This book aimed to provide an overview of the impact of EU law on Member State corporate tax systems.

In Chapter 1, the inherent limitations in the powers of the EU institutions to enact legislation in the field of direct taxes were discussed. The lack of Union competence in this area and the sensitivity of Member States to any attempts for harmonisation were identified as the main reasons for the scarce legislation. The use of ‘proxy’ legislative bases compounded the situation because for these bases unanimity was required – something very difficult to attain politically.

As a result of this legislative vacuum, it was noted that a number of tax obstacles continue to create serious impediments to the integration of the market. Many of these obstacles arise from the interaction of the taxation systems of Member States, especially when there is a different approach to the integration of shareholder and corporate taxes. This leads to economic double taxation, with taxes imposed on the same income even if the taxes are paid by different persons and affect domestic and foreign shareholders the same way. Obstacles could also arise as a result of juridical double taxation, when the same person is taxed twice by two different States over cross-border income. For some of these obstacles it was argued that the international tax community and the OECD Model do not offer solutions, or not very good ones. Especially as regards economic double taxation, the OECD Model largely defers to Member State discretion. Furthermore, the two relief mechanisms enshrined in the OECD Model – the exemption mechanism and the credit mechanism – do not always eliminate (juridical) double taxation.

As mentioned in Chapter 1 and considered more fully throughout the book, EU law has had an impact on these and a number of other obstacles to cross-border movement, mainly as a result of an expansive interpretation of the non-discrimination principle and the fundamental freedoms. The major point of conflict that has empowered the Union to act is derived from the different stance adopted by the Court of Justice on
the comparability of residents and non-residents for the purposes of the non-discrimination principle. Contrary to established international tax law and the OECD Model, under EU law it cannot be assumed that residents and non-residents are always in a non-comparable situation. When a Member State taxes residents and non-residents differently, then unless it is shown that residents and non-residents are not in a comparable situation, the taxation may be discriminatory. In other words, the starting point is one of comparability. This has led to many developments in EU Corporate Tax Law.

Chapter 1 also considered the historical background to some of the legislative proposals for the removal of tax obstacles in the cross-border movement of companies. In the various studies, reports or proposals initially produced, the suggestions varied from harmonisation of corporate taxes and imposition of a uniform rate on corporate profits (retained and distributed), to the establishment of minimum corporate tax rates and a minimum common tax base. Some studies favoured the classical system, others the split-rate system, others the imputation system with a (refundable) tax credit extended to non-resident shareholders by the host State or by their home State. Proposals for harmonisation were followed by proposals for coordination and ad hoc targeted measures. These led to piecemeal legislative solutions and soft law. Although proposals to put in place a comprehensive system for corporate taxation were never fully explored, there is one notable exception: the proposal for a Common Consolidated Corporate Tax Base, examined in greater detail in Chapter 3.

Chapter 2 examined the few instruments of positive integration that affect Member State corporate tax systems. It was shown that, notwithstanding the limitations of the Union’s power to legislate in the direct tax field, there has been legislation in areas where it was deemed expedient for the proper functioning of the Internal Market. This legislation is, however, very limited and targeted to specific situations. In all of the Directives examined, entitlement to benefits is restricted to companies listed in the Annexes of the Directives and subject to specific taxes also listed. Therefore, the benefits are not readily obtainable. In addition, from a purely practical point of view, the listing approach means that the Annexes have to be regularly updated to include new legal forms and sometimes new types of taxes created in Member States. While this is not the best method of legislative drafting, the Directives provide some (limited) solutions to problems identified in Chapter 1 and in subsequent chapters.
For instance, the Parent–Subsidiary Directive and the Interest and Royalties Directive try to address economic and juridical double taxation. However, their scope is not as extensive as that of the fundamental freedoms. They only deal with intra-group payments of dividends, interest and royalties, under very specific circumstances and subject to anti-abuse provisions. The shareholding requirement for entitlement to the Interest and Royalties Directive is still very high, but it may be lowered in the future and aligned with the shareholding requirement of the Parent–Subsidiary Directive. Overall, due to the prescriptive nature of these Directives, it cannot really be said that they lead to the abolition of source taxation on passive income between all companies. However, notwithstanding the deviations with the corresponding articles of the OECD Model, the similarities suggest that to some extent the Parent–Subsidiary and the Interest and Royalties Directives also provide for the a priori allocation of (some) taxing rights between Member States. Dividends are not taxed at all if tax has already been levied on the underlying corporate profits. Interest and royalties payments are taxed in the home State, with a tax deductibility requirement only relevant to permanent establishments making the payments (for the time being).

Other legislative instruments and their limitations were also briefly discussed in Chapter 2. It was explained that the Savings Directive, which requires automatic exchange of information between Member States on savings of individuals, could easily be circumvented by the interposition of a company and/or the routing of the payment to a third-country paying agent. The Mutual Assistance Directives deal with cross-border recovery of taxes and exchange of information but again under very specific circumstances. Although the scope of the Mutual Assistance Directives has been broadened following recent amendments, automatic exchange of information remains the exception rather than the rule. Finally, the Arbitration Convention was also discussed. It was explained that the aim of this Convention is to eliminate double taxation arising from transfer pricing adjustments and to settle disputes between Member State competent authorities. However, as it is not secondary EU law but a mere treaty, compliance with it cannot be policed by the Court of Justice, nor can disputes be resolved there.

Chapter 3 examined the Commission’s proposal for a CCCTB. This is the most comprehensive piece of European direct tax legislation proposed so far and, if enacted it will be a hugely important development in the EU and internationally. As explained, pursuant to this proposal, companies with establishments in at least two Member States are given
the opportunity to compute their group taxable income according to one set of rules, those of the new consolidated tax base, rather than national tax rules. The basic features of the Draft CCCTB Directive were analysed in Chapter 3. Following the drafting approach of previous Directives, there are strict eligibility requirements in the Draft CCCTB Directive. However, once eligible companies opt to become a CCCTB group, they are automatically subject to consolidation and apportionment according to a basic formula. One of the main benefits of the CCCTB, as advocated by the Commission, is that the administration of it would follow a one-stop shop approach and CCCTB companies would be able to deal with a single tax administration – the principal tax authority.

It was emphasised in Chapter 3 that the new tax base, as set out in the Draft CCCTB Directive, is not compulsory. The CCCTB does not replace national tax bases unless a Member State chooses so. The proposal only provides an alternative method of calculating a CCCTB company’s tax base and of apportioning part of the group’s overall tax base to the appropriate Member State(s). In addition, the CCCTB does not harmonise tax rates. Nevertheless, some Member States are very reluctant to adopt the CCCTB, either for fear that this is a prelude to general harmonisation of corporate taxes in the EU, or that their national tax bases would be seriously depleted as a result of consolidation and apportionment. Some aspects of the apportionment formula – mainly the exclusion of intangibles from the asset factor and sales by destination – are thought to be particularly troublesome to some Member States.

As discussed in Chapter 3, the proposal is likely to be enacted (if at all) through enhanced cooperation. Even though acts adopted within the framework of enhanced cooperation are not part of general European law and do not affect non-participating Member States, nevertheless non-participating Member States are under an obligation not to impede the implementation of these acts. The possible implications of this were considered in Chapter 3, especially in the context of the tax rules on inbound and outbound investment and anti-abuse rules. It was suggested that under enhanced cooperation, the potential obligations of non-participating Member States are not insignificant. Non-CCCTB Member States may lose out on the benefits of the CCCTB while being burdened with an obligation not to impede its implementation. However, nothing could be said with certainty as in the drafting of the CCCTB, the Commission had proceeded on the assumption that all Member States would adopt the CCCTB. This is an understandable position, but it does disservice to the whole project, leaving it with large gaps in the
analysis. The fact that the draft proposal does not factor in the possibility of Member State abstainers makes it very difficult to demarcate the impact of the CCCTB on non-CCCTB Member States, and their rights and obligations as such.

While the decision to adopt the CCCTB is essentially a political one, Member States are likely to reflect on the differences between their systems and the CCCTB, so as to anticipate as much as possible whether staying outside of the CCCTB zone will bring about a competitive disadvantage. It would help if the Commission disclosed its views on what the legal position of non-CCCTB Member States is likely to be, rather than leave it for later, or worse, leave it to the Court of Justice. That way, Member States could make informed decisions as to whether it would be more suitable for them to opt in or opt out of the CCCTB. The absence of this information creates more uncertainty among Member States as to the true ramifications of the CCCTB. It compromises legal certainty and encourages more Member States to just ‘wait and see’ what happens with the ones who join, if any. Comprehensive legislative initiatives such as the CCCTB, if they are to be encouraged, ought to be very precise, leaving no scope (or as little as is possible) for uncertainties and loopholes for participating and non-participating Member States.

Whether or not this important proposal is adopted leading to closer tax integration within the EU remains to be seen. It may be the case that, as in other areas, the principles derived from the Court’s jurisprudence erode Member State tax systems to a much greater extent than the CCCTB – albeit in a much more random and unsystematic way. One cannot ignore or predict the effect of future case law of the Court of Justice on Member State tax systems – that is negative integration.

The impact of negative integration was examined in the remainder of this book. It was shown that most of the developments in the area of EU corporate tax law have been generated through judgments of the Court of Justice. What is truly admirable is that the Court has managed to overcome legislative inertia without formally reversing the important position that the EU lacks competence in direct tax matters. In fact, this is consistently reiterated in the case law, to be immediately qualified by the imposition of a duty on Member States to exercise the powers retained by them in accordance with EU law. As shown in Chapter 4, this duty has been interpreted to encompass compliance with general Treaty provisions such as the non-discrimination principle, the four fundamental freedoms and the state aid prohibition. To an extent, negative integration has helped the EU to (partly) address the legislative vacuum discussed in Chapter 1.
Whether this legislative vacuum has been addressed in a satisfactory way is something questioned throughout the book.

The Court’s general methodology in direct tax cases was considered in Chapter 4. The interpretation of the various fundamental freedoms, the citizenship provision and the state aid prohibition were examined in the context of direct tax law. Chapter 4 identified some trends and ad hoc rules that have developed in the Court’s case law. Although these do not always lead to a consistent and predictable methodology that is followed by the Court, certain patterns appear to be emerging. It was shown that the Court of Justice eschews the simultaneous application of many freedoms, choosing to base its judgments only on the freedom that is predominantly or primarily relevant. This has serious repercussions when the choice is between freedom of establishment and free movement of capital, and a third-country national is involved.

The status of tax treaties and of the OECD Model in the Court’s jurisprudence was also examined. It was made apparent that even though the OECD Model has not been used to interpret or modify EU law, the Court often defers to its provisions to the extent that there is no major conflict with basic principles of EU law or that EU law requires a different approach (e.g. the comparability of residents and non-residents point made above). Tax treaties also play an important role in assessing the actual tax burden on a cross-border activity or investment, when examining the compatibility of a national tax measure with EU law. Although the Court of Justice is generally reluctant to consider the overall situation in which a national measure is applied and often ignores out-of-state benefits or burdens, tax treaties have been interpreted as forming part of the (domestic) legal context in which the measure arises.

The unsatisfactory nature of the litigation process was also discussed in Chapter 4. The arbitrary way in which cases get to the Court of Justice becomes even more apparent in later chapters. So do the difficulties of complying with what the author described as ‘reverse subsidiarity’ – the idea that Member States, in exercising what is effectively their exclusive competence in a given area, have to take into account general principles of European law and, as such, their competence is circumscribed. The concept is revisited later on.

In Chapter 5, the concept of corporate residence and its importance as a connecting factor for tax purposes was discussed. It was shown that while in international tax law this is a key concept for the attainment of certain benefits and the allocation of taxing rights, it is not as important – though not completely obsolete – under EU law, where the emphasis is on
discrimination or restriction. Member States can determine whether a company falls under their tax jurisdiction and agree between themselves (or with a third country) on how to allocate this tax jurisdiction. EU law does not prescribe what connecting factors a Member State ought to have. A company incorporated in the home State cannot demand that the host State considers it tax resident if the host State adopts a different test of tax residence. However, to the extent that a company resident in the home State is in a comparable situation to a company resident in the host State, then any tax benefits conferred by the host State to a resident company may have to be extended to the non-resident (home State) company. Therefore, while the right to prescribe the requirements for a company to be tax resident remains within the discretion of Member States, the right to restrict the benefits attaching to such tax residence may not. Member States can still determine who is tax resident and who is not, but cannot deprive non-residents of benefits if they are in a comparable situation to residents. It was questioned whether, by requiring the extension of benefits to non-residents, this takes away the essence of residence as a connecting factor.

It was shown that the Court has been less willing to tamper with tax treaty residence. The restriction of treaty benefits to residents of contracting States to a tax treaty has not been found to be contrary to EU law. Benefits given to residents of either contracting State are considered an integral part of the tax treaty and cannot be extended to residents of non-contracting States. This is another example where the Court of Justice has chosen not to interfere with tax treaties. Arguably, it is a policy decision. Although a tax treaty benefit is technically different from a benefit conferred unilaterally by a Member State, a non-resident taxpayer denied this benefit is affected in the same way.

Following this analysis, some of the tax obstacles arising in the cross-border movement of companies were examined, the emphasis being firstly on direct investment. It was reiterated that EU law does not impose any immediate obligations on Member States on how to structure their corporate tax systems in terms of rates, taxable base, depreciation and so on. What EU law does is to prevent Member States from imposing rules that hinder a domestic company from carrying on its business in another Member State (home State obstacles), or rules that hinder a non-resident company from carrying on its business in a similar way to domestic companies (host State obstacles). Therefore, national tax rules affecting a single company cannot be subject to scrutiny under EU law, unless there is a cross-border element to these rules that falls within the scope of the fundamental freedoms.
In Chapter 5, the focus was on obstacles arising in the context of corporate groups and in relations between a head office and a branch. As far as the first category was concerned, it was shown that although the OECD Model and, in general, international tax law contained limited or no provisions to remove some of the obstacles discussed, there was extensive case law of the Court of Justice to that effect. The inability of a parent company to deduct expenses in foreign holdings or to absorb losses of a foreign subsidiary where expenses in domestic holdings could be deducted or losses from a domestic subsidiary could be offset against the parent company’s profits were considered. The (more burdensome) taxation of a parent company as a result of controlling a foreign company in a low-tax jurisdiction rather than a resident company was also considered briefly. In most of the cases discussed, especially the earlier ones, the Court of Justice found freedom of establishment and/or the free movement of capital to be compromised and required the removal of the restrictions in situations where international tax law and the OECD Model were silent or deferred to the choices of the contracting States. In recent times, however, the Court’s judgments appear to be more nuanced and place greater weight on justifications such as the allocation of taxing powers between Member States and the prevention of tax avoidance. An overview of the case law on cross-border loss relief provided a good example of this development.

As for the second category of tax obstacles discussed in Chapter 5 – those arising in relations between a head office and a branch – here divergence with established international tax law and the OECD Model was noted. Whilst the norm under international tax law was for a host State to be able to treat permanent establishments differently from resident companies, certain limitations to this approach were identified under EU law. A Member State had discretion on how it defined branches or permanent establishments but not always on how it treated them for taxation purposes. There was no prima facie assumption that a permanent establishment of a non-resident company situated in the host State was not in a comparable situation to a resident company. What can be deduced from the case law is that when it came to a non-resident company claiming equal tax treatment in the host State, the comparability criterion was usually satisfied when the permanent establishment – whether itself or on the basis of profits received – was taxed in a similar way to a resident company. Other regulatory or non-tax differences were not to be taken into account. It was questioned whether this was a satisfactory approach.

In any case, it has become more difficult for Member States to tax permanent establishments (of non-resident companies) in a more burdensome way than resident companies. Rules on the attribution of profits to
permanent establishments may be similarly affected, even though the issue is not as developed in the Court’s jurisprudence and could be perceived as falling under the justification of allocation of taxing powers. It is unlikely that the Court of Justice will interfere with the separate entity approach and the application of the arm’s length principle. Nevertheless, there is nothing stopping the Court from scrutinising rules on expense allocation or on internal dealings that treat an enterprise with a foreign permanent establishment, or that treat cross-border payments within such enterprise, more adversely compared to a domestic enterprise or domestic payments. Such a development would be very drastic and may force the OECD to take a stance on the matter as well.

Chapter 6 focused on the taxation of portfolio investment in the EU, from a home State and a host State perspective. It was reiterated that the international tax community and the OECD Model sought to tackle juridical double taxation but economic double taxation was left to be addressed by Member States. This was reflected in the tax treatment of dividends, interest and royalties under the OECD Model. For example, under the OECD Model contracting States were not required to extend shareholder tax credits to either inbound or outbound dividends, but they could choose to do so anyway. An examination of the Court’s jurisprudence in this area suggests that its approach is not always aligned with the OECD Model’s approach.

For inbound dividends, the general principle is that shareholders (corporate or non-corporate) receiving foreign-sourced dividends should be treated the same way as shareholders receiving domestic dividends if they are in an objectively comparable situation, unless different treatment is justified. If the country of residence of the shareholder (the home State) chooses to provide reliefs for domestic dividends, then it must provide the same reliefs at least for EU-sourced dividends. The fact that economic double taxation is suffered because another State has imposed corporation tax on the underlying profits generating the dividends is not a relevant consideration. It is sufficient that economic double taxation has, in fact, been suffered by shareholders, whether they receive domestic or foreign-sourced dividends. However, it would seem from the Court’s case law that not all types of reliefs have to be extended in this way – only reliefs for economic double taxation. It has been found that a home State is not obliged to give to shareholders a credit for foreign withholding taxes, irrespective of whether it gives such credit for domestic withholding taxes. Juridical double taxation in this context is considered to be the result of the parallel exercise of taxing powers by Member States and, as such, is outside the ambit of EU law.
Case law on the taxation of outbound dividends starts from a similar premise to that on inbound dividends, but there are some subtle differences. The host State has to ensure equal tax treatment of resident and non-resident recipients of dividends, if they are in a comparable situation. From a host State perspective, resident and non-resident shareholders are in a comparable situation if they are both subject to host State taxes. In other words, a tax imposed by the host State only on outbound dividends, or a relief from economic double taxation only available to resident shareholders, could be discriminatory if the non-resident shareholder is also subject to tax on those dividends in the host State. As far as relief from juridical double taxation is concerned, contrary to the case law on inbound dividends, it has been held that when the host State gives a tax credit for withholding taxes on income paid to residents, then it has to extend this credit to non-residents. It is difficult to understand why the host State is required to prevent juridical double taxation on outbound dividends but the home State is not required to do so on inbound dividends. It was argued in Chapter 6 that case law on inbound and outbound dividends is not coherent on this point and the obligations of the home State and the host State are not symmetrical.

Overall, as far as dividends are concerned, whilst conferring relief for the underlying tax is not required under the OECD Model nor is it always the norm, EU law places emphasis on it, to the extent that such relief is offered domestically. What should be emphasised is that the Court targets selective relief for economic double taxation and does not show preference for either the exemption method or the credit method. In fact, the Court of Justice appears to treat these two methods as equivalent. The issue was raised in the Court’s case law on inbound dividends, where it was found that the use of both methods – exemption for domestic dividends and taxation with credit for inbound dividends – did not lead to discrimination. It was questioned in Chapter 6 whether the exemption method and the credit method are truly equivalent. The difference between the two methods becomes obvious when host State taxes exceed home State taxes and the home State only gives an ordinary credit. In this case the application of the credit method leads to unrelieved double taxation. There is no such unrelieved taxation when the exemption method applies as there is only a single layer of taxation. Even in situations where host State taxation does not exceed home State taxation, the administrative burden for complying with the credit method – an intrinsic part of its operation as accepted in recent cases – may be onerous. Although the Court has stated that administrative burdens imposed on recipient companies in order to
qualify for a credit must not be excessive, it appears reluctant to interfere with Member State evidentiary requirements, whatever their level of complexity. This is irrespective of the fact that the credit method neutralises the advantage from investing in another Member State – an Internal Market objective that perhaps ought to have been furthered rather than allowed to be curbed.

As a consequence of this approach, the Court does not appear to favour either the classical system of corporate taxation or the imputation system – the latter being inextricably linked to imputation credits. Nevertheless, the difficulty of matching imputation credits with the foreign tax burden on a distributing company has rendered imputation systems very unattractive. It is no surprise that such systems have been repealed in most Member States. This is a good example of how market forces have remedied certain defects, or rather politically (self-) imposed limitations, in the Court’s reasoning.

One question that arose in Chapter 6 was whether the dividends case law could also apply to interest or royalty payments. It was argued that there was no prima facie reason why it should not. The focus of that case law was on the different tax treatment of domestic and foreign-sourced dividends causing discrimination. The same analysis ought to apply vis-à-vis interest and royalties, unless a different treatment was justified. Therefore, where for whatever reasons economic double taxation arose on cross-border payments of interest and royalties, the case law on dividends should apply by analogy. The same was suggested as far as juridical double taxation was concerned, notwithstanding the inconsistencies of the dividends case law discussed above. Here an analogy was drawn with the tax treatment of outbound payments arising from non-portfolio holdings, where the Parent–Subsidiary and the Interest and Royalties Directives showed a clear convergence of approach in exempting these payments. This suggested that the shared aim of the Directives was the elimination of host State taxation on intra-group profit distributions and payments of interest and royalties in non-portfolio situations. It is hoped that the Court will show a similar convergence of approach in portfolio situations, unless there is something inherent in the nature of the arrangement for the interest or royalty payment to be treated differently.

Aspects of corporate reorganisations were considered in Chapter 7. It was shown that although cross-border reorganisations such as mergers, divisions and exchange of shares promote the Internal Market, many tax obstacles often exist. Unrealised capital gains and fiscal reserves may be taxed and previous year losses may not be carried over to the newly created
or reorganised entity, especially if these are foreign losses. Financing costs may become non-deductible and thin capitalisation provisions could be triggered. These issues may increase the costs of the reorganisation, having an impact not only on the companies involved but also their shareholders. EU law provides targeted solutions to some of these problems but with many limitations.

The Merger Directive provides for tax deferral on qualifying assets and stock but only for specific types of transactions strictly defined, involving companies from two or more Member States and of a legal form set out in the Annex to the Directive. Contrary to the Parent–Subsidiary and the Interest and Royalties Directives, permanent establishments of transferring or acquiring companies do not enjoy any protection under the Merger Directive, which covers only merging companies or transfers of assets between companies. The Merger Directive is additionally restrictive as it only allows this tax deferral when there is a remaining permanent establishment of the acquiring company to take over the assets and liabilities of the transferring company. This is to ensure that upon future realisation of the deferred capital gains, these will form part of the tax base allocated to the Member State of the transferring company. Furthermore, the Merger Directive does not contain rules on the valuation of shares. This, combined with the fact that gains arising out of the subsequent transfer of shares may be taxed by the Member States, could lead to double taxation if the host State does not give a step-up; an issue also relevant in the exit tax case law.

As shown in Chapter 7, much of the case law on the Merger Directive centred on its anti-abuse provision. Generally in these cases, the Court looked at whether tax considerations were predominant. If not, then a valid commercial reason could be established for the purposes of the anti-abuse provision. In determining whether a particular operation had the principal objective of tax evasion or tax avoidance, the domestic authorities could not confine themselves to applying pre-determined general criteria but rather had to subject each particular case to a general examination, open to judicial review. Mergers by acquisition of a company holding tax losses could have valid commercial reasons, though the amount of the losses may be indicative of tax evasion. The concepts of restructuring and rationalisation must involve more than the attainment of a purely fiscal advantage but not necessarily more than the reduction of administrative and management costs. In recent cases the Court has even toyed with the idea that the Merger Directive’s anti-abuse provision
reflects the general principle of EU law that abuse of rights is prohibited, a topic discussed further in Chapter 8.

Despite the limitations of the Merger Directive, freedom of establishment has been used to ensure that a wider range of reorganisation operations are protected. Chapter 7 examined situations where a company migrates to another jurisdiction by transferring its seat. It was shown that this is not always a straightforward matter, neither from a corporate law nor from a tax law perspective, as certain rules create obstacles to cross-border corporate migration, or prevent it altogether.

From a corporate law perspective, the interplay of the incorporation and real seat theories constrain the ability of companies to migrate. From an outbound/emigration perspective, the company may not be allowed to transfer its registered and/or administrative seat without having to wind up and dissolve first. From an inbound/immigration perspective, the company may not be recognised in the host State as a foreign company, losing the protection of the limited liability status. In addition, the company may have to reincorporate in the host State or have to adjust part or its entire internal law. So far in cases dealing with corporate emigration, the Court of Justice appears to defer to national rules and is reluctant to interfere with restrictions imposed by the home State. By contrast, in cases dealing with corporate immigration, the Court is less permissive. Obstacles imposed by the host State (e.g. the non-recognition of the foreign company, imposition of additional compliance requirements, lack of legal standing, etc.) were found to be incompatible with freedom of establishment. It was immaterial that the migrating company had been formed in the home State only for the purposes of establishing itself in the host State, where its main, or indeed entire, business would be conducted.

While the Court of Justice seems more willing to demand national treatment in the case of immigration rather than emigration for corporate law purposes, up until recently it was not certain whether the same could be said as regards tax restrictions to a company’s ability to migrate. It had long been argued that in the EU, corporate exit taxes are restrictive measures as they hinder a person’s ability to move to another Member State. As exit taxes only apply to a person moving their tax residence abroad, they may constitute an obstacle to free movement. Furthermore, the imposition of exit taxes could lead to double taxation, as gains would be taxed twice both by the home State and the host State, if the latter does not provide for a step-up. Where there is a transfer of assets, double
taxation (and double non-taxation) could be the result of mismatches in valuation methods.

Initially, the Court of Justice had only dealt with cases challenging exit taxes imposed on individuals. This case law was briefly reviewed in Chapter 7. It was shown that the Court considered exit taxes as a restriction to the cross-border movement of individuals. The obligation to make a tax declaration at the time of transfer and the obligation to give a guarantee for tax deferral to be allowed were also considered restrictive measures. Exit taxes could be justified on the basis of a number of grounds, such as the preservation of the allocation of taxing powers between Member States and the prevention of tax avoidance or evasion. The restriction also had to be proportional. A tax declaration at the time of transfer, setting out the accrued income but without giving rise to immediate taxation was proportional, but the demand for guarantees was not. Any home State exit tax mechanism also had to take into account reductions in value arising after the transfer of residence, unless such reductions had already been taken into account in the host State.

Although it was thought that the same principles applied as regards exit taxes affecting companies, following recent case law there appear to be some deviations. The Court has found that the immediate taxation of unrealised capital gains relating to assets transferred when a company moved its place of effective management to another Member State restricted the company’s freedom of establishment. What is important is the Court’s statement that Member States have to give companies the option of choosing between immediate payment of the exit tax, or deferred payment with all its administrative difficulties, including (possibly) the payment of interest and the provision of a bank guarantee. This option would only be available when the nature and extent of the company’s assets made it easy to carry out a cross-border tracing of the assets subject to the exit tax. Contrary to the case law on individuals, decreases in value are not to be taken into account for the establishment of the exit tax, even in cases where payment of it is deferred. A possible omission by the host State to take account of decreases in value does not create an obligation on the home State to do so. The payment of interest and the provision of a bank guarantee are not prohibited either.

Recent cases seem to tacitly approve the right of the home State not to take into account decreases in value and to request interest for the deferred payment, as well as guarantees. This development was criticised for making the emigration of companies more cumbersome and costly than the emigration of individuals. It was argued that if this is
indeed intentional, it would have to be a quasi-political decision as the EU legal framework does not make it more difficult for governments to collect taxes from emigrating companies than emigrating individuals. It was also noted that in both the case law on emigrating individuals and that on emigrating companies the host State tax rules are irrelevant in assessing the compatibility of the home State rules. Not only that, but the Court refuses to recognise an obligation on the host State to provide a step-up or a tax credit that takes into account home State taxes. It is the home State’s obligation to comply with the principles of the Court’s case law even if the cumulative application of the home State and host State tax rules leads to double taxation or double non-taxation. Notwithstanding this criticism, it was argued that the principles derived from the Court’s judgments on exit taxes could address some of the limitations of the Merger Directive discussed earlier in Chapter 7 and could help remove the (many) remaining tax obstacles that are encountered in cross-border reorganisations.

The concept of tax avoidance was considered in Chapter 8. It was questioned whether there was a general principle of abuse of tax rights for the purposes of EU law. It was shown that in harmonised and quasi-harmonised areas, the Court of Justice had more readily accepted a general principle of abuse of rights. VAT cases and cases on the Merger Directive were discussed to illustrate the point. Recent case law was also discussed to show that the Court has indeed confirmed the fact that EU law does not provide a general principle of abuse of rights in the field of direct taxation, as this is a non-harmonised area. Therefore, within the EU taxpayers are still entitled to structure their affairs in such a way as to limit their tax liability, but Member States are also entitled to put measures in place to prevent certain types of arrangements that they consider abusive. However, a finding of abuse of tax laws or tax avoidance could be relevant as far as the compatibility of national tax legislation was concerned, being a potential justification to measures restricting fundamental freedoms.

This chapter also examined various types of specific anti-abuse regimes and their compatibility with EU law. An attempt was made to assess the Court’s judgments in this area and to consider whether the principles derived have created a uniform body of law. Cases on controlled foreign companies, thin capitalisation and transfer pricing were considered.

It was argued that from an EU perspective, CFC rules penalise the parent company for investing in foreign low-tax jurisdictions, contrary to freedom of establishment. This was also the stance taken by the Court of
Justice in the case law. There it was clarified that just because an advantage results from low taxation in the Member State of the subsidiary, this does not mean that the Member State of the parent company could offset that advantage by imposing less favourable tax treatment on the parent company. The need to prevent the reduction of tax revenue was also not an acceptable justification. However, prevention of tax avoidance and evasion could be a relevant justification if the restrictive measure specifically relates to wholly artificial arrangements that do not reflect economic reality. The mere fact that a resident company establishes a secondary establishment such as a subsidiary in another Member State does not justify a general presumption of tax evasion.

In addition, CFC rules have to be proportional. When the incorporation of a CFC reflects economic reality, such a structure cannot be attacked, notwithstanding the existence of tax motives. In determining whether or not economic reality exists, the intention to obtain a tax advantage (a subjective test) has to be taken into account in addition to objective factors, such as the physical existence of the CFC in terms of premises, staff and equipment. However, the fact that the CFC’s activities could just as well have been carried out by a resident company could not lead to a conclusion that this is a wholly artificial arrangement. Furthermore, the parent company has to be given an opportunity to produce evidence that the arrangement is genuine. In fact, it is the parent company that is best placed to establish that it has not entered into wholly artificial arrangements. Compliance requirements are not, therefore, prohibited, as long as their aim is to verify without undue administrative constraints that the CFC is actually established and that its activities are genuine.

The principles set out above were not initially thought of as being restricted to CFC cases. Indeed, the wholly artificial arrangements test has been, in theory, followed in thin capitalisation and transfer pricing cases but with some important nuances in the interpretation of the proportionality requirement. Again, in these cases there is a consideration of objective and verifiable elements that could be used to determine whether a transaction represents a purely artificial arrangement. Emphasis is placed on the commerciality of the arrangement. The affected taxpayer has to be given the opportunity, without being subject to undue administrative constraints, to provide evidence of any commercial justification that there may have been for the impugned arrangement. The corrective mechanism also has to be limited to the part that exceeds what would have been agreed had the relationship between the relevant companies been at arm’s length.
The unclear relationship between the Court’s commercial justification test in these cases and the OECD’s arm’s length principle has now become a crucial issue as far as the compatibility of thin capitalisation and transfer pricing rules with EU law is concerned. From an international tax law perspective, these concepts cannot be equated as there are inherent differences – commercial justification connoting a subjective standard, not necessarily aligned with the OECD’s more objective arm’s length test. It was questioned whether the existence of a commercial justification could enable taxpayers to escape thin capitalisation and transfer pricing rules even when the arrangement was not arm’s length. It seemed that the existence of an arm’s length relationship would be one of the factors to be taken into account in determining whether the transaction represented, in whole or in part, a purely artificial arrangement, the essential purpose of which was to circumvent the tax legislation of a Member State. It was argued that to prevent a conflict between EU law and international tax law on this point Member States should be allowed to apply their thin capitalisation and transfer pricing rules to a non-arm’s length arrangement, notwithstanding the arrangement’s otherwise commercial nature. This may mean that the wholly artificial arrangements test is eventually restricted to CFC regimes.

It is obvious from the above brief summary of each chapter that the developments as a result of the case law far outweigh the advances of legislation. It is tempting to read the Court’s judgments as serving a harmonisation campaign – something the Court is often accused of by Eurosceptics. However, a closer examination of the judgments, as set out in this book, suggests that the Court is not really trying to legislate but rather responds to specific questions posed by national courts or the Commission in the limited legal framework provided. The questions tend to be centred on whether a Member State in exercising its exclusive powers to regulate its tax system is effectively constrained by general provisions of EU law. In other words, the Court is asked to police the application of reverse subsidiarity by Member States. The author has argued that the ability of a Member State to apply reverse subsidiarity depends on the following factors: the clarity and consistency of the Court’s judgments in a given area, the ability of national courts to adopt and interpret the Court’s jurisprudence and the willingness of national legislatures to comply with this jurisprudence. This book, being a general study on EU corporate tax law without a specific jurisdiction focus, mainly deals with the first part of the test and assesses the precedential value of the Court’s judgments.
As regards the choice of cases that end up in the Court of Justice, it was shown that there was an element of arbitrariness and randomness, inherent in a judicial process with multiple actors – the Commission, Member States, affected taxpayers and national courts. The limitations of the judicial process became more apparent upon closer examination of some judgments of the Court of Justice – if and when cases found their way to that forum. Certainly, the flexible use of the notion of precedent has enabled the Court to create pockets of case law that deal with specific themes, generating important developments in many areas where previous legislative attempts stagnated or were largely non-existent. Especially in early cases, the Court was more willing to break tradition with established principles of international tax law in order to protect the exercise of fundamental freedoms by EU nationals. This approach usually reached a high-water mark in certain cases, with the Court of Justice becoming more attuned to the possible repercussions from a clash with international tax law. Thereafter, the Court would place more emphasis on justifications, or on proportionality, or would give very broad guidelines and leave the question for the national courts to decide.

It is not surprising, therefore, that the flexible use of precedent has sometimes led to fragmented principles and inconsistent results arising in analogous situations. Nor is it surprising that the Court of Justice often deviated from earlier judgments without any explanation. In some cases the Court took a stance that was at odds with entrenched – and often fundamental – positions in international tax law, while in other cases, usually later ones, the Court validated those entrenched positions or similar ones without challenging their compatibility with EU law. The discussion on the treatment of juridical double taxation in the context of inbound and outbound dividends and the equivalence of the exemption method and the credit method are good examples of this, sometimes confused and confusing, approach.

This often raises concerns as to the calibre of the Court’s reasoning and the appropriateness of negative integration. It is undeniable, however, that a body of what can today be called EU corporate tax law has developed mainly as a result of negative integration. While this body of law may not always be sufficiently coherent and predictable so as to be easily followed – by national courts, legislatures and taxpayers (or their advisers) – the existence of it cannot be denied. As a result, it seems that reverse subsidiarity is bound to be applied in a variable way, depending on the area of tax law in question and sometimes the Member State involved. Some topics examined, especially those developed single-handedly by the
Court of Justice without an underlying Directive in the background (e.g. the case law on CFCs, or thin capitalisation rules, or exit taxes, or group relief) have not reached the level of maturity to be unequivocally transposed to Member State legal systems. Neither is the level of understanding of EU corporate tax law by some national courts and legislatures such as to ensure an accurate and effective implementation of it. For reverse subsidiarity to function properly, the part of EU law under question has to be sufficiently clear and Member States’ judicial, legislative and executive bodies must have a good understanding of it. Most importantly, these bodies must share the same enthusiasm (or at least willingness) to implement it. Therefore, overreliance on judicial means does not guarantee equality between Member States. Nor does it guarantee the removal of tax obstacles to the cross-border movement of companies.

It has been questioned many times in this book whether the current situation brings satisfactory results or whether in some cases, notwithstanding Member States’ exclusive competence, conceding to the European Union the power to enact direct tax legislation (or some aspects of it) may ensure a more harmonious coexistence of European law and national legal systems. It is submitted that the limitations of the European judicial process in removing the many remaining tax obstacles to cross-border movement can be better addressed through legislation – be it comprehensive or targeted. Instead of pre-emptively rejecting any proposals for reform and further integration such as the CCCTB, it may be worth considering first whether the European tax community is heading towards that direction, or a similar direction anyway.

The author has tried to show in this book that the European tax community does indeed appear to be moving towards closer integration, but not always in a systematic or coherent way due to the vagaries of the judicial process. The Court of Justice is increasingly being asked to decide complex tax questions, on issues which the OECD Model itself refrains to take a stance and defers to the discretion of Member States. There are also questions that require a bilateral or multilateral approach – that is an overall approach rather than a per-country approach – to ensure a fairer outcome. In dealing with such issues, the Court is between Scylla and Charybdis: it will either be accused of inappropriate lawmaking or elusive and evasive decision-making.

It is hoped that soon the role of the Union’s institutions in the development of tax policy will be reinvigorated and reassessed, diminishing the need to resort to such intrusive judicial activism. Whatever happens, the Court has proved a good ally for taxpayers wishing to benefit fully
from EU law. It has certainly changed the legal landscape for companies engaging in cross-border activities. Although the nature of the European litigation process has given EU corporate tax law a peripatetic flavour, the Court’s commitment to an Internal Market without obstacles – any obstacles, including tax obstacles – cannot be disputed. Whatever conclusions are reached in this book, they can only be interim conclusions. More developments are likely to follow.