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Belgium – CJEU rules deduction of alimony payments for non-residents contrary to the freedom of movement for workers

In a Judgment of 10 March 2022, the CJEU decided that Belgium's deduction of alimony payments for non-residents is contrary to the freedom of movement for workers (*C-60/21*, *Commission v Belgium*).

According to current Belgian legislation, alimony payments cannot be deducted from the taxable income of non-resident taxpayers who earn less than 75% of their worldwide income in Belgium. Belgium refuses the deduction if the 75% condition is not met, even when the taxpayer has no significant taxable income in their State of residence, which makes it impossible to deduct alimony payments from taxable income in this State. Because of this refusal, the alimony payments are deducted neither from their taxable income in their State of residence nor in Belgium (State of employment). The CJEU is of the opinion that there is an infringement of the freedom of movement for workers, as the 75% condition - which is only applicable to non-resident taxpayers - is of a general nature and does not allow that the personal and family situation of the non-resident is taken into consideration. This discrimination between Belgian and non-resident taxpayers cannot be justified by the fact that the concerned situation would, according to the European Commission, be purely theoretical.

As a result of this CJEU Judgment, Belgium will have to bring its legislation in line with EU law.

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Belgium – AG Opinion on the DAC6 obligation for lawyers to provide information regarding potentially aggressive cross-border arrangements to other intermediaries

Council Directive (EU) 2018/822 of 25 May 2018 (commonly referred to as DAC6), providing for a mandatory exchange of information in the field of taxation in relation to reportable potentially aggressive cross-border arrangements, was implemented in Belgium in the federal tax code as well as in tax legislation in the Flemish Region, Brussels Region and Walloon Region (given that e.g., immovable withholding tax is a regional tax matter).

The federal as well as the regional DAC6 implementation provides for a derogation on the reporting obligation for intermediaries that are bound by a legal professional privilege. The holder of the legal professional privilege who wishes to invoke their legal privilege in this context is required to notify in writing the other intermediary(ies) involved in the implementation of such arrangements, if any, that the holder cannot fulfill their reporting obligation. The reporting obligation then shifts to the other intermediary(ies) who may in turn invoke their legal privilege. In absence of another intermediary, the taxpayer must be notified in writing of their reporting obligation.

Under Belgian legislation, lawyers that are members of the bar as well as tax consultants that are members of the Institute of Tax Advisors and Accountants (ITAA), are bound by legal professional privilege. In the case at hand, the Flemish Region DAC6 regime, and more specifically the legal privilege derogation, was challenged by the Belgian Association of Tax Lawyers (supported by ITAA), and the suspension and annulment of the Flemish Region DAC6 regime (Decree of 26 June 2020) was claimed before the Constitutional Court.

The plaintiffs notably pointed out that it is impossible to fulfill the above-mentioned reporting obligation without breaching professional secrecy. Moreover, according to them, such an obligation is not necessary to ensure that the potentially aggressive cross-border arrangements are reported, since the client, whether assisted by the lawyer or not, can inform the other intermediaries and ask them to fulfill their reporting obligation. The plaintiffs consider in the case at hand that the reporting obligation infringes the right to respect for private life (guaranteed by Article 7 of the Charter of Fundamental Rights of the European Union (the Charter) and Article 8 of the European Convention on Human Rights) and the right to a fair trial (guaranteed by Article 47 of the Charter).

The Constitutional Court decided to refer the case to the CJEU for a preliminary ruling (case *C-694/20*).

In this context, on 5 April 2022, AG Rantos delivered his Opinion. In a nutshell, after a thorough analysis, he concluded first that the right to a fair trial was not infringed as the reporting obligation by the lawyers to the other intermediary(ies) is not meant to be part of a judicial procedure. Regarding the question as to whether the reporting obligation to the other intermediary(ies) could infringe the right to respect for private life, which includes professional secrecy, the AG concluded that it cannot be ruled out, but that the infringement would be duly justified in order to protect States from tax base erosion. Moreover, according to the AG, an infringement in relation to professional secrecy would be proportionate because:

- the reporting obligation would only be applicable when the lawyer is aware and informed that (an)other intermediary(ies) is (are) involved; and
- the infringement in relation to professional secrecy would be very limited because the information to be provided by the lawyer to the other intermediary(ies) is not as such sensitive information, but only general information, probably already known by the other intermediary(ies).

However, the AG considered that the disclosure of the name of the lawyer to the tax authorities by the reporting intermediary(ies) infringes the right to respect for private life and is not justified and proportionate.

If the CJEU's Judgment were to be in line with the AG's Opinion, this would mean that the Flemish DAC6 regime should be amended (and in practice also the federal and the other regional regimes in Belgium), but only in order not to disclose the lawyers' name to the tax authorities. The AG's interpretation seems questionable as it reflects a very restrictive interpretation of the concept of legal professional privilege and does not take into account the tradition of legal secrecy in Belgium and in many other countries.

The question now is whether the CJEU will confirm this restrictive interpretation of the concept of professional secrecy for lawyers.

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Belgium – AG Opinion on the transfer of dividend received deduction carried forward following a tax-neutral merger

On 28 April 2022, AG Rantos delivered his AG's Opinion on the tax treatment of dividend received deduction (DRD) carried forward in the case of a tax-neutral merger (*C-295/21*, *Allianz Benelux*), concluding that there is no violation of Article 4(1) of the EU's Parent-Subsidiary Directive (PSD).

In Belgium, Article 4(1) of the PSD is implemented via the DRD regime, which provides that a received dividend is first included in the taxable base of the company. Through the DRD the company can deduct 95% (currently 100%) of the dividend from this base ("inclusion-deduction method"), but only to the extent that taxable profits remain. Following the CJEU's *Cobelfret* Judgment (*C-138/07*), the Belgian legislation was amended to allow excess DRD to be carried forward to future taxable periods.

In the present case, a Belgian insurance company (AGF L'Escaut SA) had absorbed two Belgian insurance companies in 1995. Upon a second merger in 1999, AGF L'Escaut SA and five other insurance companies were absorbed by a separate Belgian insurance company (Assubel-Vie SA). The absorbed companies had DRD carried forward that, upon the tax-neutral mergers, was entirely transferred to the absorbing company. At the time of the events, in the case of a tax-neutral merger, there was no provision in Belgian law governing the transfer to an absorbing company of the DRD carried forward of an absorbed company. However, for carried forward tax losses, a specific rule provides that upon a tax-neutral merger a proportion of the carried forward tax losses of an absorbed company can be transferred to the absorbing company, in particular, in proportion to the share of the net tax assets of the merging companies. Although this "pro rata rule" for carried forward tax losses was extended to DRD carried forward at the end of 2017 and was even before that date already applied to DRD carried forward by the Belgian Rulings Office, at the time of the facts of this case such "pro rata rule" did not yet exist for DRD carried forward. Nevertheless, the Belgian tax authorities and the Belgian Court of First Instance accepted the transfer of the DRD carried forward to the absorbing company to the extent of the "pro rata rule" provided for carried forward tax losses, rejecting the full transfer of DRD carried forward as applied by the taxpayer.

Based on the following arguments, the AG recommends the CJEU to conclude that Article 4(1) of the PSD has not been violated:

- First, the AG notes that the previous CJEU case law stating the Belgian DRD regime was not in line with the PSD, in particular the *Cobelfret* case, the *KBC* case (*C-439/07* and *C-499/07*) and the *Brussels Securities* case (*C-389/18*), was rendered in a different factual and legal context. Indeed, the present case does not concern a transfer of DRD carried forward between companies belonging to the same group, but a transfer of DRD carried forward from a previously independent company to another company following a merger. Therefore, this case law cannot be transposed to the present case.
- No provision of EU law, including the PSD and the Merger Directive 90/434, seems to recognise the right to an unconditional transfer of DRD carried forward from the absorbed company to the absorbing company, as claimed by the taxpayer.
- When applying the reasoning of the CJEU in the *Brussels Securities* case, it appears that the tax neutrality between the current "inclusion-deduction method" and a pure exemption method is respected. If the DRD carried forward is transferred in full to the absorbing company, while a pro rata limitation applies to the transfer of carried forward tax losses, the absorbing company would be in a more favourable situation than if the Belgian State had provided for a simple exemption of the dividend. Neither the referring Court, nor the taxpayer has been able to provide an example that would illustrate indirect taxation of exempt dividends pursuant to Article 4(1) of the PSD.
- Even if the question of a justification does not arise, the limited transfer of DRD carried forward based on the "pro rata rule" in the context of a merger can, at first sight, be justified in the light of the legitimate objective of combating abuse and tax evasion, provided, of course, that the measure is necessary and respects the principle of proportionality.

This case may be relevant for companies with DRD carried forward involved in a tax-free restructuring. The answer of the CJEU, should it not follow the AG's Opinion, could also have an impact on the existing "pro rata rule" that was introduced for DRD carried forward at the end of 2017.

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Finland – CJEU rules Finnish tax treatment of a French real estate investment fund incompatible with EU law

On 7 April 2022, the CJEU issued its Judgment in C-342/20, *A SCPI v Veronsaajien oikeudenvalvontayksikkö*. The Finnish tax treatment of a non-Finnish corporate fund was found to be discriminatory and contrary to the free movement of capital and the discriminatory tax treatment could not be justified by any overriding reasons in the public interest.

The Finnish Tax Authority (FTA) issued an advance ruling in which it stated that a *société civile de placement immobilier à capital variable* ("SCPI"), a corporate fund with variable capital, was objectively comparable to a Finnish tax-exempt real estate investment fund and therefore exempt from Finnish income tax for tax year 2019, *but not for tax year 2020* due to the new tax rules (Income Tax Act ("ITA") §20a) introduced and applicable as of 1 January 2020. The new ITA §20a requires both Finnish and foreign investment funds, such as the SCPI, to be contractual in nature in order to qualify for tax-exempt status. The SCPI failed to meet this criterion, as it is established as a corporate fund. The SCPI appealed the decision to the Administrative Court of Helsinki insofar as the ruling concerned tax year 2020.

Finnish tax-exempt investment funds, including real estate investment funds, can only be established as contractual funds. Other types of investment vehicles may be established under Finnish law, but such vehicles do not benefit from a similar categorical income tax exemption.

The Administrative Court stayed the proceedings and requested the CJEU to issue a preliminary ruling on whether Finland is allowed to exclude foreign investment funds from the scope of the investment fund tax exemption simply as a result of them being non-contractual in nature.

The CJEU first determined that, as a matter concerning income from real estate investments without any intention to undertake business activities in Finland, the question of the preliminary ruling would be analysed only with respect to the free movement of capital.

The criterion which requires investment funds to be contractual in nature to qualify for the tax exemption applies equally to Finnish and foreign investment funds. Accordingly, it does not, as a starting point, place Finnish investment funds in a more advantageous position compared to foreign investment funds. Still, the CJEU considered that, as the criterion is by its nature likely to result in Finnish investment funds fulfilling the criterion and foreign investment funds potentially failing to fulfil the criterion, the requirement for the investment fund to be of a contractual nature constituted a restriction to the free movement of capital.

Next, the CJEU examined if the French SCPI's situation was objectively comparable to the situation of a Finnish tax-exempt real estate investment fund. The CJEU referred to its preceeding case law regarding the comparability of cross-border situations and reiterated that the comparability of a cross-border situation with a purely domestic situation must be analysed with regard to the aim pursued by the national provisions at issue as well as to the purpose and content of those provisions, here ITA §20a. The CJEU found that the objective and purpose of the tax exemption under ITA §20a was to avoid the double taxation of income from investments and to endeavour to treat indirect investments made through funds similarly to direct investments for tax purposes. From this perspective, the relevance in tax treatment is the level at which taxation (if any) takes place. Finnish investment funds investing in real estate that are tax exempt under ITA §20a are not subject to tax at the level of the fund, unlike Finnish corporate entities investing in real estate.

However, in a cross-border situation, the objective of ensuring taxation only at the level of the investors, and not the fund, may be achieved where an investment fund has been established as a corporate fund but benefits, in its country of residence, from an exemption from income tax *or* from a system of tax transparency. Accordingly, in this regard the French SCPI, which is a fiscally transparent corporate entity, was considered to be objectively comparable to a Finnish tax-exempt real estate investment fund, which is a contractual fund. The CJEU found no overriding reasons in the public interest that could justify the restriction of the free movement of capital.

The requirement of being contractual in nature is only one of the basic criteria that need to be met in order to obtain tax-exempt investment fund status in Finland. However, according to our experience, this criterion has typically been the most critical.

The CJEU Judgment is of fundamental importance for all non-contractual funds investing in the Finnish market. The new rule ITA §20a, applicable as of 1 January 2020, which introduced the general requirement for an investment fund to be of contractual nature for the tax exemption and which resulted in the preliminary ruling to be requested by the Finnish court, has resulted in much ambiguity in the Finnish market in relation to the Finnish tax treatment of foreign non-contractual funds. The prevailing interpretation by the FTA for fiscal years 2020 and thereafter has been that the tax exemption in question may only be granted to contractual funds in line with the wording of ITA §20a. This interpretation can no longer stand as a result of this CJEU Judgment.

While the decision by the CJEU specifically concerns real estate income, it will likely become critical also for cases concerning the Finnish tax treatment of other types of Finnish source income, e.g. dividends. Additionally, the reasoning of the CJEU should also extend to opaque but tax-exempt funds. Therefore, our expectation is that the applicability of the judgment will not be limited to foreign tax transparent funds; it should also benefit corporate funds, such as Luxembourg SICAVs established as an SA, and trusts which are either tax transparent or tax exempt.

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Germany – AG Opinion on the deduction of final losses incurred by a German company in its permanent establishment in the UK

On 10 March 2022, AG Collins opined in the CJEU case *C-538/20* (*W AG*) that Germany does not infringe the freedom of establishment by not allowing the deduction of final losses which a German company had incurred in its permanent establishment (PE) situated in the UK.

The plaintiff is a German securities bank which owned a loss-making PE in the UK from August 2004 until February 2007. Having closed the PE, the plaintiff claimed the deduction of the final losses in its German tax returns filed for 2007 and made the case that the German tax authorities' construction of the UK-German tax treaty, according to which exemption of profits from a UK PE means that losses are also exempt, violates the freedom of establishment. The Federal Fiscal Court referred the case to the CJEU.

AG Collins is of the view that the situation of a resident company with a domestic PE on the one hand and the situation of a resident company with a PE in another Member State on the other hand are not objectively comparable if the residence State has concluded a tax treaty with the PE State pursuant to which it exempts the profits (and losses) of the foreign PE. Therefore, a difference in treatment between domestic PE losses and foreign PE losses does not constitute an infringement of the freedom of establishment.

AG Collins' answer to the question on objective comparability made all further questions obsolete. Nonetheless, the AG's Opinion replied to them in the alternative. AG Collins believes that, if a deduction of the PE losses must be allowed for corporate income tax purposes, the same holds true for German trade tax purposes. However, losses that were carried forward do not qualify as final losses and the deduction cannot exceed the amount that would be deductible under the tax laws of the residence State.

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Portugal – CJEU rules Portugal's withholding tax on dividends paid to non-resident collective investment undertakings incompatible with the free movement of capital

On 17 March 2022, the CJEU issued a long-awaited ruling on *AllianzGI-Fonds AEVN* case (*C-545/19*) finding that Portuguese withholding tax on dividends paid to non-resident collective investment undertakings ("CIUs") is in breach of the free movement of capital as laid down in Article 63 TFEU.

Articles 3(1)(d) and 4(2) of the Portuguese Corporate Income Tax Code ("CIT Code") subject to CIT certain types of income earned in Portugal by non-resident entities, such as dividend payments made to a non-resident CIU. However, the same payments are, under Article 22(3) of the Portuguese Tax Benefits Statute, exempt from CIT if made to a resident CIU. This exemption applies only to CIUs incorporated under and governed by the laws of Portugal. The different taxation based on the CIU's tax residency, considered by many taxpayers as inadmissibly discriminatory, has led to several proceedings in Portugal. In 2019, the matter was referred to the CJEU.

On 6 May 2021, AG Kokott published her AG's Opinion, opining that there is no discrimination as Portugal taxes all CIUs, although through different legal mechanisms. The AG pointed out that, even though exempt from CIT, Portuguese CIUs are subject quarterly to Stamp Duty on their total net assets, and this taxation offsets the absence of CIT. Contrary to the AG's Opinion, the CJEU considered that, since CIT taxes income and, on the other hand, Stamp Duty taxes net assets, one is incapable of offsetting the other. Moreover, the CJEU emphasised that, further to the Portuguese regime, a resident CIU might avoid any taxation through the immediate distribution of dividends, while a non-resident CIU will always be subject to CIT if a dividend payment occurs. As a result, considering that (i) resident and non-resident CIUs are in a comparable situation, and (ii) no overriding reasons of public interest can justify this discrimination, the CJEU decided that the Portuguese regime constitutes an unjustified restriction to the free movement of capital.

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National Developments

Austria –Austrian High Administrative Court on taxation of derivatives

In its decision of 8 March 2022 (Ro 2019/15/0184-7), the Austrian High Administrative Court (VwGH) ruled that the Austrian provisions concerning the taxation of non-securitized derivatives infringed the freedom to provide services.

In 2017, an Austrian taxpayer earned income in the amount of approximately EUR 1.5 million out of non-securitized derivatives. The transactions were carried out via a bank in Denmark using the trading platform provided by this bank. In principle, such income is subject to the progressive income tax rate of up to 50%. However, there is a special clause available that is applicable only to domestic banks or domestic PEs of foreign banks. Under this special clause the domestic banks/PEs can voluntarily withhold Austrian withholding tax on income out of non-securitized derivatives leading to the application of a flat tax rate of 27,5%. The application of this special clause is at the sole discretion of the domestic bank/PE and the recipient of the income has no influence on whether the bank makes use of this option.

In the case at hand the taxpayer requested the application of the 27,5% flat tax on their income out of non-securitized derivatives claiming that the special clause was not in line with the freedom to provide services as well as with the free movement of capital. Both, the tax office and the court of first instance (BFG) denied the application of 27,5% flat tax on this derivatives income arguing that the progressive income tax rate is also applicable in purely domestic scenarios where the bank does not voluntary withhold Austrian withholding tax.

The Austrian VwGH overruled the BFG decision due to the unlawfulness of its content. According to the VwGH the different taxation of non-securitized derivates solely based on the residence of the bank restricts the freedom to provide services (Article 56 TFEU). Since no justification could be brought forward for this different treatment, the VwGH decided that the special clause infringes the freedom to provide services.

In the case at hand, the Austrian VwGH concluded that the taxpayer should be entitled to apply the flat tax rate of 27,5% on the income out of non-securitized derivates earned via the Danish trading platform. Since this interpretation now puts taxpayers trading non-securitized derivates with foreign banks in a better position than those trading with domestic banks (i.e. always application of flat tax rate vs. application of flat tax rate only in cases where the bank voluntarily withholds Austrian withholding tax) it remains to be seen how the Austrian legislator will react to this VwGH decision. Since the special clause was initially implemented only because of the withholding tax treaty between Austria and Switzerland (which was in force between 2013 and 2016), it may well be that the special clause will be abolished, resulting in all income out of non-securitized derivatives being subject to the progressive income tax rate in the future.

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Germany – Fiscal Court of Düsseldorf: free movement of capital inapplicable when a company resident in a third country owns a controlling shareholding in a German company

On 2 March 2022, the Fiscal Court of Düsseldorf dismissed the claim of a Japanese resident corporation for a refund of withholding tax on the grounds that the case was in the scope of the freedom of establishment which the plaintiff, being a resident of a third country, could not invoke (case no. 7 K 1424/18 KE).

The plaintiff is a Japanese corporation that received three dividends in 2009-2011 from its German subsidiary, in which it held 100% of the shares. In accordance with the double taxation agreement Germany/Japan, a German withholding tax of 15% was withheld from the dividends. The plaintiff applied for a refund of the withholding tax, claiming that a German corporation in a comparable purely domestic situation would have been entitled to the exemption of dividends from corporate income tax and full credit of the withholding tax. Since the German authorities rejected the application, the plaintiff brought the action before the Fiscal Court. The latter dismissed the action.

In the present case, the German rules on the taxation of dividends received by the plaintiff apply to both controlling shareholdings and portfolio shareholdings. It is, therefore, impossible to determine the applicable freedom based on the subject matter of the German laws.

According to the Fiscal Court, the circumstances of the specific case must be considered in a second step, because the case concerns outbound dividends. In a case where a company resident in a third country holds a controlling interest in a company resident in the EU, the market access of the parent company is at stake. However, this market access of a third country company cannot be subject to the same protection under the fundamental freedoms as the market access of a company resident in the EU.

Since the plaintiff held 100% of the shares and had, thus, clearly a controlling interest, the potentially applicable freedom was the freedom of establishment, but this could not be invoked.

The appeal against this judgment is pending with the Federal Fiscal Court (case no. I R 16/22).

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Spain – Spanish tax reform committee presents its report to the Ministry of Finance

On 3 March 2022, the Spanish tax reform committee delivered its “White Paper for tax reform in Spain" to the Minister of Finance, in which it makes recommendations on taxation. Related to Corporate Income Tax, the tax reform committee recommends the following:

Taxpayers
In this area, issues such as improving the definition of the effective place of management, integrating the definition of permanent establishment into the CIT regulations, greater precision in the anti-offshoring regulations and improving the tax transparency regime for asset-holding entities are proposed.

Taxable income
In relation to the participation exemption, the experts recommend that the reduction of the exemption to 95% is replaced by a tightening of the requirements to apply the exemption (i.e., a shareholding of, at least, 10% in the subsidiary, uninterruptedly held for two years and minimum effective taxation abroad). Reforms are also proposed in the area of tax depreciation, such as periodic updates of coefficients, the simplification of the methods and the analysis of the depreciation of intangible assets. Regarding net operating losses (NOLs), the elimination of the EUR 1M offset of losses without limiting it to the compensation percentage, establishing a compensation percentage (up to 70% of the positive tax base) regardless of the level of income and maintaining an unlimited period of compensation, are the measures proposed. With regards to the tax treatment of financial burden, the introduction of a deduction based on the increase in shareholders' equity is proposed, together with the elimination of capitalization and equalization reserves. Finally, the minimum taxation imposed on accounting income is rejected.

Tax benefits and special tax regimes
With regards to the R&D deduction, a number of reforms are proposed such as: its exclusion for the computation of the minimum tax rate of 15%, simplification of the procedures, improvements on deductions for investments, inclusion of expenses regarding Big Data, Artificial Intelligence or Next Generation Funds, and the elimination of the limit to the deduction of expenses. Moreover, the experts recommend maintaining all existing tax incentives.

Additional issues
In relation to the advanced CIT payment, it should operate on the taxable base of the period itself and the rate should be 5/7 of the final rate (i.e.,17%). The elimination of the minimum advance payment is also advocated. Finally, the elimination of the Tax on Economic Activities (IAE) is recommended.

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Spain – Two new "Green" Taxes introduced

On 9 April 2022, Law 7/2022, on Waste and Contaminated Land for a Circular Economy, was published in the Spanish Official Gazette, approving two new taxes: the special tax on nonreusable plastic packaging and the tax on landfill, incineration, and co-incineration of waste. The new Act also introduces important new features, such as the reintroduction of the hydroelectric canon (a form of environmental tax) or the approval of a specific tax regime for donations for VAT purposes. In this regard, both taxes will not enter into force until 1 January 2023.
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UK – HMRC v VolkerRail Plant Ltd & Others v HMRC [2022] UKUT 78 (TCC)

In March 2022, the UK's Upper Tribunal allowed an appeal by the UK Tax Authorities (HMRC) in the case of *VolkerRail* – determining that, although s.403D of the UK's Income and Corporation Taxes Act ("ICTA") 1988 entailed a restriction on the freedom of establishment under Article 49 TFEU, it was justified on the grounds of public interest in preventing double deductions. Further, although the legislation operated disproportionately to the objective of preventing double deductions, it could be 'read down' so as to conform with Article 49 TFEU.

The case considers the effect of Article 49 TFEU and the CJEU case law as applicable in the UK prior to Brexit. After the end of the Brexit transition on 31 December 2020, all such EU law issues (as applicable in the UK) must be decided by the UK tribunals and courts themselves, because under UK law they are not permitted to make any further references to the CJEU.

VolkerRail relates to losses arising in the UK permanent establishment (PE) of a Netherlands-resident group company in the periods from 2004 to 2008, which the group sought to relieve against profits of certain UK-resident group or consortium companies by way of group relief and consortium relief. It should be noted that the case does not concern cross-border group relief as it relates to relief of UK PE losses against UK profits in the UK group.

The legislation, in s.403D ICTA 1988, permitted group relief for UK PE losses only if *'no part of the loss … is represented in any amount which is deductible or allowable against non-UK profits for purposes of any foreign tax'*. Here, the €46m losses had all been set off against the Dutch group's profits within a Dutch fiscal unity, albeit €2m had been 'recaptured' by way of denial of Dutch tax credit for UK tax on UK PE profits in 2009 and 2010. HMRC denied UK group relief on grounds that, under s.403D, the losses were deductible against Dutch profits for Dutch tax purposes.

The First-tier Tribunal had held in 2020 in VolkerRail's favour that s.403D infringed the freedom of establishment, was not justified, and fell to be disapplied. In this regard, it had considered itself bound by Case *C-18/11 Philips Electronics*. In *Philips*, in 2012, the CJEU had considered the same section (s.403D) in materially identical circumstances and held that it entailed a difference in treatment between UK losses of an EU company's UK PE and losses of a UK-resident subsidiary (in relation to which no similar restriction existed), and further that it could not be justified by the need to prevent double use of losses and it should therefore be disapplied.

Subsequent to *Philips*, however, the CJEU had given its judgment in 2018 in Case *C-28/17 NN A/S*. In *NN*, a similar Danish restriction on using local PE losses of a non-resident company was not found to discriminate between establishment via a Danish PE as opposed to a Danish subsidiary, because Danish law also prohibited a Danish-resident company from claiming deductions for expenditure which could be deducted in another state. Nonetheless, the CJEU held that the Danish restriction entailed a difference in treatment 'of another nature' – between a Danish PE of a subsidiary resident in another EU Member State, and (on the other hand) a wholly domestic group. However, the CJEU held that the restriction was justified by the need to prevent double use of losses, which would otherwise give cross-border situations an unjustified advantage over comparable national situations, in which a double deduction was not possible.

In *VolkerRail*, HMRC argued that in *NN* the CJEU had departed from *Philips* in this respect. The First-tier Tribunal had rejected this argument, on grounds that the CJEU in *NN* had not expressly stated that it was departing from *Philips*, and that in any event *NN* concerned a national provision entailing a different type of difference of treatment - of a domestic PE as compared with a wholly domestic group.

On appeal, however, the Upper Tribunal held that the CJEU does not always state expressly when it is departing from its previous Judgments - citing the example of Cases *C-115/81* & *C-116/81* *Adoui & Cornuaille v Belgium*. It concluded that, on the question of justification, *NN* did represent a departure from *Philips*. As the Advocate General (Campos Sánchez Bordona) had noted in *NN*, subsequent to the judgment in *Philips* both the OECD's 'BEPS' reports and the EU 'ATAD' had specifically targeted the prevention of double relief for the same loss or expense. Against that background, it was not surprising that the CJEU had decided that preventing double loss relief should now constitute an acceptable justification.

S.403D was disproportionate to that objective, in that (1) it denied UK group relief for the whole loss even where only part was allowable against non-UK profits, and (2) it denied relief even if the loss was only deductible (i.e., even if not actually deducted, on the facts) against non-UK profits. However, the disproportionality could be cured by adopting a 'conforming construction' whereby the restriction in s.403D, denying UK group relief, was to be construed as applying only to the extent, pound for pound, that the loss had actually been deducted against non-UK profits.

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EU Developments

EU – ECOFIN Council fails to agree on the draft Directive to transpose the global agreement on Pillar Two into EU law

As was the case for their monthly meeting on 15 March 2022, EU-27 Finance Ministers failed to agree unanimously on the European Commission's proposal to transpose the global agreement on Pillar Two into EU law via a Directive. Poland vetoed and reiterated the need for a legal link between Pillars One and Two in what is seen as a political move to try to obtain concessions from the EU in unrelated policy areas. Discussions in the ECOFIN Council are continuing and the draft Directive is expected to be on the agenda of one of the remaining ECOFIN meetings under the French Presidency (24 May and 17 June).

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EU – European Commission provides updated information on its multilateral Cooperative Compliance (ETACA) pilot project for MNEs

The European Commission has provided further guidance regarding its multilateral Cooperative Compliance pilot project for MNEs, as part of its proposed EU Cooperative Compliance framework, commonly called ETACA (*European Trust and Cooperation Approach*). The aim of this non-legislative initiative is to facilitate and promote tax compliance by taxpayers based on greater cooperation, trust and transparency between taxpayers and tax administrations and among tax administrations. The other aim according to the European Commission is "to provide a framework to stimulate a preventive dialogue leading to the performance by the tax administrations of a high-level risk assessment of the transfer pricing policy adopted by large multinational enterprises. As a result, companies receive support in their internationalisation in order to avoid double taxation issues and reduce tax compliance costs."

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EU – European Commission DG TAXUD publishes Management Plan for 2022

The European Commission's DG TAXUD published its Management Plan for 2022 on 7 March, which includes inter alia:

- a draft Directive for multinationals to disclose their effective tax rates (Q2 2022).
- Pillar One draft Directive (Q4 2022), NB: originally scheduled for adoption on 27 July 2022
- DAC 8 draft Directive (Q2 2022)

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EU – European Parliament adopts Resolution on fair and simpler taxation supporting the recovery strategy

On 10 March 2022, the European Parliament's Plenary adopted a Resolution on fair and simple taxation supporting the recovery strategy. The Resolution contains recommendations regarding the follow-up to the European Commission's July 2021 EU Action Plan and its 25 initiatives in the areas of VAT, business and individual taxation.

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Spain – European Commission sends reasoned opinion regarding tax payments from foreign bank accounts

On 6 April 2022, the European Commission sent the Spanish government a reasoned opinion establishing that the Spanish law prevents a non-resident from paying taxes by direct debit, or in some cases, credit, if its bank account is located in another EU Member State. The Spanish regulations state that the bank must be authorized by the Spanish Tax Authorities as a "collaborating entity". The European Commission notes that it can be very difficult in practice for foreign payment service providers to get authorized. The European Commission considers that these regulations contravene Single Euro Payment Area (SEPA) Regulation 260/2012. If Spain does not provide an answer within two months, it might be referred to the CJEU. The Spanish Ministry of Finance has said it would review the reasoned opinion, highlighting that the law had been revised recently to allow non-residents to pay taxes even if the bank account is localized in the EU or abroad.

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ABOUT THE EUDTG

EUDTG is PwC's pan-European network of EU law experts. We specialise in all areas of direct tax, including the fundamental freedoms, EU directives and State aid rules. You will be only too well aware that EU direct tax law is moving quickly, and it's difficult to keep up, but it is crucial that taxpayers with an EU/EEA presence understand the impact.

See for more info: www.pwc.com/eudtg or contact bob.vandermade@pwc.com