of information – being a procedural provision – applied both immediately and retroactively after entry into force

Case 2:

prior DTC/new DTC

- 2008 Italian profits of an Italian subsidiary of US parent adjusted in 2015
- Subsequent treaties:
 - (1984) Italy-US Treaty (effective as from 1 January 1985) → Old DTC
 - (1999) Italy-US treaty (effective as from 1 January 2010) → New DTC
- Opening of a MAP in 2015, which treaty applies?

Case 2: prior DTC/new DTC



Case 2: prior DTC/new DTC

- Art. 28(4) new DTC:

"The provisions of the prior Convention shall cease to have effect when corresponding provisions of this Convention take effect in accordance with paragraphs 2 and 3 [*i.e., 1 January 2010*] , and the prior Convention shall terminate on the last date on which it has effect in accordance with the foregoing provisions of this paragraph."

US Technical Explanation (1999 IT-US Treaty)

*"A case may be raised by a taxpayer under a treaty with respect to a year for which a treaty was in force after the treaty has been terminated. [...] A case also may be brought to a competent authority under a treaty that is in force, but with respect to a year prior to the entry into force of the treaty. The scope of the competent authorities to address such a case is not constrained by the fact that the treaty was not in force when the transactions at issue occurred, and the competent authorities have available to them the full range of remedies afforded under this Article. **Even though the prior Convention was in effect during the years in which the transaction at issue occurred, the mutual agreement procedures of the Convention would apply.**"*

Case 2:

prior DTC tax treaty

- Art. 28(4): new DTC should apply (unclear whether it is relevant for MAP article)
- US TE: MAP under new DTC should apply
- Different treaties apply at the same time
 - Art. 7 Italy - US (1984)
 - Art. 25 Italy – US (1999)
- Procedural rules: “Tempus regit actum” principle

Thanks you

- Mario Tenore
Maisto e Associati
M.Tenore@maisto.it



Timing disadvantages and tax treaty non-discrimination

Niels Bammens
26 January 2017

Introduction

- Scope of the presentation
- Definition of timing disadvantages
 - Late benefits ⇔ early burdens
- Applicability of article 24
- Conclusions

Early burdens: examples

- Taxation at an earlier time
 - Taxation at source (taxpayer) ⇔ assessment (object of comparison)
 - E.g. Swiss source tax on employment income of foreign nationals with Swiss tax residence but no long-term residence permit (Art. 83 DGB; Art. 32 StHG)
 - Compatible with article 24(1)?
 - Verwaltungsgericht Zürich 3/3/1992; Verwaltungsgericht Thurgau 3/9/2008
 - Comm. OECD para. 15: “*when a tax is imposed on nationals and foreigners in the same circumstances, it must be in the same form as regards [...] the method of assessment*”
 - Clearly other taxation, but is this also less favourable taxation?

Early burdens: examples

- Taxation at an earlier time
 - Prepayment ⇔ no prepayment
 - E.g. UK ACT regime: ACT functioned as a prepayment of MCT
 - No ACT if group income election, but group election only possible if parent and subsidiary were UK residents → discrimination under art. 24(5)?
 - Compare ECJ in *Metallgesellschaft* (C-397/98 and C-410/98, 8/3/2001): “[group income election] gives the subsidiary of a parent company resident in the UK a cash flow advantage inasmuch as it retains the sums which it would otherwise have had to pay by way of ACT until such time as MCT becomes payable”
 - ... and House of Lords in *Boake Allen* (23/05/2007): “Discrimination against the group as a whole is thus a restriction on the parent's freedom of establishment. If a group with a UK parent has a cash flow advantage which a group with a parent in another member state does not enjoy, that is a restriction on the latter's freedom of establishment. [...] A DTC, on the other hand, does not give a company or individual resident in one country a right of establishment in the other. [...] the equality it ensures is only that any enterprise it owns in the other country will not be subject to taxation which discriminates on the ground of its foreign control”

Early burdens: examples

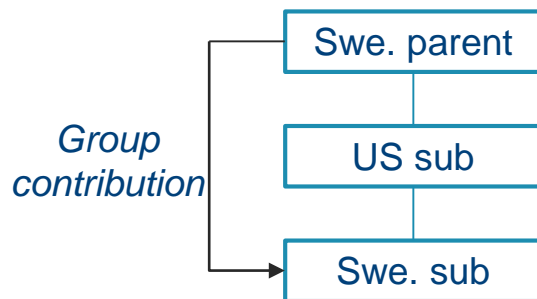
- Procedural timing differences (“connected requirements”)
 - Shorter filing or reporting deadlines
 - E.g. Spanish Supreme Court 25/3/2010 (no. 2598/2010)
 - Filing deadline for refund claims: 4 years for residents ⇔ 1 year for non-residents
 - Court: less favourable connected requirement → infringement of article 24(1) (!)

Late benefits: examples

- Deductibility timing difference
 - Payments to residents deductible on accrual basis ⇔ payments to non-residents deductible on cash basis → compatible with art. 24(4)?
 - E.g. Argentina, art. 121 decreto 1344/98
 - Literal interpretation of “paid” in art. 24(4)?
 - E.g. *Square D* (US Court of Appeals for the Seventh Circuit 13/2/2006)
 - IRC § 267(a)(2): deduction for payor is matched to taxability for related recipient → US resident accrual taxpayer paying interest to recipient cash taxpayer: deductible upon payment
 - US accrual taxpayer paid interest to its French parent that did not conduct a US trade or business → deductibility on cash basis
 - Court: no discrimination (but decided on the basis of foreign ownership provision, in the absence of a provision analogous to art. 24(4) OECD)

Late benefits: examples

- Timing of loss set-off
 - E.g. group contribution and loss relief regimes
 - Art. 24(5) may be applicable if a foreign-owned enterprise suffers a disadvantage
 - Cash flow disadvantage for the group as a whole?
 - Compare ECJ in *Marks & Spencer* (C-446/03): “Group relief such as that at issue in the main proceedings constitutes a tax advantage for the companies concerned. By speeding up the relief of the losses of the loss-making companies by allowing them to be set off immediately against the profits of other group companies, such relief confers a cash advantage on the group” ⇔ Comm. OECD para. 77: only foreign-owned enterprise is protected + not applicable to rules on group treatment (e.g. group consolidation or transfer of losses)
 - Swedish Supreme Administrative Court RÅ 1993, ref 91 I:



- Group contribution: deductible for transferor, taxable for transferee
- No entitlement to group contribution because non-resident intermediary company
- Is this less favourable taxation of the foreign-owned enterprise? Other taxation?
- Court: other taxation, because the subsidiary is unable to receive the contribution

Late benefits: examples

- Timing of loss set-off
 - E.g. group contribution and loss relief regimes
 - Similar issue in UK FTT, *Felixstowe* (19/12/2011): UK resident foreign-owned company sought to surrender its losses to related UK resident. Group relief denied due to foreign ownership → discrimination?
 - Surrendering company is not liable to a greater amount of tax due to refusal, and could even pay more tax if it subsequently made profits
 - FTT: *“construing Article [24(5)] so as to relate only to discrimination that results in a liability to tax or a burden in respect of tax would be to take too narrow an approach to the interpretation of that article. [...] Although the inability to surrender losses can have no impact on the immediate tax liability of the surrendering company, and the fact that it carries forward the losses and may therefore suffer lower taxation in future accounting periods than if the losses had been surrendered, this inability, both to surrender and to obtain payment from the claimant companies for the losses, is a difference in treatment that in our view falls within Article [24(5)].”*
 - Compare ECJ in *Felixstowe* (C-80/12): *“Relief such as that at issue in the main proceedings constitutes a tax advantage for the companies concerned. By speeding up the relief of the losses of loss-making companies by allowing them to be set off immediately against profits of other group companies, such relief confers a cash-flow advantage on the group”*

Applicability of article 24

- Difference between paras. (1), (2), (4) and (5) ⇔ para. (3)
 - Para. (1), (2) and (5): *“any taxation or any requirement connected therewith, which is other or more burdensome”* and para. (4): *“deductible under the same conditions”*
 - All types of timing disadvantages are covered
 - But Comm. OECD, paras. 75 and 80: “additional information requirements” are not prohibited under art. 24(4) and (5)
 - ↔ Para. (3): *“taxation shall not be less favourably levied”*
 - Only taxation (“connected requirements” are not covered) and only less favourable treatment (“other” treatment is not covered)
 - Comm. OECD para. 15: taxation = basis of charge, method of assessment and tax rate ⇔ connected requirements = formalities connected with the taxation (returns, payment, prescribed times, etc.)
 - E.g. *Commerzbank* (High Court, Queen’s Bench Division 12/04/1991): repayment supplement is not “taxation”
 - Comm. OECD, para. 34: *“it is the result alone which counts”* → is art. 24(3) only concerned with the direct burden of tax, i.e. what must be paid in terms of money?

Applicability of article 24

- Preliminary conclusions
- Remedies
 - Future differences in treatment
 - Taxpayer is entitled to the application of the rules applicable to object of comparison
 - Past differences in treatment
 - Compensation for the loss of the use of funds?
 - Compare to ECJ in *Metallgesellschaft*, para. 87: *“In the main proceedings, however, the claim for payment of interest covering the cost of loss of the use of the sums paid by way of ACT is not ancillary, but is the very objective sought by the plaintiffs' actions. In such circumstances, where the breach of Community law arises, not from the payment of the tax itself but from its being levied prematurely, the award of interest represents the 'reimbursement' of that which was improperly paid and would appear to be essential in restoring the equal treatment”*
 - Similar argument under international law?

VALUE OF PRECEDENTS IN EU TAX LAW

Ieva FREIJA – PECCATI

Référendaire – European Court of
Justice

Time and Tax – Luxembourg

26.01.2017

Substantive impact of the ECJ case- law on EU direct tax

- ▣ Limited legislative action at the Union level due, inter alia, to the unanimity requirement at the Council
- ▣ Development of the EU direct tax law through negative integration based on interpretation of the fundamental freedoms and State aid rules
- ▣ Particularities of the tax cases
- ▣ Outcome vs Guidance vs Referral cases or mixture thereof

ECJs' APPROACH TO CASE-LAW

- ▣ Previous decisions are formally not binding
- ▣ Great deference to the case-law as means of assuring uniformity, coherence and legal certainty within the European legal order
- ▣ An accepted framework of interpretation – departing needs to be motivated

PURPOSE OF THE USE OF PRECEDENTS BY ECJ

- ▣ Legitimation
 - Internal
 - External
- ▣ Legal certainty, predictability, coherence
- ▣ Efficiency gains

USE OF PRECEDENTS

- ▣ String citations, substantive citations
- ▣ Every stage of reasoning – determining the legal norm, interpreting, qualification, proportionality analysis
- ▣ Building a case-law line
- ▣ Departing from previous case-law

Case-law line

- ▣ Applying the initial precedent in a coherent way
- ▣ Completing and fine-tuning the initial precedent without modifying it's scope
- ▣ Substantial vs apparent consistency
- ▣ Risks: inertia, reiteration of non-convincing solutions

Example: fiscal coherence as justification of a restriction

- ▣ Recognition : 1992 (C-204/90 Bachmann)
- ▣ Acknowledgment and fine-tuning without acceptance *in casu* (e.g. C-319/02 Manninen; C-418/07 Papillon) – until 2008
- ▣ Acceptance: C-157/07 Krankenhaus; C-250/08 Commission/Belgium; C-253/09 Commission/Hungary; C-322/11 K; C-123/15 Feilen

Fiscal coherence: recognition and strict definition (1)

- ▣ Bachmann: connection between the deductibility of contributions and the liability to tax of sums payable by the insurers under pension and life assurance contracts.
- ▣ Condition explicitly stated in Bachmann, reiterated further (e.g. C-484/93 Svensson & Gustavsson; C-264/96 ICI):
 - Direct link between an advantage and a tax that needed to be preserved for the coherence of the tax system

Fiscal coherence: recognition and strict definition (2)

- ▣ Further conditions: same tax payer, same tax
- ▣ Baars (C-251/98, 13.04.2000):
 - « ...no ...link (as in Bachmann) in the present case, which concerns two separate taxes levied on different taxpayers. »
 - Negative coherence: Baars does not fall under Bachmann because of absence of the link, in the circumstances of separate tax payers and separate taxes
- ▣ Verkooijen – (C-35/98, 6.6.2000) recognising same tax payer, same tax as already present in Bachmann

Verkooijen, p. 40

- ▣ « In Bachmann a direct link existed, in the case of one and the same taxpayer, between the grant of a tax advantage and the offsetting of that advantage by a fiscal levy, both of which related to the same tax. In those cases, there was a link »

Fine-tuning coherence (1)

- ▣ Manninen C-319/02, 7.9.2004)
 - cohesion argument must be appreciated in the light of the objective pursued by the tax legislation in question
 - doesn't exclude the direct link between different taxpayers and different tax (refers to link between tax advantage granted to beneficiary of dividends and corporate tax paid by company)

Fine-tuning coherence (2)

- ▣ C-418/07 Papillon (27.11.2008)
 - Recognition of a direct link under the tax integration regime available to groups between the tax advantages and the neutralisation of intra-group transactions
- ▣ C-35/11 Test Claimants in the FII Group Litigation (13.11.2012)
 - Recognition of a direct link between on one side -tax credit in the case of foreign-sourced dividends and the tax exemption for nationally-sourced dividends, and, on the other- the tax to which the distributed profits have already been subject.

Acceptance

- ▣ C-157/07 Krankenhaus (23.10.2008):
reintegration of losses present a direct,
personal and material link to their having earlier
been taken into account.
- ▣ C-250/08 Commission/Belgium (...): offsetting
of registration duties paid at the time of the
acquisition of residential property in the
Flemish Region against the registration duties
payable on the acquisition of a new principal
residence in that Region (same tax, same taxpayer)

Acceptance (2)

- ▣ C-322/11 K (7.11.2013): acceptance of direct link, in the case of the same taxpayer and the same tax, between, on the one hand, the tax advantage granted, namely the taking into account of losses generated by a capital investment, and, on the other, the taxation of returns on that investment
- ▣ C-123/15 Feilen (30.6.2016): reduction of inheritance tax only to persons receiving assets by way of an inheritance which has given rise to the imposition of such taxes in Germany – same tax, direct link, but same payer not possible in heritance cases

Departing from the case law

- ▣ Overruling
- ▣ Distancing, soft over-ruling or avoiding
- ▣ Distinguishing

Distinguishing

- ▣ Disapplication – the requirements of the previous precedent are not met
- ▣ Manipulation - modifying the precedent to some extent so that it does not apply to the present case, by increasing its the specificity

Example: C-282/07 Truck Center (22.11.2008)

- ▣ Charging of withholding tax on interest paid to non-resident companies when such withholding tax was not charged on interest paid to resident companies
- ▣ Difference in treatment, consisting in the application of different taxation arrangements to companies established in Belgium and to those established in another Member State, relates to situations which are not objectively comparable.

C-282/07 Truck Center

- ▣ Differences found:
 - position of the Belgian State (source as opposed to resident of the recipient company)
 - two distinct charges which rest on separate legal bases (withholding tax & internal corporation tax)
 - situations in which those companies find themselves with regard to recovery of the tax
- ▣ In addition:
 - difference in treatment does not necessarily procure an advantage for resident recipient companies

Commission/Spain (C-478/08)

- ▣ Different treatment of dividends paid to resident and non-resident companies owning between 5% and 20% of the shareholding, exempting from the withholding tax only the dividends paid to the resident companies
- ▣ Truck Center is irrelevant as it concerned different taxation arrangements (as opposed to taxation and exoneration here)

Commission/Spain C-269/09 (12.07.2012)

- ▣ obligation for the taxpayer, transferring its residence outside Spanish territory, to pay tax before taxpayers who continue to reside in Spain are required to do so
- ▣ Truck Center is irrelevant as the present case does not concern a straightforward technique for recovery

C-498/10 X (18.10.2012)

- ▣ obligation on the recipient of a service to withhold at source the wages tax on the remuneration due to a service provider established in another Member State
- ▣ Court stresses that Truck Center is about perception techniques and in addition no adverse treatment for non-residents
- ▣ However present case is about service recipient, with distinct interests and separate rights

Joint cases C-338/11 – 347/11 Santander Asset management e.a. (10.05.2012)

- ▣ Different treatment of dividends paid to non resident undertakings for collective investments in transferable securities (UCITS), subject to withholding tax, and dividends paid to resident UCITS, not subject to such tax
- ▣ Truck Center: both non residents and residents were taxed and simply provided for different procedures for charging tax
- ▣ Here exemption vs taxing

Joint cases C-53/13 and C-90/13 Strojírny Prostějov, a.s. (19.06.2014)

- ▣ obligation to withhold an advance payment on the income tax of workers supplied by temporary employment agencies not established in the Czech Republic and to pay that advance payment to the Czech State
- ▣ By analogy to X, the present case concerns service recipient

Joined cases C-10/14, C-14/14 and C-17/14,
Miljoen e.a. (17.09.2015)

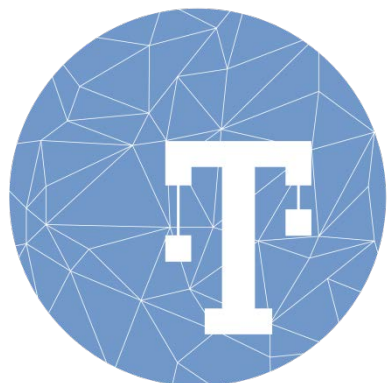
- ▣ legislation imposing a withholding tax on dividends paid by a resident company, both to resident taxpayers and non-resident taxpayers; making provision for a mechanism for deducting or reimbursing the tax withheld solely for resident taxpayers, while for non-resident taxpayers, both natural persons and companies, the tax withheld is a final tax.

Distinguishing

- ▣ In case at hand the restriction does not arise from a difference between the collection arrangements applied to resident taxpayers and those applied to non-resident taxpayers, but stems from an advantage granted to resident taxpayers which does not extend to non-resident taxpayers
- ▣ As opposed to Truck Center, the withholding tax is levied on all taxpayers

Temporal Aspects of ECJ Judgments

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Summary

- Introduction
- TFEU recognition vs ECJ expansion
- Consequences for tax matters
- The ECJ doctrine
- Considerations on the ECJ doctrine



Introduction

- Careful weight of challenges and risks
- Equilibrium between legality and legal certainty
 - Legality for the future/Legal certainty for the past
- Never compromise future application of law (because of sensible repercussions for the past)



Introduction

- Effects in tax matters: associated with
 - the right to obtain refund for taxes paid incompatible with EU Law (or compensation for State liability)
 - recovery of tax benefits constituting unlawful State aid
- Rights directly linked with the proper defense of EU Law in tax matters

TFEU recognition vs ECJ expansion



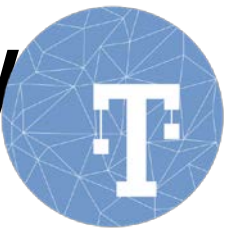
- TFEU: limitation of temporal effects only recognized in action of annulment
 - art 264 TFEU: If the action is well founded, the Court of Justice is to declare the act concerned to be void and may, **if it considers necessary**, state which of the effects of the act which it has declared void are to be considered as definitive
 - General rule: nullity with *ex tunc* effects
 - Exception: possibility to maintain the effects of void acts
- TFEU: no specific recognition of temporal effects as regards other actions

ECJ expansion (elaboration)



- On grounds of analogy (Defrenne) -general scope, uniform application-, material identity (Roquette), context and coherence
- Although same procedural mechanism (preliminary ruling), differences regarding object, effects and scope
- However, broader acceptance of the exception in EU law validity cases (Borealis, C-191/14)
- Functions assimilated to constitutional control on EU law validity of domestic rules
- Criticism
 - Invasion of functions on applicability of EU Law
 - Evaluation of the applicability of the EU Law rule (and indirectly the validity/compatibility of the domestic rule)
 - Establishes solution of the compatibility judgment to the domestic Court

Limitation of temporal effects in EU Law annulment/validity decisions



- Validity/annulment of EU (tax) legislation
 - Less restrictive application of temporal limitation doctrine
 - Burden of proof of financial repercussions loosened
 - Presumption of validity of EU secondary legislation
 - Broader prospectivity considerations

EJC elaboration on interpretative preliminary rulings



- General Rule
 - Formulation and consequences
 - Fundamental
 - Implication
- Departures: exception
 - Requirements/elements
 - Consequences
 - Time setting
 - (Tax) cases
- Exception to the exception



General rule

- “the interpretation which, in the exercise of the jurisdiction conferred on it by Article 234 EC, the Court gives to a rule of Community law clarifies and defines the meaning and scope of that rule as it must be or ought to have been understood and applied from the time of its entry into force”
 - it must be or
 - it **ought to have been** understood
 - time of its **entry into force**



Fundamental

- Declarative nature of the ECJ decision
 - Limited to clarifying and defining the meaning and scope of the rule
 - General binding effect (but not erga omnes)
 - Effect *ex tunc*
- Restitution of the law has it should be or have been (correlation with right to obtain refund of incompatible paid taxes)
 - Only limited in certain situations: limitation of effects and justification of preclusive terms are two different limitations based on different criteria but based on the same principle (legal certainty)

Consequence (for domestic courts)



- The rule as thus interpreted may, and must, be applied by the courts even to legal relationships which arose and were established before the judgment ruling on the request for interpretation, provided that in other respects the conditions for bringing a dispute relating to the application of that rule before the competent courts are satisfied
 - retroactive (judicial) application of proper interpretation
 - provided (domestic) conditions for bringing disputes are satisfied
- Conditions for determining a legal remedy
 - If there is an EU law specific procedure, it must be applied
 - If there is not an EU Law procedure, the principle of autonomous procedure should provide one subject to the effectiveness and equivalence principles
- Unless exceptional temporal limitation applies:



Parallel condition

- Provided that in other respects the conditions for bringing a dispute relating to the application of that rule before the competent courts are satisfied
- Limitation of effects doctrine is an exception to the effectiveness/equivalence requirements for revising/refunding an incompatible tax
- Limitation of temporal effects must not be confused with acceptance of preclusive terms for domestic remedies



Exception

- Temporal effects can be **(exceptionally) limited** if two conditions are met:
 - **Bona fide behavior** (protection of good faith relationships by MS and individuals, because of legal certainty)
 - Specifically: Objective and significant legal uncertainty
 - **Risk of serious repercussions**
 - Specifically: serious economic/financial repercussions



Exception configuration

- Rule can only be excluded in EXCEPTIONAL cases: restrictive application
- Only by the ECJ, not by domestic courts
- On a case by case basis
 - Careful consideration of the practical effects
- In the 'first' decision on the matter
- Not inherent function: only under request-proved by a MS/interested party (petition)
 - Burden of proof: sufficiently substantiated: not purely hypothetical
- Only if two conditions are met together



Effects of the limitation

- Effects of the limitation
 - Interpretation valid with *ex nunc* effect
 - Unless the exception to the exception applies
 - Fixation of time of the effects of the interpretation: normally the date of the decision
- ECJ has not followed
 - Strict prospectively: setting a future date from which the judgment may be relied on
 - Limitation ex post since the first interpretation case law (clarity of law) unless established in the same decision

Exceptional acceptance (examples)



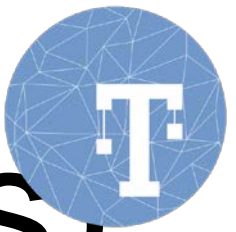
- Refund of taxes incompatible with EU Law
- Discrimination issues, mass and class action claims
- Conditions:
 - Main: of a constitutional/prudential character (recognition of the principle of legal certainty: presumption of validity of domestic legislation)
 - Secondary: of an opportunity character (allow the continuity of the law/system: prevent causing difficulties)



Examples (tax cases)

- **Salumi** 66/79 and 127-128/79 (agricultural duty): lack of authoritative interpretation + protection of legitimate expectation (difference of levy payment impossibility to recover) + restitutio in integrum which proves more harmful than the damage for which it is to compensate + resulting in aid if tax passed on to customers
- Denkavit Italy 61/79
- Legros, C-163/90. (Octroi de mer, dock dues, excise duty), equivocal/contradictory Commission behavior + specific/particular trends of tax
 - Surgelés, C-126/94: recognition of limitation of effects on first Decision
- Simitzi, C-485 and C-486/93 (ad valorem tax, import municipal tax)
 - Uncertainty until Legros C-163/90 + local budget constraints (no proof) + protection diligent taxpayer
- **EKW** and Wein (C-437/97) Beverage duty contrary to art 33 VAT Directive
 - Uncertainty (no previous ruling) + difficult proofs to deny reimbursement + local budget constraints (no global amount) + confusion of the local tax system
 - Against AG opinion

Examples of denial (tax cases)



- Similar cases already decided with no limitation of effects (same MS -Nicula-/other MS -Meilicke-)
- Similar but not equivalent tax measures accepted by the Commission (C-82/12 Besora)
- Clear infringement or incompatibility (Italmoda)



Bona fide action

- Individuals and national authorities led into adopting practices which do not comply with Community legislation by reason of objective significant uncertainty
- Uncertainty on implications of Community provisions
 - Lack of revelation of the legal meaning and implications
- Conduct of other MS or the Commission may have contributed
 - Not the ECJ conduct/case law?
 - Not a necessary element but certain indicia
- Good faith of 'those concerned' (both individuals and MS)
 - What if considerable number of claims?
- Doesn't imply protection of legitimate expectations

Objective and significant legal uncertainty



- Good faith relationships
- National rules to be validly in force
- Objective vs subjective uncertainty
 - Revealed by the ECJ
 - Predictability?
 - Does not exist if settled case law: may exist in ‘first case’ on the issue
- More restrictive than ‘acte clair doctrine’ or ‘sufficiently characterized violation’
- Commission inaction or opinion not understood as sanctioning favorably MS actions
 - Discretionality of Commission in infringement proceedings
 - Evidence of Commission opinions and specific to the case
 - ECJ only body to fix rights and duties of MS

What is the 'first' decision on the matter?



-
- Same questions of interpretation
 - High degree of similarity (Gravier/Blaziot cases)
 - of rulings/interpretative issues (relevance of the issue: basic
 - of taxes/tax regimes/tax incentives/tax schemes/tax consequences (need to interpret by analogy-comparison of tax systems and their effects) secondary element: precision of expansive effects of the interpretative rule (depends on which type of EU Law provision/principle has been interpreted)
 - Clarification of previous questions
 - Further interpretation (Defrenne, FII, Meilicke,... and effects on interpretation)
 - Different opinions between ECJ cases/ ECJ-court of first instance
 - Need for an 'authoritative answer': clarity of the EU Law meaning
 - AG Stix-Hackl in BPC p 159-164.

Risk of serious economic repercussions



- Large number of legal relationships entered in good faith
 - Bad argument AG: worse is treated better (greater/smaller instead)
- Financial consequences cannot in themselves justify limiting the temporal effect of such a ruling
- Ex tunc effects both for charges and/or benefits
- Burden of proof: ECJ should prevent impossible evidence requirement (simple expectations)
- Per country limitation?



Effects

- Date for recognition of effects
 - General rule: date of the ECJ decision in which limitation has been decided
 - Other alternatives (AG) not accepted
- Date for exercising rights associated with these 'new' effects
- Depending on whether there is acceptance for the exception to the exception:
 - limitation of future-present claims on past situations



Time of the limitation

- Only by the ECJ; not by the domestic Courts
- Only at the time of the judgment ruling upon the interpretation sought (Barra)
- Justification:
 - Uniform application of EU Law: equality among MS and individuals
- Distinction:
 - Time of the effects
 - Date of delivery of the decision (not before or after)
 - Time of the exception (claims accepted)

Exception to the exception



- Protection of the **special diligent citizen/taxpayer**
 - Limitation to the prospective effects (except for those diligent taxpayers that have appealed/made a claim)
 - Exception not of objective character
- What type of diligence?
 - Severe diligence/relaxed -careful- diligence
- Limited prospectivity of acceptance of (previous) claims
 - Variance of proposals for the determination of the date
 - DOUE publication of preliminary request; AG opinion release, ECJ decision



Criticism

- Declarative vs constitutive character of case law revelation
- Invasion of MS functions of applicability of EU Law
- Linking effects to the entry into force and not to the date of recognized direct effect
 - Transforms nature, content and effects of the rule
- Settled vs unsettled case law. Alternative criteria
 - Gradation of the incompatibility analysis/infringement.
 - Predictability of the outcome
 - Non-clarifying previous case law
- On request function/ case by case evolving nature: objectivity of legal changes
- Per country assessment: interpretation with general effect



Many thanks;

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Muchas gracias;

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Tax Deferral and EU Fundamental Freedoms

Tax and Time
Luxembourg
26 January 2017

Karoline Spies

- I. Tax Deferral and Fundamental Freedoms
- II. Cash-flow disadvantages in ECJ case law
 - I. Exit Tax
 - II. Foreign Losses
 - III. Withholding Taxes
- III. Conclusion

Why is the cash-flow disadvantage accepted by the ECJ?

- Deferred payment of tax is a benefit for taxpayers: cash-flow and interest advantages
- A cash-flow disadvantage constitutes a **restriction** on the fundamental freedoms which needs to be justified
 - a restriction on a fundamental freedom is prohibited by the Treaty, ***“even if it is of limited scope or minor importance”*** (de Lasteyrie, para. 43)
 - ***“A cash-flow disadvantage which arises from a cross-border situation can form a restriction on a fundamental freedom where such a disadvantage does not arise in a purely national situation”*** (Familienprivatstiftung Eisenstadt, para. 51, landmark case: Metallgesellschaft Höchst)

- **Justification:** Ensuring effective tax collection
- **Proportionality:** denial of deferral is disproportional ...
 - if tax authorities can easily recover the tax from the taxpayer itself
 - resident person (*Com/DK, Haribo*)
 - non-resident person with domestic permanent establishment or other „physical presence in the territory“ (*Strojirny Prostejov*)
 - if tax authorities can rely on other less restrictive means
 - Mutual Assistance Agreements in Tax Collection
 - lack of efficiency?
 - diverging evaluation of Tax Collection Directive by the Court: *Turpeinen/Scorpio vs NGI vs X*
 - Guarantees
 - restrictive in itself
 - diverging evaluation by the Court: *N vs NGI vs DMC*

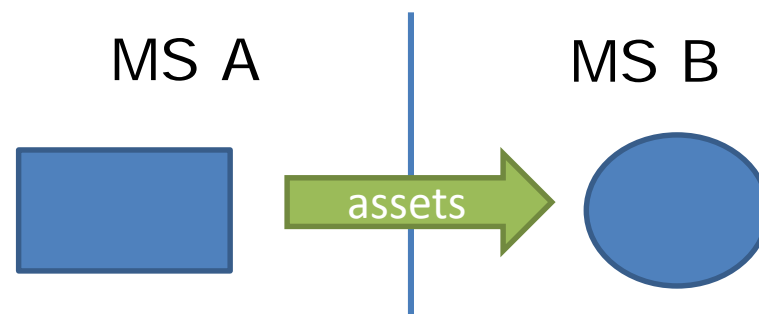
- Cash-flow disadvantages for cross-border situations seem to be in conflict with fundamental freedoms
- However: ECJ accpets cash-flow disadvantages
 - Payment of exit tax in 5/10 annual instalments (*DMC, Verder LabTec*)
 - No deduction with recapture for foreign losses (*Marks & Spencer, Lidl Belgium, Timac Agro*)
 - Withholding tax (and credit) instead of assessment (*Scorpio, X, Brisa*) (*Denkavit, Amurta*)

Why?

Exit Tax



capital gains are taxed
upon actual realization only



tax payment on hidden reserves
at the time of exit

Issue of Discrimination

- Time of tax payment:
cash-flow disadvantage
- Tax amount:
non-deductibility of subsequent
reductions in value

Justifications

- Efficient tax collection,
if non-resident person ✓✗
- Balanced allocation of
taxing rights ✓

From *de Lasteyrie* and *N ...*

2004-2006

- Time of tax payment:
 - Immediate payment disproportional - deferral until actual realization
 - No guarantee for deferral
- Tax amount: subsequent reductions in value deductible, unless in other state

... to *National Grid Indus ...*

2012

- Time of tax payment: Guarantee and interest for tax deferral
- Tax amount: No consideration of subsequent reductions in value

... and *Com/DK, DMC, Verder LabTec, Com/Port*

2013-...

- **Choice** between immediate payment and payment in **5 annual instalments**
- „no objective reason for distinguishing between the exit taxation of natural persons and that of legal persons" (*Com/Port*, 2016)

Art 5 ATAD: payment in 5 annual instalments obligatory

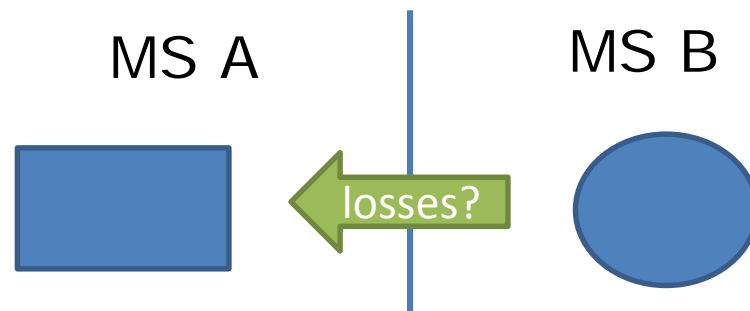
- Cash-flow disadvantage inseparably linked to balanced allocation of taxing rights?
 - Separate evaluation of both discrimination issues possible, but ...
 - Many assets are not sold (depreciable assets, shares, intangibles)
→ hidden reserves are exploited without alienating ownership

"a period of recovery where the tax is payable in allotments better reflects the contribution of these rights to the ability to pay tax"
(AG Jääskinen in *Verder LabTec*)
- Deferral of exit tax not only linked to effective tax collection, but also to balanced allocation of taxing rights
 - Payment in instalments combats profit shifting by relocation of functions and assets (Art 5 Anti-Tax Avoidance Directive)
 - Exit tax state indirectly participates in the profits generated by using the hidden reserves built up in its territory

Foreign Losses



Losses are deductible immediately



Losses are not deductible in MS A
Losses may be deductible in MS B
in subsequent years (carry forward)

Issue of Discrimination

- Tax amount: non-deductibility of foreign losses
- Time of loss utilization: cash-flow disadvantage

Justification

- Balanced allocation of taxing rights ✓
- Efficient tax collection **not** a valid justification, since resident taxpayer ✗

From *Marks & Spencer, Lidl Belgium* ...

2005-2008

- Time of tax payment:
 - cash-flow disadvantage not analyzed; deduction-recapture not necessary
 - AG Sharpston in *Lidl Belgium*: deduction with automatic recapture after five years = less restrictive means
- ~~▪ Tax amount: only „final“ losses need to be deducted~~

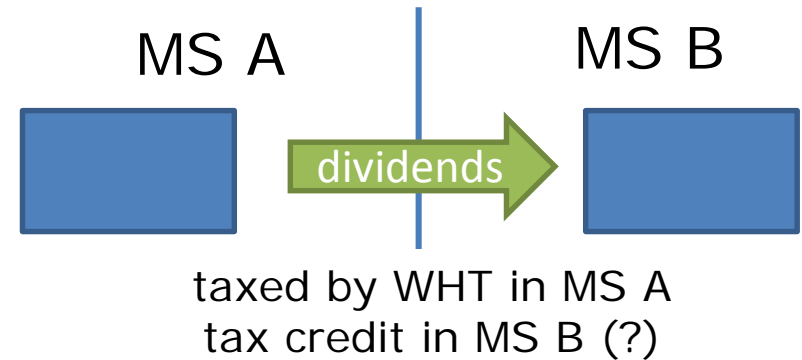
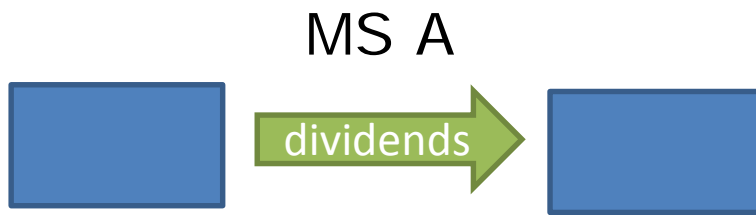
... to *X Holding, K, A Oy, Com/UK, Timac Agro* 2010-...

- Time of tax payment
 - deduction with recapture still not obligatory
 - on the contrary: „**penalized**“: „final loss“-doctrine applies (*Timac Agro*)
- Tax amount: very high requirements for „final losses“: rendered ineffective

Art 42 CCTB proposal: deduction with automatic recapture

- Cash-flow disadvantage inseparably linked to deductibility of losses and balanced allocation of taxing rights?
 - Separate evaluation possible
 - deduction with automatic and full recapture to avoid cash-flow disadvantage (Com(2006) 823, CCTB proposal 2016)
 - non-recapture of final loss to ensure balanced allocation of taxing rights
- Recapture Rule leads to other disadvantages for taxpayer?
 - Administrative burdens due to the need for recalculation and monitoring of foreign losses = restriction as well
 - However: free choice between deduction with automatic recapture and non-deductibility less restrictive? (similar option in *NGI*)
- Implicit justification by the need for administrative simplification?

Withholding taxes



Is there a different treatment at all?

Issue of Discrimination

- Tax amount: heavier tax burden
- Time of tax payment: cash-flow disadvantage
- Administrative obligations for payer: withholding, liability

Justification

- ~~Neutralization by other state?~~
- Efficient tax collection ✓ ✗

From *Scorpio* and *Truck Center* ...

2006-2008

- Time of tax payment: Tax collection by withholding proportionate, no mutual assistance (*Scorpio*), with mutual assistance (*Truck Center*)

Denkavit, Amurta, Com/Italy, Com/Spain, Miljoen 2006-...

- Tax amount: neutralization by tax credit in a DTA possible
- Time of tax payment: cash-flow disadvantage not discussed at all

... and *X, Strojirny Prostejov, Brisal*

2012-...

- Time of tax payment: withholding tax proportionate
 - the aim of the Tax Collection Directive „*was not to replace the taxation at source as a method of collecting tax*“ (X, C-498/10)
 - disproportional if taxpayer has a „*physical presence in the territory*“ (*Strojirny*)

- Cash-flow disadvantage inseparably linked to tax amount?
 - Separate evaluation possible
 - higher tax burden may be offset by DTA tax credit in other MS
 - method of withholding could be replaced by assessment (pay tax in MS A after credit in MS B only)
- Is there an unequal treatment at all?
 - residents might equally be subject to WHT with refund (*Miljoen*)
- Assessment leads to other disadvantages for taxpayer? (AG Kokott in *Truck Center/X*, ECJ in *X*)
 - Income recipient: administrative burdens (declaration, language); payer: reporting obligation = restriction as well
 - However: Free choice between WHT and assessment less restrictive (similar in *NGI*)?
- Implicit justification by the need for administrative simplification?

- Cash-flow disadvantages are treated very differently and are increasingly accepted by the Court
- Tax Collection Directive: possibility to ask for assistance should render denial of tax deferral disproportional in many cases
- Possible reasons for stricter approach chosen by the Court
 - cash-flow disadvantage is linked to a higher tax burden
→ however: separate evaluation possible in many cases
 - tax deferral may lead to other disadvantages for the taxpayer
→ however: free choice for the taxpayer more proportional (example *NGI*)
 - Implicit justification by the need for administrative simplification?

*„While it is true that considerations of an administrative nature cannot justify a derogation by a Member State from the rules of EU law (...) Member States cannot be denied the possibility of attaining legitimate objectives through the introduction of rules which **are easily managed and supervised** by the competent authorities“ (Sopora, para. 33)*

Thank you!



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Taxation - Retroactive effect and EU Law

prof. dr. Dennis M. Weber
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EU law with retroactive effect

Substantive law

- ☐ Not allowed: based on principle of legal certainty (*Racke*-case)
- ☐ Permitted:
 - ☐ a. “where the purpose to be achieved so demands”
 - ☐ b. “where the legitimate expectations of those concerned are duly respected”

***Goed Wonen-II*-case (press release to prevent notification effects)**

- ☐ Press release 31 March 1995: future legislation announced: after approval: in force 31th March 1995, 18.00
- ☐ direct retroactive effect
 - ☐ Fear that new financial arrangements on a large scale will be put place
- ☐ CJEU: such fear is not unfounded, provided that legitimate expectations are duly respected
 - ☐ The procedures for dissemination of information normally used by the Member States must be taken into account
- ☐ CJEU: is the press release sufficient clear “to understand the consequences of the legislative amendment”

EU law with retroactive effect

Procedural rules

- Immediately enter into effect
- also applicable to all disputes which are pending before the time that they enter into effect
- Retroactive effect permitted
- *Tsapalos-case*: Mutual Tax Recovery Directive also applicable to tax claims – from before the Directive entered into effect

Immediate entering into effect of national legislation – transitional provisions -

- ☐ This is not retroactive effect
- ☐ Permitted (*Gemeinde Altrip*)
 - ☐ ‘Prudent and discriminating trader’
 - ☐ A trader cannot rely that a law will never change (*Gemeente Leusden/Berlington*)
 - ☐ Prevention of tax avoidance or fraud is OK (*Gemeente Leusden*)

Transitional period?

- Principle of the protection of legitimate expectations
 - Particular situations
 - When change is suddenly and unexpected
 - The objective did not require it
 - Allowing the taxpayer the time necessary to adjust
 - In particular, taxable persons must have time to adapt when withdrawal of the right which they enjoyed until then obliges them to carry out consequential economic adjustments (*Rey*, para. 62); costly investments (*Berlington*, para. 87)

Examples-I

- *Gemeente Leusden: VAT from taxed to exemption*
 - legislative amendment announced by press release and provision for transition from taxed to exempt: so time to adapt
- *Plantanol: tax exemption on energy products withdrawn prior to the expiry date: Forseeable?*

Examples-II

- *Berlington* (C-98/14)
 - Introduction of very high tax (two different taxes) and transition of new operating system, but prohibiting the operation outside casinos
 - CJEU: restriction, but could be justified by the protection of gambling protection
 - No transitional period: check breach of legal certainty and legitimate expectations
 - Introduction of 5 fold increase of flat ate tax + introduction of proportional tax
 - First change in tax regime in 20 years
 - Automatic revocation of licenses
 - invested in new system for slot machines (1 Jan. 2013); withdrawn with the law of 1 Jan. 2012

Examples-III

- ☐ *Wolfgang and Wilfried Rey* (C-332/14): change in input tax adjustment
- ☐ No withdrawing of a right to deduct input VAT
- ☐ But of adapting its ambit
- ☐ Consequential economic adjustments seems not necessary
- ☐ AG Mengozzi: legislation with retroactive effect: forbidden unless

Time, Tax and the Fiscal Merger Directive

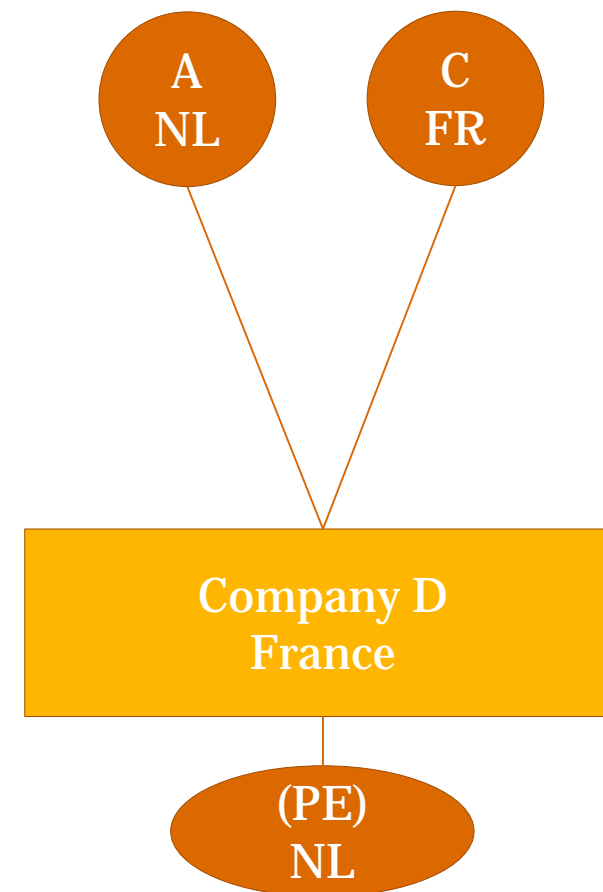
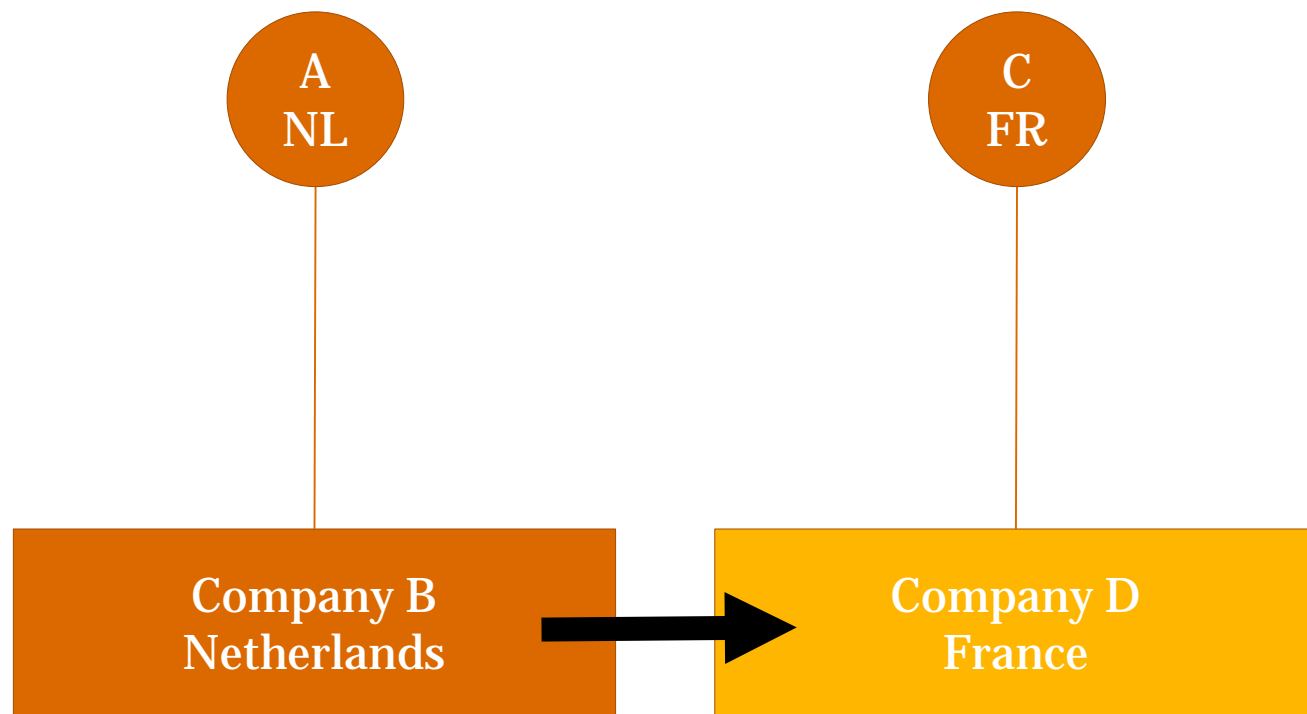
Frederik Boulogne

Timing and the Merger Directive

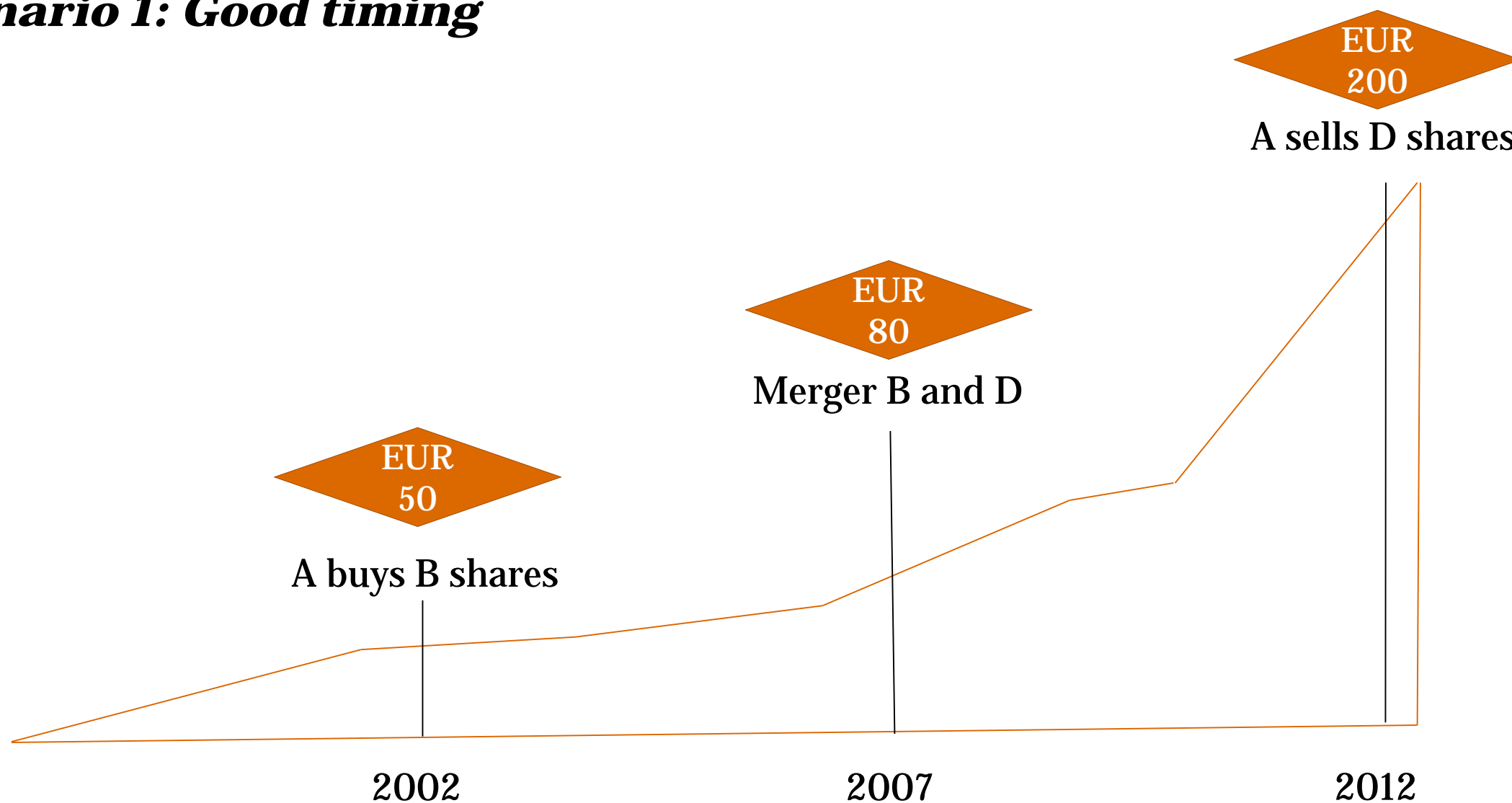
Key timing issues from Merger Directive perspective:

1. Does it matter when a restructuring operation takes place?
2. Does it matter when the subsequent sale of shares takes place?

A basic merger



Scenario 1: Good timing



Scenario 1: Good timing

2002

Shareholder A values its shareholding in Company B at 50

2007

Virtual gain on shares of 30 (80-50), but Shareholder A elects for carry-over relief (Art. 8 MD)

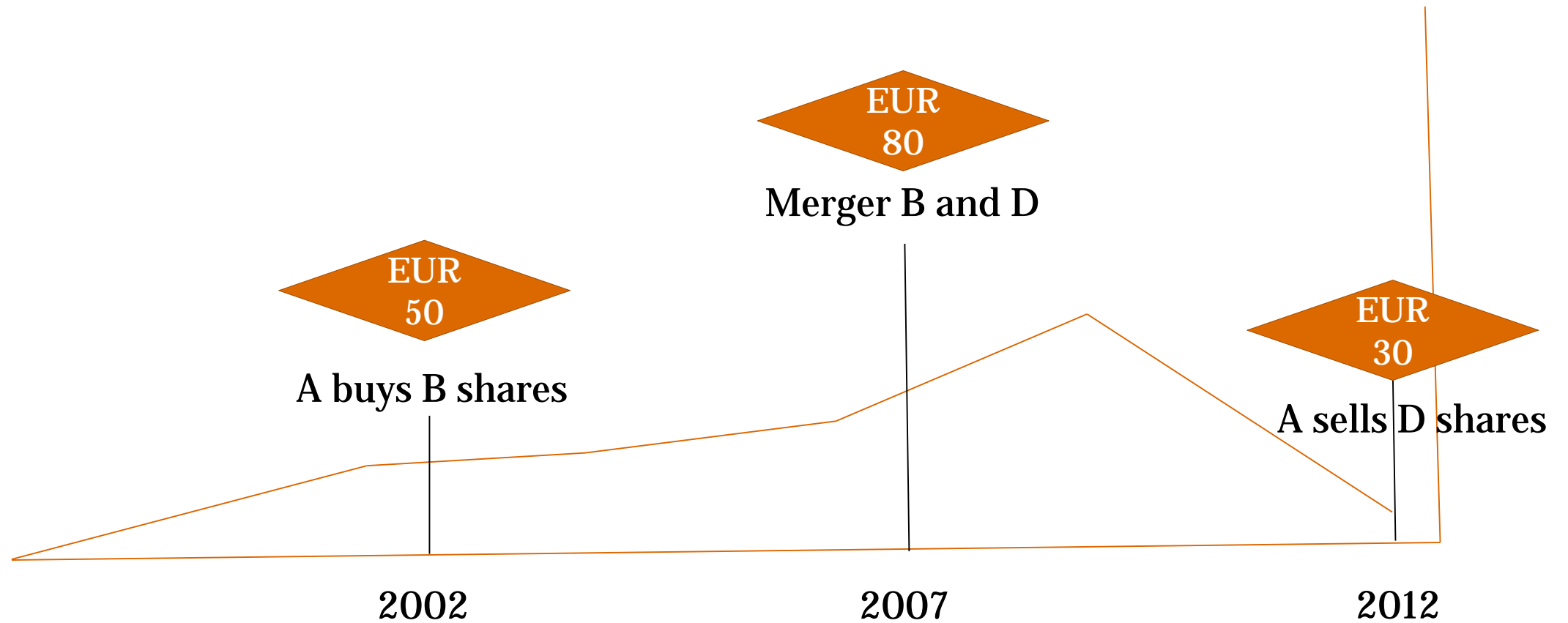
2012

Shareholder A is taxed by Luxembourg on gain realised of 150 (200-50).

What if no carry-over relief? A would be taxed on 30 first, and 120 afterwards.

Economically: also a 150 gain for Shareholder A

Scenario 2: Bad timing



Scenario 2: Bad timing

2002

Shareholder A values its shareholding in Company B at 50

2007

Virtual gain on shares of 30 (80-50), but Shareholder A elects for carry-over relief (Art. 8 MD)

2012

Shareholder A incurs a loss of 20 (50-30). Perhaps deductible, then carry-back/carry-forward.

What if no carry-over relief? A would be taxed on 30 first, perhaps carry-back for loss of 20.

Economically: a 20 loss for Shareholder A

Conclusions from Scenarios 1 and 2

Merger Directive aligns tax treatment with economic result

Because without the Merger Directive:

- Cash-flow disadvantage (in the good scenario)
- Possibly a permanent tax disadvantage (in the bad scenario)

As a result of carry-over mechanism (instead of 'fixing' tax claim): tax does not affect timing of restructuring and sale of shares

Complication – change in regime

Assume : A is corporate shareholder -> 100% shareholding in B to 3% shareholding in D

Participation exemption regime now no longer applicable

Art. 8(6) MD: Netherlands may continue to apply 'old regime' (but won't do that)

Taxation of full 150 gain? Or compartmentalisation and 'only' tax 120?

Applying participation exemption (instead of carry-over relief): better choice. Election for carry-over relief not useful.

Is ‘fixing’ a gain allowed after all? Marc Lassus (C-421/16)

Exchange of shares (French shares into Lux company).

‘Fix’ gain at time of exchange of shares?

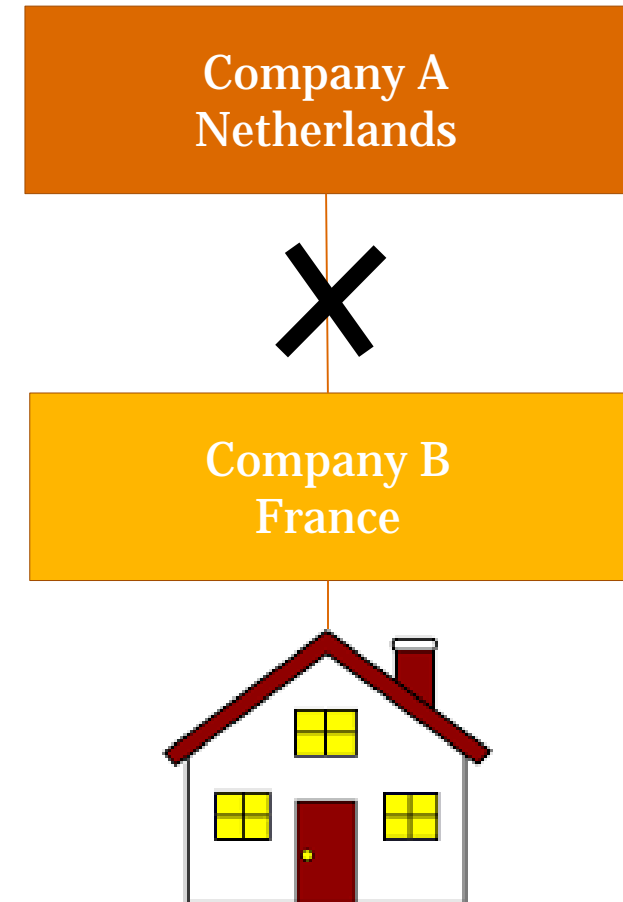
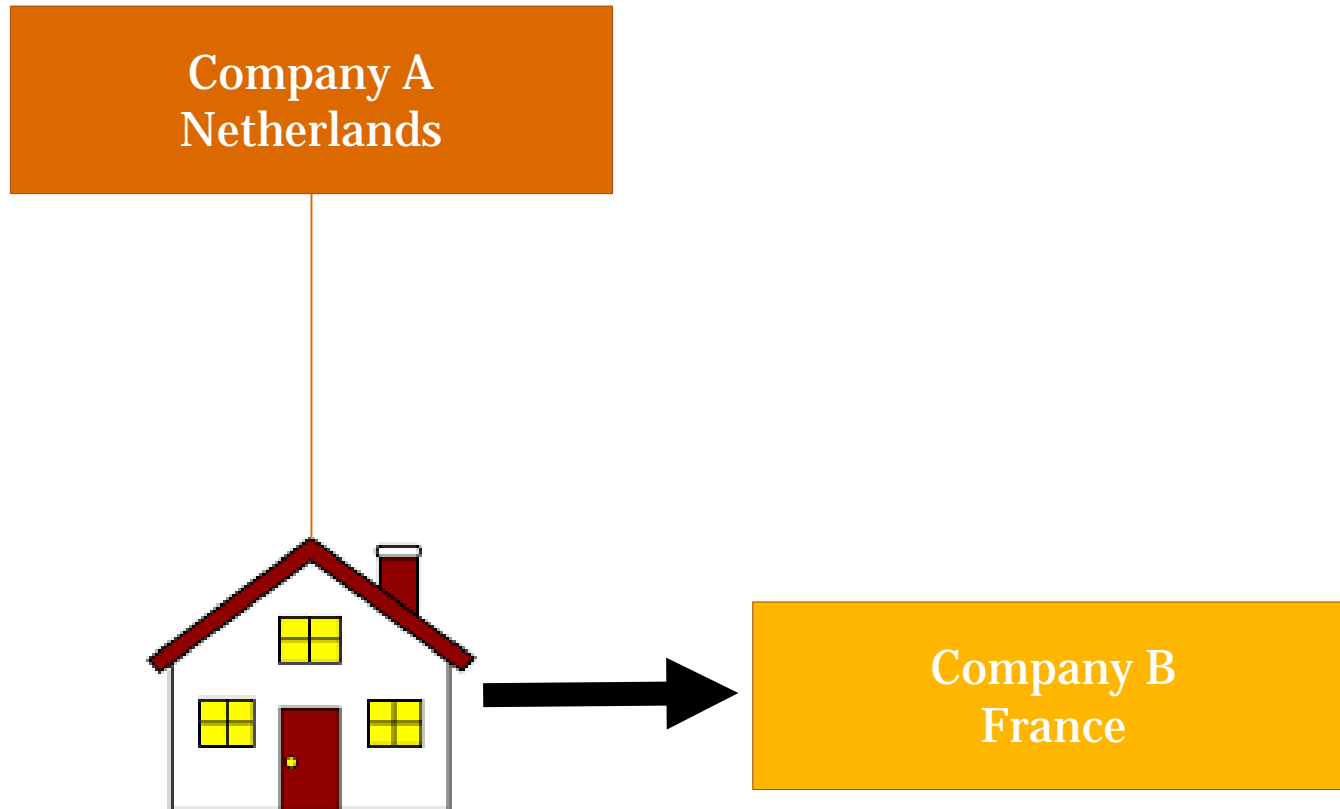
Tax that gain when shares in acquiring company are sold?

Even if no taxing right over those shares?

Offset subsequent loss?

Value calculation

Timing: transfer of assets followed by sale of shares



Timing: transfer of assets followed by sale of shares

What if sale follows relatively quickly after transfer of assets?

Still a 'transfer of assets' (Art. 2 MD)?

Kofoed (C-321/05) decision suggests literal interpretation of requirements

Anti-avoidance provision (Art. 15 MD)?

Depends on interpretation of Merger Directive's objective

'Hard' minimum gap requirement (e.g. 3 years)?

Although proposed, doubtful if compliant

Thank you

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The Evolution of the Internal Market & the Application of State Aid Law to Tax Rules

Luxembourg, 26 January 2017

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- **Issues raised by the application *rationae temporis* of EU State aid rules in the area of taxation**

- 1. Time frame of the Commission's control**

- Risk for MS (procedural) tax autonomy?

- 2. Recovery of unlawful aid (with a 10 years limitation period)**

- Intrinsic legal uncertainty & violation of legitimate expectations ?

- 3. Potential evolutionary interpretation of EU State aid law**

- Linked to the development of the internal market?

1. Key role of 'timing' in EU State aid law

- **Notification by the Member State (art. 108, §3 TFEU)**

"The Commission shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. If it considers that any such plan is not compatible with the internal market having regard to Article 107, it shall without delay initiate the procedure provided for in paragraph 2. The Member State concerned shall not put its proposed measures into effect until this procedure has resulted in a final decision"

- **Commission's final decision within 2 months**

- Explicit or tacit approval
- Decision to initiate the formal investigation procedure

- **See Council Regulation 2015/1589**

1. Key role of 'timing' in EU State aid law

Existing aid

- **Existing aid (art. 108 TFEU, §1 and 2)**

“1. The Commission shall, in cooperation with Member States, keep under constant review all systems of aid existing in those States. It shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the internal market.

2. If, after giving notice to the parties concerned to submit their comments, the Commission finds that aid granted by a State or through State resources is not compatible with the internal market having regard to Article 107, or that such aid is being misused, it shall decide that the State concerned shall abolish or alter such aid within a period of time to be determined by the Commission. (...)”

➤ **Influence of progressive development of the Internal market on the notion of State aid?**

1. Key role of 'timing' in EU State aid law

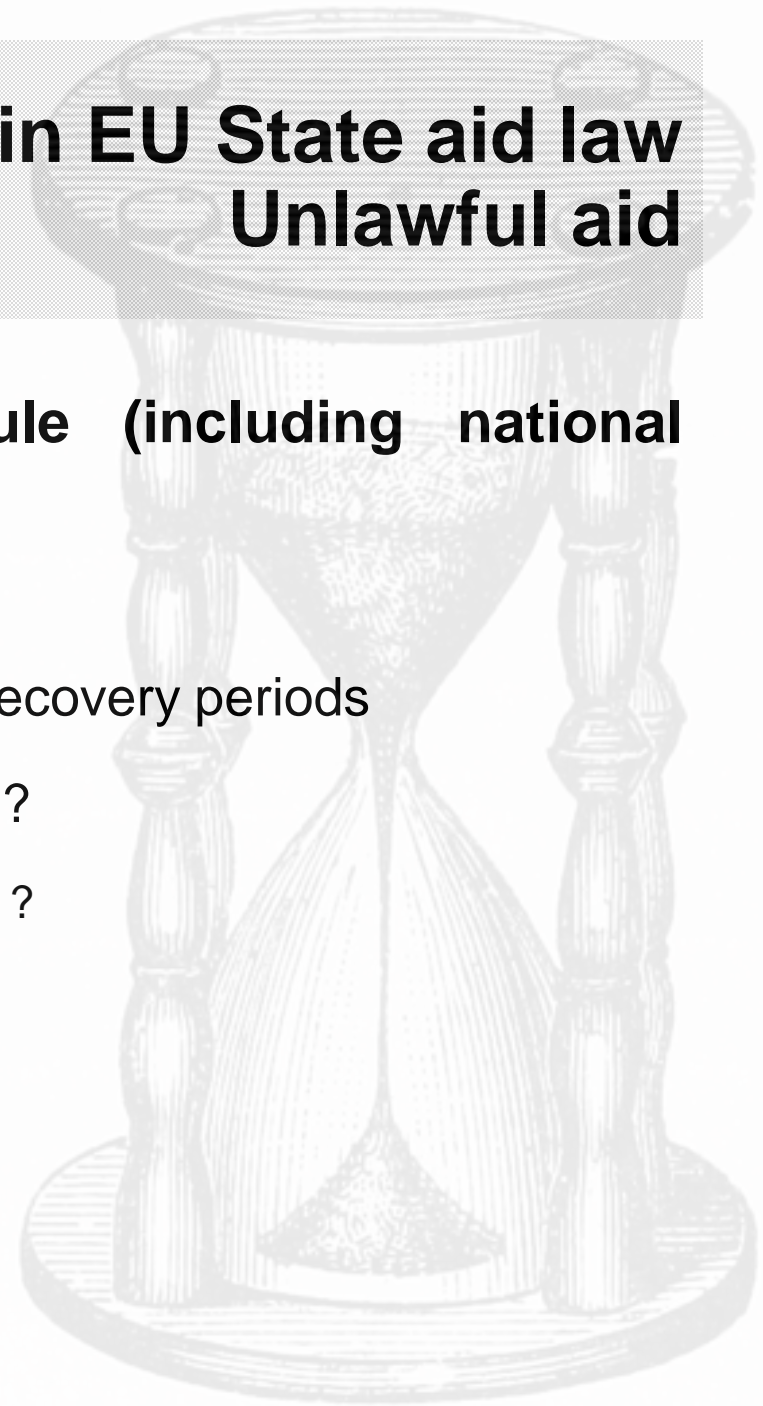
Unlawful aid

- **In the absence of (complete) notification**
 - For MS, Commission & **beneficiary undertakings** : recovery within a 10 years' limitation period
- **Starting point**
- **Duration : Not 18 + 2 months (exception)**
- **Total : more than 10 years!**
- **Exceptions :**
 - Absolute impossibility to recover the aid (e.g. 'impossible to extrapolate retroactively')
 - Legal certainty – legitimate expectations

1. Key role of 'timing' in EU State aid law

Unlawful aid

- **Gap with MS procedural tax rule (including national limitation periods)**
 - Different goals ?
 - Distinction between establishment and recovery periods
 - Conflicts between EU and domestic law ?
 - Violation of MS tax (procedural) sovereignty ?



2. Recovery issues (A)

A. Time and legal certainty

- **Intrinsic characteristic of EU State aid law ?**

- Procedural guarantees (Council Regulation 2015/1589)
- For MS & beneficiary undertakings
- Factors: complexity of the measure; appearance of compliance (by the Commission, not the MS!)
- Consequences: no or limited recovery (SA.21233 C/2011) ; transitional measures (Joined cases C-182/03 & C-217/03)

- **Specificity of tax law:** integration in the general tax system (heavy burden on undertakings!)

2. Recovery issues (A)

Time is not sufficient

- *“A **long lapse of time as such is insufficient** to claim legal certainty and a delay can be imputed to the Commission only from the time when it learnt of the existence of the aid. In this case, since the contested tax rulings were never notified to the Commission by Ireland, nor otherwise publicly available, the Commission could only have learnt of the existence of those rulings when their existence was publicly disclosed, which happened for the first time during hearings of the US Senate”.*

Commission decision of 30 August 2016 on State aid SA.38373 (2014/C)
[Apple case], para. 440.

2. Recovery issues (A)

Evolution in time of legal certainty

- “In view of the complexity of the measures at hand, the Commission cannot exclude that there may have been **legal uncertainty**, as alleged by Spain and the beneficiaries (...) but only until the publication in the OJ on **30 April 2007** of the Commission decision concerning the French GIE Fiscaux, where the Commission established that such scheme constituted State aid.
- As a consequence the Commission concludes that it should not order the recovery of the aid resulting from STL operations in respect of which the aid was granted between the entry into force of the SL in 2002 and **30 April 2007”**.

2. Recovery issues (A)

Legal certainty and transition

- “(...) *in the absence of an overriding public interest, the Commission infringed a superior rule of law by failing to couple the repeal of a set of rules with **transitional measures** for the protection of the expectations which a trader might legitimately have derived from the Community rule*”.

CJEU, 22 June 2006, Kingdom of Belgium and Forum 187 ASBL v. Commission of the European Communities, Joined Cases C-182/03 and C-217/03, §149.

2. Recovery issues (A)

Legitimate expectations

- Subjective dimension
- Role of the EU institutions
- Potential change over time
- Excessive burden of proof on beneficiaries?



2. Recovery issues (B)

- **B. Calculation of the aid to be recovered**
- **Recovery decision : ‘self executing’ ?**

➤ Commission:

“National authorities are allowed to take into account the incidence of the tax system in order to determine the amount to be reimbursed (...) [The may] take account of the earlier payment of tax by recovering only the net amount received by the beneficiary”.

Notice from the Commission – Towards an effective implementation of Commission decisions ordering Member States to recover unlawful and incompatible State aid, OJ C272, 15 November 2007, pp. 4-17.

2. Recovery issues (B)

Illustration

- **The Belgian excess profit rulings case**

- Chapter 5 of “Program Law” of 25 December 2016 : Regime to recover the aid concerning the excess profit ruling
 - Aid to be determined by calculating (again!) the tax that should have been paid, based on the tax law in effect at the time, without taking into account the excess profit rulings but by taking into account deferred tax advantages, based on the new calculation (art. 101 & 102)
 - Impact on future tax returns: need to adapt deferred tax advantages that 'disappear' due to recalculation (art. 103)
 - Non application of usual recovery deadlines in case of unpaid (enrolled) taxes based on art. 288 TFEU (art. 116)

3. Evolutionary interpretation of the notion of aid

- **EU State aid law : a *political* instrument ?**

“Applying the arm’s length principle as a State aid tool and suggesting that it has been part of Union law since 1958 would constitute a total rewriting of history and be inconsistent with the principle of legal certainty”

Irish government in EC Apple Decision, 30 August 2016; para. 197

3. Evolutionary interpretation of the notion of aid

*“In order to ensure **legal certainty**, it is appropriate that the circumstances under which aid is to be considered as existing aid be defined. The **completion and enhancement of the internal market** is a **gradual process**, reflected in the permanent development of State aid policy. Following those developments, certain measures, which at the moment they were put into effect did not constitute State aid, may since have become aid”.*

3. Evolutionary interpretation of the notion of aid

- **Are the decisions on tax rulings the result of an evolution of the State aid concept linked to the development of the Internal market ?**
 - **Clear criticism** following the Commission' decisions on tax rulings
 - **Commission's "activism" under pressure of NGO and public opinion?**
 - **According to the Commission : NO**
 - **'Old' argument** related to the strengthened role of the Commission, following the adoption of the Code of Conduct
 - *Belgian Coordination Centres case*
 - *But EU State aid law is the legal basis (no new law: no retroactivity)*
- **Constitutional dimension of the debate from a MS perspective**
 - **Legality of taxation vs. Equality of taxation**
 - **Internal market as fair competition** ("competition among equals" and "without undue intervention on cross-border trade")



Many thanks for your attention



Effective Legal Remedies and Fair Trial in Tax and Time

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Effective judicial protection in tax and time

■ *'Justice delayed is justice denied'*

- *'Concept of effective judicial protection'* broad concept which generally encompasses various core elements, including *access to justice*, the *right to an effective remedy* and the *principles of fair trial* and *due process of law*.
- The *time* element
 - Excessively lengthy procedures/delays in the administration of justice.
 - Limitation periods / insufficient time
 - to bring an action for taxes unduly paid or
 - to be heard within a reasonable time
 - to prepare his case/defense
 - to apply to be granted a tax advantage
 - to comply with a tax assessment

Effective judicial protection: Legal context

- Art. 19 (1) TEU: Member States shall provide remedies sufficient to ensure *effective legal protection* in the fields covered by Union law.
- essential element of the ‘rule of law’ within the EU and as such general principle of EU law. ‘ [A] principle “which must be taken into consideration in Community law [as it] underlies the constitutional traditions common to the Member States and [...] is laid down in Articles 6 and 13 of the ECHR (Johnston Case 1986)
- Charter of Fundamental Rights
- ECHR
- Constitutional principle / National procedural autonomy (‘restricted’ by principles of equivalence and effectiveness)
- Effective judicial protection *in tax law*
 - Ensure access to justice
 - Ensure access to legal remedies and possibility to be refunded if breach.

} ...within a reasonable time!!

Legal Context: Charter of fundamental rights

- Art. 41 Charter ‘Right to good administration’
 - Every person has the right to have his or her affairs handled impartially, fairly and *within a reasonable time* by the institutions and bodies of the Union.
- Article 47 Charter ‘Right to an effective remedy and to a fair trial’
 - ‘Everyone whose rights and freedoms guaranteed by the law of the Union are violated has the *right to an effective remedy* before a tribunal in compliance with the conditions laid down in this Article.
 - Everyone is entitled *to a fair and public hearing within a reasonable time* by an independent and impartial tribunal previously established by law. Everyone shall have the possibility of being advised, defended and represented.’

Legal Context: ECHR

■ Article 6 ECHR - *Right to a fair trial*

In the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing *within a reasonable time* by an independent and impartial tribunal established by law. Judgment shall be pronounced publicly [...].

■ Article 13 ECHR - *Right to an effective remedy*

Everyone whose rights and freedoms as set forth in this Convention are violated shall have *an effective remedy* before a national authority notwithstanding that the violation has been committed by persons acting in an official capacity.

- Of all guarantees of Art. 6, alleged violations of the reasonable time requirement account for the largest proportion of cases before the ECHR
- Evidence of systemic problems within domestic judicial systems.
- MS can avoid a violation of Art. 6 by compensating for the excessive duration of the proceedings (compensation, reduction of a fine).

Definition of 'reasonable time'

- 'the approach taken thus far to establishing whether proceedings have been unduly lengthy has perhaps been more *pragmatic than scientific*.' [AG Sharpston, Groupe Cascogne]
- 'I cannot emphasise sufficiently that quantifying *delay* is not an exact science. Any assessment is *approximate*.' [AG Sharpston, Groupe Cascogne]
- Ad hoc basis, general criteria (CJEU and ECHR):
 - **the complexity of the case,**
 - **the behavior of the applicant** in comparison with that of the judicial authorities & his contribution to the delay,
 - The behavior of the domestic authorities
 - **The importance of the dispute for the applicant.**

Art. 6 ECHR: 'a fair and public hearing within a reasonable time'

- Applicability?? [If criminal character of the offense/ tax penalty as a 'criminal charge']
 - **Ferrazzini (2001):** 'The Court considers that tax matters still form part of the hard core of public-authority prerogatives [...] It considers that tax disputes fall *outside* the scope of civil rights and obligations, despite the pecuniary effects which they necessarily produce for the taxpayer.'
 - **Jussila (2006):** tax surcharges which, although, were part of the fiscal regime, were imposed by a rule whose purpose was *deterrent* and *punitive* => criminal offense, within the meaning of Article 6 ECHR.
 - **Janosevic v. Sweden & Vastberga Taxi Aktiebolag and Vulic v. Sweden (2001):** tax surcharges and the purpose of the penalties (deterrent and punitive) = *criminal offence* within the meaning of Article 6 ECHR .
 - violation of Article 6(1) ECHR. '[...] in taking *almost three years to decide the applicant's requests for reconsideration of the assessments*, the tax authority had failed to act with the urgency required by the circumstances of the case and thereby *unduly delayed* a court *determination* of the main issues concerning the imposition of additional taxes and tax surcharges.
 - **Yukos (2011):** Article 6(1) ECHR had been violated in consequence of the wholly insufficient time given to Yukos to prepare its case at first instance and on appeal in respect of its alleged tax liability.

Art. 13 ECHR: Effective remedy

- Since remedies under Art. 13 ECHR must be ‘effective’ both in law and in practice, undue delays in providing remedies due to **lengthy procedures** might render it ineffective.
 - Ex. An appeal might be rendered practically ineffective by the length of the proceedings and hence be in breach of Art. 13 ECHR. [Bottazzi v. Italy]
- Kudla v. Poland: the applicant had **no domestic remedy** whereby he could enforce his right to a “**hearing within a reasonable time**” as guaranteed by Article 6 § 1 of the Convention.
 - Violation of Art. 13 ECHR in addition to Art. 6 ECHR the ECHR when there is no internal remedy available to deal with violations of the reasonable time requirement.
 - ‘If Article 13 is [...] to be interpreted as having no application to the right to a hearing within a reasonable time as safeguarded by Article 6 § 1, individuals will systematically be forced to refer to the Court in Strasbourg complaints that would otherwise, and in the Court’s opinion more appropriately, have to be addressed in the first place within the national legal system. 156. In view of the foregoing considerations, the Court considers that the correct interpretation of Article 13 is that that provision guarantees an effective remedy before a national authority for an alleged breach of the requirement under Article 6 § 1 to hear a case within a reasonable time.’

Charter of fundamental rights vs ECHR

- Article 47 (1) Charter 'is based on Article 13 of the ECHR' and Art. 47 (2) corresponds to Article 6(1) of the ECHR.
- Article 47 of the Charter has a **wider scope** *ratione materiae*. It applies where '[the] rights and freedoms guaranteed by the law of the Union are violated' (whether or not they are set out in the Charter), whereas Article 13 of the ECHR requires a violation of '[the] rights and freedoms as set forth *in the [ECHR]*'. In addition, Article 6(1) of the ECHR limits the right to a fair trial to the determination of civil rights and obligations or of any criminal charge. No such restriction is to be found in the second paragraph of Article 47 of the Charter. Charter should also be effective in **pure administrative law proceedings**, as opposed to Art. 6 ECHR)
- Applicability of the Charter
 - Art. 51 (1) the Charter can be relied on as against Member States only when *they are implementing Union law*. (*this way the link to rights and freedoms guaranteed by EU law is established*)
 - 'the intention to authorise the automatic application of Article 47 of the Charter where the Charter is itself applicable is enshrined in the use of the expression 'hearing' in the second paragraph.' [AG Wathelet, Berlioz]
 - 'it seems logical that the systematic identification of a specific right or freedom guaranteed by the law of the Union as a condition for the application of the right to an effective remedy is not required in the Court's case-law.' [AG Wathelet, Berlioz]

Limitation periods

- Legal proceedings may not be initiated once a defined period of time has elapsed after loss has been suffered.
 - Detrimental to the effective protection of the taxpayer who might miss a deadline
 - Valuable to the promotion of legal certainty and efficient administration of justice.
 - Limitation rule cannot be so short so as to deny the applicant effective protection of his EU law right.
 - It is for the national law to determine from when time starts to run, subject only to the proviso that this must not totally deprive an individual of an opportunity to enforce his rights.
- *Mutandis mutandis* for assessment of rules for restitution, refunds of tax & application to be granted tax advantage.

When should the limitation period start running from?

- Classification of the action/ Nature of the claim/ Procedural issues: national court to decide (*Metallgesellschaft*)
 - Restitution vs. damages = longer time limits > high protection to taxpayers
 - Administrative law procedures for refund vs. civil law procedures for damages
- 'The existence of a wholly independent claim for damages, subject to **longer time limits** than the comparatively short ones prescribed for restitutionary and entitlement claims in many Member States, is consistent **with the different nature of the claim**. Its basis is not merely the unjust enrichment of the State resulting from simple error in the routine application of technical legislation but a serious violation of individual rights, calling for a re-appraisal of the balance between such rights and the collective interest in a measure of legal certainty for the State.' [AG Jakobs, Fantask]
- The starting point of the time limit for bringing a claim for reimbursement of taxes unduly made should be moved to the time when the measure is found to be contrary to EU law [= when the relevant CJEU decision is published]
 - *Metallgesellschaft*
 - UK Courts: Unjust enrichment and right to restitution covered ACT.
 - Question: 'When could have the mistake been reasonably discovered?' [CJEU judgment]
- Deem that the time limit starts running as from the time the right to a refund was born [= the incompatibility of the measure at issue was established and the right to refund was born]

Other safeguards: Procedural Aspects in limitation periods

- National procedural autonomy: ‘[...] it is for the domestic legal system of each Member State [...] to lay down the detailed procedural rules governing actions for safeguarding rights which individuals derive from Community law, provided, first, that such rules are not less favourable than those governing similar domestic actions (**principle of equivalence**) and, secondly, that they do not render virtually impossible or excessively difficult the exercise of rights conferred by Community law (**principle of effectiveness**)’ [Rewe & settled case law]
- Time – limits in recovery of unlawful /unduly paid charges= compatible with EU law, provided that principles of equivalence and effectiveness are respected.
 - “[I]t is compatible with Community law to lay down reasonable limitation periods for bringing proceedings in the interests of **legal certainty** which protects both the taxpayer and the administration concerned.” [effectiveness]
 - “[...] in order to serve their purpose of ensuring legal certainty, **limitation periods must be fixed in advance**. A situation marked by significant legal uncertainty may involve a breach of the principle of effectiveness [...]’
 - Intransparent or discretionary time limit not in compliance with EU law.

Other safeguards – Procedural Aspects: Equivalence

- ‘Community law precludes the competent authorities of a Member State from relying, in proceedings brought against them by an individual before the national courts, [...] on national procedural rules relating to time-limits for bringing proceedings so long as that Member State has not properly transposed that directive into its domestic legal system.’ [Emmot, par. 24]
 - ‘[...]the solution adopted in Emmott was justified by the particular circumstances of that case, in which the time-bar had the result of depriving the applicant of any opportunity whatever to rely on her right to equal treatment under a Community directive’ (*Texaco and Olieleskabet Danmark [1997] Johnson v Chief Adjudication Officer [1994]*).
- Tax imposed in violation of EU law, taxpayer can bring an action for recovery of the tax in accordance with national rules that govern the recovery of taxes unduly paid, including time limits applicable to such actions. [Edis]
- ‘the existence of different rules on limitation periods does not breach the principle of equivalence.’: MS may rely on a shorter time limit for tax refund claims, in derogation from ordinary rules of civil law applicable to actions between private individuals, provided that time limit applies **in the same way to tax-related actions based on EU law or on national law.** [IN.CO.GE]
 - Need for identification and comparison of (classification) of action.
- (Longer) time-limits applying to claims for unduly (=unconstitutionally) paid taxes should apply also to claims of taxes paid against EU law. [Weber’s Wine World]

Other safeguards – Procedural Aspects: Effectiveness

- Compatible with EU law to lay down reasonable time-limits for bringing proceedings to ensure legal certainty. Such time-limits do not make it impossible in practice or excessively difficult to exercise the rights conferred by EU law [Meilicke II (C-262/09)]
 - ‘excessively difficult’ must be assessed by reference to the role of that provision in the procedure, its progress and its special features, viewed as a whole, before the various national instances. [Peterbroeck, C-312/93]
- Ex. In cases of restitution of national taxes unduly levied, where the rules for restitution are amended by national law with retroactive effect, the principle of effectiveness requires new legislation to include **transitional arrangements** allowing an adequate period after the enactment of the legislation for lodging claims for repayment (*Grundig Italiana* [2002]).
- Subsequent case law: the limitation period might not apply if it appears that because of the limitation period the individual has no possibility of asserting the rights conferred to him by the Directive.

'Reasonableness' of limitation period: Examples

- Ad hoc: CJEU case law inconclusive
- ex. Non – tax cases: 15 day time to bring action for nullity not reasonable (*Pontin* [2009]) ≠ 'a 15 day time limit for bringing an action does not seem, generally, to be insufficient in practical terms to prepare and bring an effective action and appears reasonable and proportionate in relation to the rights and interests involved' (*Samba Diouf* [2011])
- ... a national limitation period of up to a minimum of 4 years and a maximum of 5 years preceding the year of the judicial decision finding the rule of national law establishing the tax to be incompatible with a superior rule of law **must be considered reasonable**. [C-88/99 Roquette Frères]
- a period of 60 days for bringing proceedings is not objectionable in itself (*Peterbroeck* [1995], *Asturcom Telecomunicaciones* [2009]).
- **[T]hat case-law also applies to the assessment of rules for the restitution of national taxes unduly levied** (*Meilicke and Others*). The same must therefore apply to the assessment of compliance with the principle of effectiveness as regards the **setting of a time-limit in connection with the submission of an application to be granted tax advantages**. Consequently, it does not appear that national legislation which grants the tax advantages provided for by Directive 90/434 **only on condition that the relevant application is made at least 30 days before the proposed restructuring operation** is liable to make it impossible in practice or excessively difficult to exercise the rights derived by the taxpayer from European Union law. (Pelati [2012])

Conclusions

- Many 'safeguards' to ensure 'effective legal remedies and fair trial' but
 - Either set of conditions (ECHR & Charter) or
 - Decided ad hoc → legal uncertainty for the taxpayer (and the State).
 - Domestic rules, either inexistent or not meeting the standards of effective judicial protection or ignored.
 - Much leeway to the MS to 'manoeuvre' with regard to
 - Classification of claims (escape principle of equivalence)
 - Determination of the starting point of the limitation period
 - Complexity and particular characteristics of the case.

“TIME AND TAX”

Constitutional Limits to Retroactivity in Tax Law

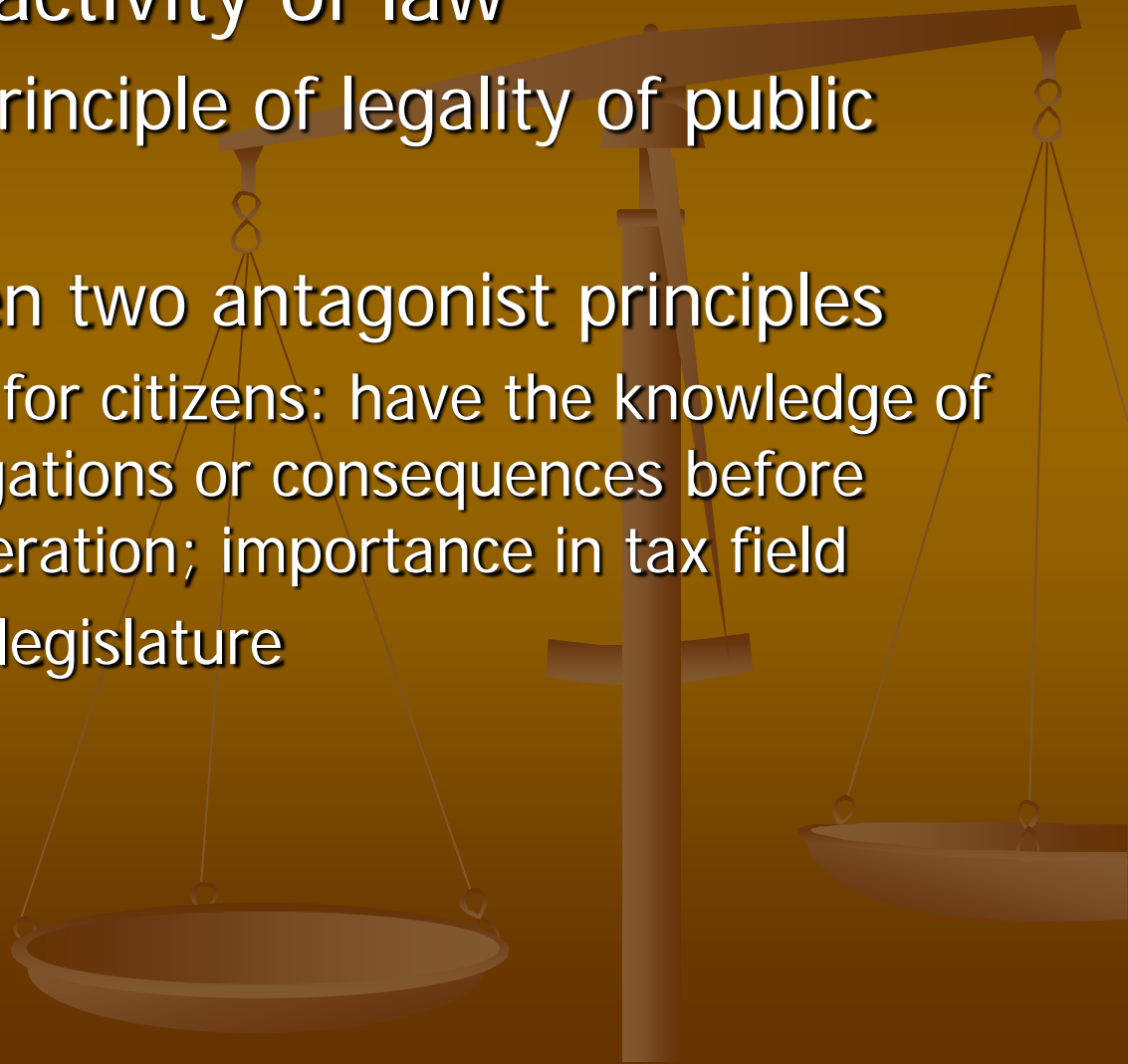
Serge N. SCHROEDER

Premier Conseiller à la Cour administrative



I. Retroactivity and retrospectivity

- Subject of retroactivity of law
 - related to the principle of legality of public action
 - Balance between two antagonist principles
 - Legal certainty for citizens: have the knowledge of rights and obligations or consequences before realizing an operation; importance in tax field
 - Sovereignty of legislature



I. Retroactivity and retrospectivity

■ Traditional distinction in retroactivity

- Legal or real retroactivity: new law applies to acts, facts and situations that have been definitely finalized before its entry into force
 - Periodic taxes: the taxable event of the end of period has occurred before the entry into force of the law
 - Tax based on a single taxable event: the event occurred before the entry into force of the law
- Economic or factual retroactivity: the new law applies entirely to acts, facts and situations that are still ongoing at the date of entry into force
 - Periodic taxes: the current period leading to taxable event is ongoing at the time of entry into force of the law
- Retrospectivity: the new law changes for the future a regime of continuous effects of a situation or an act definitely finalized in the past
 - New law changes favorable consequences attached for the future to an operation in the past

II. Legal retroactivity

- Legal situation in Luxembourg
 - In the lux. Constitution only art. 14: legality of sanctions → implies retroactivity of lower sanction (Cour const. 22-3-2002, n° 12/01)
 - Principle of non-retroactivity only in the "two Two's"
 - Art. 2 Civil Code: « *la loi ne dispose que pour l'avenir ; elle n'a point d'effet rétroactif* »
 - Art. 2 Criminal Code: « *nulle infraction ne peut être punie de peines qui n'étaient pas portées par la loi avant que l'infraction fût commise* »
 - Principle qualified in the legal doctrine as general principle of law having a legal value → binding on the regulatory power but the legislature may derogate
 - Substance of the principle
 - Conseil d'Etat 13-12-1973 (n° 6328): the applicable tax law is the law in force at time of the taxable event
 - Conseil d'Etat 12-3-1985 (n° 7399): retroactive effect of law only in exceptional circumstances and for special reasons
 - Same position in opinions on draft law bills
 - → non-retroactivity is the normal rule and retroactivity is exceptional
 - Also no provision in the new draft Constitution
 - No case-law of the Constitutional Court

II. Legal retroactivity

- Legal situation in Luxembourg (cont.)
 - First question: do the limits of exceptional circumstances and special reasons impose themselves on the legislature??
 - Second question: if there are limits to the use retroactivity of the law, who is going to control the respect of the limits???
 - Regulations: control + annulment by administrative judge if direct legal action against the regulation; refusal of application by both judicial and administrative judges in case of illegality → art. 95 Constitution
 - But for law:
 - judicial and administrative judges have to apply the law except where it violates superior international law or where the Constitutional Court has decided that it violates a provision of the Constitution
 - Conseil d'Etat: can only refuse waiver of second vote by Parliament
 - So presently no real control of the respect of the principle of non-retroactivity of the law, so two positions are possible:
 - Consider that the principle is untouchable even without control or
 - Never trust a politician with large powers?? → need to fill the gap

II. Legal retroactivity

- Legal situation in Belgium
 - Common constitutional history
 - Same situation as regards formal provisions
 - Same distinction between legal (real) and economic (false) retroactivity; same criterion of the taxable event
 - Traditional analysis:
 - Non-retroactivity is a precept for legislature, an obligation for the judge and a guarantee for the citizen (Cass. 10-1-1924)
 - But Cour d'arbitrage's 5-7-1990 decision:
 - Retroactivity impairs the fundamental principle of legal certainty
 - Retroactivity is admissible if justified by an objective of general interest and if the harm to the principle is not disproportioned
 - Subsequent jurisprudence of the Constitutional Court: retroactivity can only be justified by particular circumstances, linked to an objective of general interest

II. Legal retroactivity

■ Legal situation in Germany

- Country of origin of our direct tax law
- Also no general provision in the Constitution ("*Grundgesetz*")
- Same distinction between legal (real) and economic (false) retroactivity; same criterion of taxable period and taxable event ("*Veranlagungszeitraumrechtsprechung*")
- Constitutional Court 31-5-1960: the rule of law implies the principle of legal certainty which, combined with the individual rights, prohibits in principle retroactivity of legal provisions affecting negatively individual situations; a protected legitimate expectation in maintaining legal consequences of acts and facts completed before the new law enters into force is to be recognized
- In it's constant jurisprudence, the Constitutional Court allows 4 reasons for exceptions to non-retroactivity:
 1. The legal change was foreseeable at the date when the law becomes applicable;
 2. The law was not clear or confusing;
 3. An invalid legal provision created an appearance not allowing legitimate expectation
 4. An overriding reason relating to public interest justifies a retroactive legal provision

II. Legal retroactivity

- Conclusions for those countries
 - In both Belgium and Germany, non-retroactivity is a non written rule
 - In both countries, non-retroactivity is based on the principle of legal certainty and is granted constitutional value
 - In both countries, the Constitutional Courts control the respect of the principle of non-retroactivity of law
 - In a nutshell: non-retroactivity is the rule and retroactivity is the exception – retroactivity is only admissible where legitimate expectation must be questioned or where an overriding reason justifies a proportioned exception
- ... and for Luxembourg
 - Hardly arguable that the rule of law and legal certainty would be no fundamental principles in Luxembourg
 - Non-retroactivity should be qualified as a general principle of constitutional value
 - Precedent exists → principle of separation of powers deduced from the regime of parliamentary democracy (Cour const. 1-10-2010, n° 57/10)
 - Constitutional Court should control the respect of the principle on the basis of the criteria defined by Conseil d'Etat or of criteria it should itself define

III. Economic retroactivity

- In Luxembourg and in Belgium
 - Economic retroactivity does not fall into the scope of the principle of non-retroactivity → full discretion of legislature
 - → Maurice COZIAN: Play first, we'll give you the rules at the end of the game!!
 - But in Germany
 - For long time same analysis
 - In legal doctrine, repeated critics led to a proposal of a single criterion based on the "*Dispositionsschutz*" in periodic taxes: the criterion for retroactivity should not be the taxable event, but the moment at which the taxpayer is to be considered as having made disposals or arrangements which he can no longer cancel for economic or legal reasons
 - On 7-7-2010, the Constitutional Court rendered 3 decisions which maintained the taxable period criterion, but ruled that economic retroactivity is not in principle inadmissible, but that it is subjected to higher requirements of justification as regards legitimate expectation and proportionality when a taxpayer has created a protectable legal position
- Also in France
 - Conseil constitutionnel 29-12-2012: decisions have qualified as retroactive and submitted to a condition of justification by reason of general interest economically retroactive provisions

III. Economic retroactivity

■ Conclusion

■ Potentially 3 different regimes

- Strict distinction between legal and economic retroactivity – limitation for legal retroactivity but discretion of the legislature for economic retroactivity (Belgian way)
- Single criterion based on the criterion of disposals or arrangements by the taxpayer which he can no longer cancel for economic or legal reasons – abandon of distinction between legal and economic retroactivity and application of the same regime for both (alternative German way)
- Distinction between legal and economic retroactivity – stricter limitation for legal retroactivity and lower criteria for economic retroactivity (present German and French way)

- Luxembourg should have at least one and choose one offering effective protection of legal certainty → future case before Cour constitutionnelle??

IV. Retrospectivity

- Is in some way a question about the future of the past
 - The legislature changes a favorable tax regime or a tax treatment granted in the past for the future on the basis of acts, facts or situations created and finalized in the past
 - Especially where the law had provided for special favourable regimes or incentives that create advantages granted over several years
 - Question: can the legislature freely abolish these regimes or incentives before they expire according to the initial rules or does the taxpayer who made disposals or arrangements or carried out a certain transaction to come under the regime or incentive may claim that he must be entitled to the entire benefit of the regime or incentive as a protected right, except where valid reasons of general interest call for their abolition??
 - Analysis:
 - also in this case, the taxpayer is in a situation finalized in the past and he has a legitimate expectation that the tax regime at the time of the act, fact or situation remains in place, especially where the tax regime or incentive was the determining factor;
 - Only particularity: legitimate expectation does not end at the time of finalization but is also projected to the future!!
 - → also here potential for limitation of the discretion of the legislature on the basis of legal certainty!!

V. Conclusion

- This contribution was an analysis of retroactivity on the basis of a legal approach → searching for rules to frame pure discretion
- BUT behind most individual rights there are also economic implications for the taxpayer → protection of legal certainty also protects economic interests over which the economic interest of a State cannot always prevail
 - *"the businesses have the money, the States want the money – the question is who is gonna make it!!"*

THANK YOU FOR YOUR ATTENTION

A high-angle, blurred photograph of a crowd of people walking on a light-colored pavement, creating a sense of motion and a busy public space.

TIMING TAXATION: CONSTITUTIONAL AND ECONOMIC PERSPECTIVES

Werner Haslehner

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IN LAW

The logo of the University of Luxembourg, featuring a stylized 'uni.lu' in red and blue, with the text 'UNIVERSITÉ DU LUXEMBOURG' below it.

UNIVERSITÉ DU
LUXEMBOURG

□ FACULTY OF LAW, ECONOMICS AND FINANCE

- Elements of Timing Taxation
- Constitutional Perspective(s) on Timing Taxation
- Perspectives and Tools of Economics
- Economic Perspectives on Timing Taxation

- Rules of ***substance***
 - defining the taxable base and rate → irrespective of timing
 - e.g. income or consumption
- Rules of ***accounting***
 - defining (timing of) taxable event
 - e.g. accrual or realisation, receipt or expense
- Rules of ***collection***
 - determining when to collect the tax
 - e.g. withholding or via tax return, deferred collection
- Rules of ***transition***
 - Meta-rules to the rules of taxation

Constitutional Perspective(s) on Timing Taxation

- Principle of **Equality**
 - Equal treatment entails taxation on the basis of “**ability to pay**”
 - **Annual vs. life-time** ability to pay
 - **Realization** condition as derivation from ability-to-pay principle
- The Right to **Property** and the **Rule of Law**
 - Interference with private property requires legal basis
 - Retroactive change supplants elected legislature with unauthorized legislative body
- Principle of **Legal Certainty** and **Legitimate Expectations**
 - Legitimate reliance on existing law may require transition relief in case of nominally prospective taxation

- Two competing approaches of law and economics
 - **Utilitarianism** – welfare maximisation under consideration of rational choice: optimal balancing of equity and efficiency
 - **Public choice theory** – conceiving of public institutions as self-interested actors: limiting institutions' power to control outcomes
- Important concepts for economic analysis
 - **Scarce resources** are ideally allocated by supply and demand
 - People (rationally) respond to **incentives** and have **rational expectations**
 - Incentives produce **direct and indirect (second-order) effects**
 - In the real world, practicality constraints may favour **second-best solutions**

- A note on **tax deferral**
 - Distinguish between “**pure deferral**” and “**counter-party deferral**”
(*Halperin & Warren, Tax Law Rev. 2014, 317*)
 - Timing of taxation mainly matters in cases of “**pure deferral**”, which affects the tax base effectively captured by the relevant provisions relative to the normative tax base
 - *E.g. deferring taxation of gains until realisation; interest-free deferral of realised income through roll-over relief*
 - Timing of taxation is largely irrelevant in cases of “**counter-party deferral**” (no effect on comprehensive taxation of the right tax base)
 - *E.g. deferring taxation on pension income under ‘EET’ system*

- Taxation on ***accrual vs realisation*** based taxation
 - Realisation requirement additionally distorts behaviour, grants interest-free “pure deferral” measured against comprehensive income tax
 - Welfarist approach clearly mandates accrual basis taxation
- A ***retrospective tax on capital income***
 - going beyond the accrual/realisation dichotomy (*Auerbach*, Amer. Econ. Rev. 1991, 167; *Kwak*, Corn. J. of Law & Pub. Pol. 2015, 191)
 - Idea: *maintain taxation only on realisation, but eliminate deferral-induced lock-in effect by “effectively charging interest on deferral”* (transforming “pure deferral” into mere “counter-party deferral”)
 - Mechanism: upon realisation, calculate interest on assumed linear gain during holding period

Economics Perspective on Timing Taxation

- The generalised argument for effective retroactive taxation
 - **Idea:** A tax imposed on completed facts does not distort resource allocation as individual decisions are fixed in the past
 - **Mechanism:** E.g. one-time levy on capital
 - **Benefit:** Raising revenue without “deadweight loss” from price distortion
 - **Limits:** Making tax come “out of the blue” without anticipation; credible commitment of non-repetition

- Tax Law Changes and Transition Relief
 - **Traditional view**: transition relief (grandfathering) should be granted to avoid distortionary effect of uncertainty on investment decisions
 - **“New view”**: in the face of (unavoidable) uncertainty of future law, risk should be borne by the party best placed to diversify
 - If changes in law are systematically comparable to factual changes (in the absence of persistent bias), private actors are best placed to absorb risk – through **anticipation, diversification, “insurance”**
 - Limits and objections: adjustment presupposes functioning markets, which are based on reliance in law; systematic biases and limits to insurance; imperfect analogy between factual and legal change
 - A question of fairness (as well as efficiency): ensure symmetry for transition gains and transition losses

- Constitutional and economic perspectives often differ on “timing”
- Yet both are important determinants of good tax policy
- Both perspectives should thus be taken into account
- Constitutional analysis can be enhanced by application of the tools of economic analysis to understand the practical impact of norms governing timing issues in taxation:
 - Deferral does not always affect the tax base
 - Retrospective taxation can solve practical problems of fair capital taxation
 - Nominally retroactive and nominally prospective rules are part of a continuum
 - Nominally retroactive taxation may be desirable (under certain circumstances)