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European Capital Movements and Corporate Taxation

From Transaction-Based Origins
to More Principle-Based
Capital and Taxation Policies

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European Capital Movements and Corporate Taxation

Why this book?

The basic premise of this book is the existence of the EU regime for capital transactions – which also concerns direct taxation – consisting of both capital transactions regulation within the European Union and harmonized and non-harmonized regulation of direct taxation. The book develops the idea of such parallel existence of liberalization and direct taxation policies by exposing the current EU capital liberalization regime and its objectives and effects, as well as policy elements of the EU taxation regime. It compares and contrasts the building blocks of EU capital and taxation regimes with the OECD and the WTO regimes, in so far as possible. Moreover, the author draws upon her experience as a fourth référendaire at the European Court of Justice to demonstrate how, on the subject of direct tax, the Court only interprets the EU fundamental freedoms and principles.

Furthermore, the book tests how certain common features of the EU regulation of capital and taxation are applicable in terms of a future EU policy in the area of capital transactions and direct taxation, in particular within a CCCTB or a CCTB environment and in the context of the OECD BEPS project. The BEPS initiative is discussed in terms of its methodological value for the interpretation of the balance of taxation powers of Member States, as well as the premises of coordination, non-discrimination and abuse, the three interpretative pillars of future EU taxation policy defined in the book. The book concludes by proposing a methodological alternative to the Court's appreciation of tax matters, particularly from the perspective of EU fundamental freedoms and the entitlement to such freedoms.

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Introduction

In the European Union, freedom of capital transactions is one of the fundamental freedoms. Regulation of such transactions concerns capital movements as defined by EU legislation and the case law of the Court of Justice of the European Union (the European Court of Justice or the Court) on the free movement of capital, the freedom of establishment and the freedom to provide services. In addition to its liberalization aspect, regulation of capital transactions inevitably concerns taxation. Direct taxation,¹ only partly harmonized at the EU level, is of a great relevance to capital regulation due to its potential to encroach upon the freedom of capital transactions.

The basic premise of this discussion is the existence of the EU *regime for capital transactions, which also concerns direct taxation*. The regime consists of capital transactions regulation within the European Union as well as harmonized and non-harmonized regulation of direct taxation. In particular, regulation of direct taxation at the EU level is inseparable from regulation of the EU fundamental freedoms and the freedom of capital transactions specifically and thus aspects of each of them, should one want to appreciate them properly, must be contextualized with regard to characteristics of the resulting merger. This regime has developed over the years in legislation and case law of the European Court of Justice and is endemic.

The European Court of Justice examines direct taxation at the EU level by using criteria and guidelines *primarily developed for promoting trade policy and freedom of movement*. Indeed, the concepts that have forged throughout the years in this subject area are a *specific combination of commercial and non-commercial elements*. In commercial terms, *the freedom of capital transactions is promoted* either because such transactions represent

1. Direct taxation is levied in accordance with a taxpayer's ability to pay. Examples of direct taxation are tax on income and tax on capital, the tax payable being calculated on the basis of the assets owned by the taxpayer when it accrues. However, tax on capital is different from tax on income because only some of the Member States apply it. *See*, among other sources, DE: Opinion of Advocate General Mengozzi, 29 Mar. 2007, Case C-298/05 *Columbus Container Services* [2007] ECR I-10451, paras. 99-100. In contrast, indirect taxation affects the EU trade of goods and provision of services through value added tax (VAT). *See* N. Maydell, *The Services Directive and Existing Community Law*, in *Services Liberalisation in the Internal Market*, European Community Studies Association of Austria (ECSA Austria) Publication Series Vol. 6, pp. 21-124 (F. Breuss, G. Fink & S. Griller (eds.), Springer, 2008), at p. 77, at footnote 230.

payments parallel to trade in goods and services or because they concern trading in financial markets.² In terms of capital regulation, such commercial approach to capital, depending on the exact definition of capital and specific policy orientation, is associated with regulator's objective of liberalization of capital transactions or maintaining of capital value.³ In contrast, taxation perspective on capital is *non-commercial* and focuses on the *value of capital transactions* in a given jurisdiction and given time period for the purpose of calculating tax portions. While capital policy focuses on liberalization of capital and economic efficacy, fiscal policy is concentrated on the *redistribution of resources*; the latter is done in accordance with Member States' jurisdiction in taxation matters. Since a state may tax its residents or income paid on its territory in accordance with its fiscal sovereignty, exercise in parallel of such sovereignty of two or more states may result in double taxation. Thus, fiscal policy regulates international transactions in light of the exercise of taxation powers of two or more fiscal sovereigns. In terms of freedom of capital transactions this means that while capital liberalization policy is focused on elimination of barriers to such movement, tax policy focuses on the achievement of this objective primarily through elimination of double taxation.⁴

The idea of the parallel existence of liberalization and taxation policies that requires a *common appreciation* has not been commented in depth; commentators of Community (now EU) regulation have focused on separate

2. In that sense, see K. Suzuki, *Endogenous Trade Policies, WTO Rules and International Capital Movement*, Discussion paper No. 21, School of Economics, Kwansai Gakuin University, pp. 1-59 (2003), also available at: <http://ideas.repec.org/p/kgu/wpaper/21.html>, at p. 3. See also WTO Working Group on the Relationship between Trade and Investment, *Scope and Definitions: "Investment" and "Investor"*, Note by the Secretariat, WT/WGTI/W/108 (2002).

3. Liberalization of capital movements on the international level is parameterized importantly by OECD, *Code of Liberalisation of Capital Movements [including Commentary to the Code]*, OECD Publications (2013), also available at: http://www.oecd.org/daf/inv/investment-policy/CapitalMovements_WebEnglish.pdf; OECD, *Code of Liberalisation of Current Invisible Operations*, OECD Publications (2013), also available at: http://www.oecd.org/daf/fin/private-pensions/InvisibleOperations_WebEnglish.pdf; and OECD, *Measurement of Capital Stocks, Consumption of Fixed Capital and Capital Services*, Manual (2001), also available at: <http://www.oecd.org/dataoecd/61/57/1876369.pdf>. See also OECD, *Methods Used by OECD Countries To Measure Stocks of Fixed Capital* (2000), also available at: <http://www.oecd.org/dataoecd/38/63/2674361.pdf>.

4. J.B. Slemrod & R.S. Avi-Yonah, *How Should Trade Agreements Deal with Income Tax Issues?*, 55 Tax Law Review, pp. 533-554 (2002), at p. 536; C. Singh, *Non-Discrimination in Tax Matters in the GATT – National Treatment*, in *The Relevance of WTO Law for Tax Matters*, Schriftenreihe zum Internationalen Steuerrecht Herausgegeben von Univ.-Prof. Dr Michael Lang, Band 45, pp. 49-71 (J. Herdin-Winter & I. Hofbauer (eds.), Linde, 2006), at p. 69.

aspects of capital transactions and direct taxation.⁵ Certain authors note the coexistence at the EU level of fundamental freedoms and taxation but comment it only in the context of interpretation of case law of the Court.⁶ Such an approach to the issue is of necessity flawed if one wants to properly assess current EU policy and its principles taking also in account the fact that Court's reasoning is of casuistic nature,⁷ let alone to build policy elements on the basis of the existing legislation and premises developed in the case law of the Court.

Therefore, a parallel analysis of the freedom of capital transactions and direct taxation as *coexisting parts of a single phenomenon* especially with regard to areas of direct taxation addressed by the European Court of Justice but non-harmonized at the EU level, is necessary since its sets ground for future policy development specifically tailored to the European Union,⁸ be

5. However, authors do grasp this duality, for instance by discussing the need to adjust criteria of both freedom of movement and taxation which may require considerable tax reform, see K. Vogel, J. Brands & K. van Raad, *Taxation of Cross-Border Income, Harmonization and Tax Neutrality under European Community Law: An Institutional Approach*, with comments by J. Brands & K. van Raad, pp. 11-34 (EFS Series Vol. 2, Kluwer Law International, 1994); S. Clossen, *How Much Tax Harmonisation in the European Union*, in *Tax Policy and the Impending Economic and Monetary Union: Generale Bank B.232.1 lectures 1997-1998*, pp. 67-70 (F. Abraham, J. Stuyck & F. Vanistendael (eds.), Leuven Law Series, Leuven University Press, 1999), pp. 67-70; C. Peters, *Non-Discrimination: The Freedom of Establishment and European Tax Law*, in *Legal Protection Against Discriminatory Tax Legislation, The Struggle for Equality in European Tax Law*, ch. 7, pp. 101-122 (H. L.M. Gribnau (ed.), Kluwer Law International, 2003), pp. 101-122, and P. Farmer, *Striking a Proper Balance between the National Fiscal Interests and the Community Interests – A Perpetual Struggle?*, in *The Influence of European Law on Direct Taxation, Recent and Future Developments*, ch. 3, pp. 31-34 (D. Weber (ed.), EUCOTAX Series on European Taxation Vol. 16, Kluwer Law International, 2007), pp. 31-34. Specifically as to allocation of rights to tax, see D. Hohenwarter, *The Allocation of Taxing Rights in the Light of the Fundamental Freedoms of EC Law*, in *Tax Treaty Law and EC Law*, Schriftenreihe zum Internationalen Steuerrecht, Band 46, pp. 83-124 (M. Lang, J. Schuch & C. Staringer (eds.), Linde, 2007), pp. 83-124. For criticism of the European Court of Justice, see S. Douma, *Optimization of Tax Sovereignty and Free Movement* (Doctoral Series Vol. 21, IBFD, 2011), pp. 9-30.

6. C. HJI Panayi, *Double Taxation, Tax Treaties, Treaty-Shopping and the European Community* (EUCOTAX Series on European Taxation Vol. 15, Kluwer Law International, 2007), ch. 4, pp. 131-175, 143-169 & 173-175, commenting on the European Court of Justice case law in comparison with the US regulation in (direct) tax matters, notes, at p. 173, that there are no tax specific tests in the case law of the European Court of Justice and that the provisions of Community (now EU) law are applied in general to the area of taxation.

7. According to Panayi (2007), *supra* n. 6, at p. 169, decisions of the European Court of Justice concerning allocation of taxation powers in terms of Community (now EU) law seem to be “a matter of impression”.

8. On anti-treaty shopping provisions see Panayi (2007), *supra* n. 6, pp. 231-250. Panayi also mentions recommendations of the Commission of the European Union (European

it the Common Consolidated Corporate Tax Base (CCCTB), the Common Corporate Tax Base (CCTB),⁹ or, for purposes of an academic debate, the EU Tax Treaty Model,¹⁰ Community (now EU) multilateral tax treaty,¹¹

Commission or Commission) as one of the possible alternatives for a future EU policy, *supra* n. 6, pp. 243-245.

9. See Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB), SEC(2011) 315, SEC(2011) 316, COM(2011) 121/4, 2011/0058 (CNS) (2011) also available at: http://ec.europa.eu/taxation_customs/resources/documents/taxation/company_tax/common_tax_base/com_2011_121_en.pdf (CCCTB Directive Proposal 2011). For a discussion on general points as well as requirements for forming a group, tax base, consolidation, on regime for financial institutions and on international and administrative aspects in the context of the CCCTB, see C. Spengel, *Concept and Necessity of a Common Tax Base, An Academic Introduction*, in *A Common Consolidated Corporate Tax Base for Europe – Eine Einheitliche Körperschaftsteuerbemessungsgrundlage für Europa*, pp. 1-48 (W. Schön, U. Schreiber & C. Spengel (eds.), Bilingual ed. Springer, 2008), pp. 16-22 (on effective tax burdens); Cussons (2007), C. HJI Panayi, *The Common Consolidated Corporate Tax Base and the UK Tax System*, Institute for Fiscal Studies Discussion Paper No. 9 (2011), available at: <http://ssrn.com/abstract=1809568> (2011), and T. Sanders, *Consolidation in the CCCTB Proposal*, in *CCCTB, the Selected Issues*, ch. 1, pp. 1-10 (D. Weber (ed.), EUCOTAX Series on European Taxation Vol. 35, Wolters Kluwer Law & Business, Kluwer Law International, 2012). For a discussion on the United States' experience with common tax base, see J. Hey, *EU Common Consolidated Corporate Tax Base: Guided Variety versus Strict Uniformity – Lessons from the “U.S. States’ Tax Chaos”*, Jean Monnet Working Paper 02/08 (2008), also available at: <http://www.jeanmonnetprogram.org/papers/08/080201.pdf>, and W. Hellerstein, *Lessons of US Subnational Experience of EU CCCTB Initiative*, in *A Common Consolidated Corporate Tax Base for Europe – Eine Einheitliche Körperschaftsteuerbemessungsgrundlage für Europa*, pp. 150-154 (W. Schön, U. Schreiber & C. Spengel (eds.), Bilingual ed., Springer, 2008), pp. 150-154. For a discussion on drawbacks of the CCCTB and advantages of an enhanced CCTB, see E. Roeder, *Proposal for an Enhanced CCTB as Alternative to a CCCTB with Formulary Apportionment*, 4 World Tax J. 2, pp. 125-150 (2012), Journals IBFD; Working Paper of the Max Planck Institute for Tax Law and Public Finance No. 2012-01 (2012); also available at SSRN: <http://ssrn.com/abstract=2012640> or <http://dx.doi.org/10.2139/ssrn.2012640>.

10. P. Pistone, *The Impact of Community Law on Tax Treaties: Issues and Solutions*, 1st ed. (EUCOTAX Series on European Taxation Vol. 4, Kluwer Law International, 2002), ch. V, pp. 235-324. Pistone proposes a comprehensive EC Model Tax Convention, a multilateral non-self-executing convention, combining existing provisions of international tax law, as embodied in the OECD *Model Tax Convention on Income and on Capital*, 2010 Condensed Version and Commentary (22 July 2010), Models IBFD, with the principles of Community (now EU) tax law as enunciated by the European Court of Justice. The author notes that it would be necessary to consider at the same time the body of scholarship. For a period, the European Commission supported such a solution to the conflict between tax treaties and Community (now EU) law by stating, on 23 Oct. 2001 in its document COM(2001) 582 final, at pp. 14-15, that “the most promising way ... is to agree [on] an EU version of the [OECD Model (2010)] (or of certain articles) which meet the specific requirements of EU membership”. Also, in Panayi (2007), *supra* n. 6, pp. 231-250, pp. 239-243.

11. See Panayi's opinion, *supra* n. 6, at p. 245. M. Lang, *The Personal Scope of a Multilateral Treaty*, in *Multilateral Tax Treaties, New Developments in International Tax Law*, ch. 7, pp. 119-128 (M. Lang et al. (eds.), Series on International Taxation Vol. 18, Kluwer Law International and Linde, 1998) (1998a), discusses residence as a criterion

“fractional taxation”,¹² enactment of additional direct tax directives and other instruments,¹³ a potential international expansion of the EU models and policies¹⁴ or fiscal surveillance measures enacted at the EU level in response to the Organisation for Economic Co-operation and Development (OECD) initiative on Base Erosion and Profit Shifting (BEPS).¹⁵ With exception of the CCCTB, the CCTB and the BEPS, the present discussion will not concentrate specifically on these policy proposals or on the idea of tax harmonization and/or approximation of laws at the EU level.¹⁶ It will

easily incorporated into a multilateral treaty; see also M. Lang, *The Concept of Multilateral Treaty*, in *Multilateral Tax Treaties, New Developments in International Tax Law*, ch. 10, pp. 187-196 (M. Lang et al. (eds.), Series on International Taxation Vol. 18, Kluwer Law International and Linde, 1998) (1998b); M. Lang et al., *Draft for a Multilateral Tax Treaty*, in *Multilateral Tax Treaties, New Developments in International Tax Law*, ch. 11, pp. 197-245 (M. Lang et al. (eds.), Series on International Taxation Vol. 18, Kluwer Law International and Linde, 1998); H. Loukota, *Multilateral Tax Treaty Versus Bilateral Treaty Network*, in *Multilateral Tax Treaties, New Developments in International Tax Law*, ch. 5, pp. 83-103 (M. Lang et al. (eds.), Series on International Taxation Vol. 18, Kluwer Law International and Linde, 1998); J. Schuch, *The Methods for the Elimination of Double Taxation in a Multilateral Tax Treaty*, in *Multilateral Tax Treaties, New Developments in International Tax Law*, ch. 8, pp. 129-152 (M. Lang et al. (eds.), Series on International Taxation Vol. 18, Kluwer Law International and Linde, 1998) (1998a), and R. Mason, *US Treaty Policy and the European Court of Justice*, in *Comparative Fiscal Federalism, Comparing the European Court of Justice and the US Supreme Court's Tax Jurisprudence*, ch. 11, pp. 405-464 (R.S. Avi-Yonah, J.R. Hines, Jr. & M. Lang (eds.), EUCOTAX Series on European Taxation Vol. 14, Kluwer Law International, 2007) (2007a), pp. 443-463. S. van Weeghel, *The Tie-Breaker Revisited: Towards a Formal Criterion?*, in *A Vision of Taxes within and outside European Borders*, Festschrift in honour of Prof. Dr Frans Vanistendael, pp. 961-969 (L. Hinnekens & P. Hinnekens (eds.), Kluwer Law International, 2008) (2008a), discusses alternatives to the OECD tie-breaker clause.

12. K. van Raad, *Fractional Taxation of Multi-State Income of EU Resident Individuals – A Proposal*, in *Liber Amicorum Sven-Olaf Lodin, K. Andersson*, pp. 211-221 (P. Melz & C. Silfverberg (eds.) Kluwer Law International, 2001).

13. Panayi (2007), *supra* n. 6, pp. 245-246. Such instruments should, according to the author, gradually cause tax treaties to become obsolete. According to this approach, not only the state of residence of a taxpayer (the residence state) but also the state of source of taxable income (the source state) should calculate the taxpayer's worldwide income and the resulting tax, and restrict the tax they effectively levy to the fraction thereof that corresponds with the fraction that the source state income represents of the worldwide income.

14. In this sense, see E. Raingard de la Blétière, *Les relations entre le droit communautaire et le droit fiscal international: nouvelles perspectives*, PhD thesis under supervision of Daniel Gutmann, Université Panthéon-Sorbonne Paris, Paris 1 (2008), who advocates tailoring of international tax law according to the Community (now EU) regulation of taxation, i.e. harmonization at a supranational level paralleled by a tax network at international level.

15. OECD *Action Plan for Base Erosion and Profit Sharing* (19 July 2013), International Organizations' Documentation IBFD.

16. This position is undertaken in view of a vast literature and academic writing existing on the subject of the Community (now the Union) tax harmonization as well as the current political configuration of the European Union. In that sense, I agree with authors

focus on capital and fiscal *policy elements* as may be discerned from current law of the European Union; notably, one may not speak of fully developed EU policies in the area where the analysis of capital transactions coincides with concepts of direct taxation.¹⁷ These elements can be identified from *legal premises* found in the case law of the Court and from certain pieces of EU legislation.

One may discern clear policy elements¹⁸ from the current regulation of capital movements and the Court's examination of Member States' direct

such as McLure, who consider that the degree of economic integration implying full tax harmonization (including tax base and tax rates, as well as EU tax administration) would probably require a federal system; in C.E. Jr. McLure, *The Long Shadow of History: Sovereignty, Tax Assignment, Legislation, and Judicial Decisions on Corporate Income Taxes in the US and the EU*, in *Comparative Fiscal Federalism, Comparing the European Court of Justice and the US Supreme Court's Tax Jurisprudence*, ch. 5, pp. 119-190 (R.S. Avi-Yonah, J.R. Hines, Jr. & M. Lang (eds.), EUCOTAX Series on European Taxation Vol. 14, Kluwer Law International, 2007) (2007a), at p. 147. Similarly, P. Pistone, *Towards European International Tax Law*, 14 EC Tax Review 1, pp. 4-9 (2005) (2005a), at p. 6, speaks in favour of full equality of tax treatment between residents and non-residents in the European Union but adds that such a solution would require a substantial change in the actual international tax law order.

17. Certain authors refer to "European tax law" in the sense of compendium of Community (now EU) law in the field of taxation. Inter alia, see H. Sterdyniak et al., *Vers une Fiscalité européenne*, (Economica, 1991), ch. 2, pp. 31-77, on what may be called the general principles of taxation within the Community (now European Union). See also A.J. Easson, *Taxation in the European Communities* (European Community Law Series 5, The Athlone Press, 1993); D.W. Williams, *EC Tax Law*, 1st ed. (European Law Series, Longman, 1998); L.W. Gormley, *EU Taxation Law* (Richmond Law and Tax Ltd., 2005), and Pistone (2005a), supra n. 16, pp. 4-9. P. Pistone, *General Report*, in *The EU and Third Countries: Direct Taxation*, Schriftenreihe zum internationalen Steuerrecht Herausgegeben von Univ.-Prof. Dr Michael Lang, Band 46, pp. 15-55 (M. Lang & P. Pistone (eds.), Linde, 2007) (2007a), at p. 36, underlines that European International Tax Law is a new dimension of international tax law whereby the Member States are bound to comply with the primacy of Community (now EU) law when dealing with cross-border situations. According to the same author, the new system distinguishes itself from international tax law principally with regard to its concept of comparability of residents and non-residents and a different configuration of national sovereignty. See also D.M. Weber, *European Direct Taxation, Case Law & Regulations* (Wolters Kluwer, 2009); J.F. Avery Jones, *Flows of Capital between the EU and Third Countries and the Convergences of Disharmony in European International Tax Law*, in *Tax Policy and the Impending Economic and Monetary Union*, pp. 71-92 (Leuven Law Series, F. Abraham, J. Stuyck & F. Vanistendael (eds.) Leuven University Press, 1999), previously published in 7 EC Tax Review 2, pp. 95-105 (1998), and P. Farmer & R. Lyal, *EC Tax Law* (Oxford European EU law Library, Clarendon Press, 1995). C. Brokelind, *Introduction*, in *Towards a Homogenous EC Direct Tax Law: Assessment of the Member States' Responses to ECJ's Case Law*, pp. 1-23 (C. Brokelind, A. Bullen & A. Cordewener (eds.), IBFD, 2007), pp. 15-17, notes that while a more homogeneous approach is evolving through Member States response to case law of the European Court of Justice, there is still no uniformity of Community (now EU) law in direct taxation.

18. With regard to the balances of power, different levels of policymaking and discernible regulatory elements in terms of taxation – rather than well-defined tax policies – that

taxation, in particular, *the balance of powers between Member States and the European Union* when it comes to direct taxation, *the EU concept of discrimination between residents of different Member States* and a certain concern for the *protection of assets* in capital transactions. Certain premises of these policy elements form part of the core of the EU law, obligatory for the Member States, and represent the foundations of what may possibly become a specific EU tax model or at least a more coherent tax policy in the future. Such a model would possibly include an eventual adoption of the CCCTB or the CCTB and potential EU-level measures against fiscal abuse, coupled with measures of fiscal surveillance.

This discussion builds on the existing legislation of the European Union and case law of the European Court of Justice and defines the basic character of the EU regulation of capital transactions and its approach to direct taxation. It defines and discusses the most important policy elements and points to difficulties of the EU regulation that need to be addressed independently of any steps towards future tax policy or tax harmonization. Such difficulties arise from the current definition of the balance of powers between Member States and the European Union in direct taxation matters as well as the interplay between commercial and non-commercial aspects of capital transaction liberalization, in the sense that these may contradict international standards and international obligations of the European Union or are non-sustainable in light of the possible future development of the EU markets.

For this reason, the book proposes certain policy reorientations, clarifications concerning interpretation of homonymous terms such as discrimination in terms of transaction policy and in the context of taxation, and policy build-ups particularly with regard to premises of non-discrimination and anti-abuse. Policy build-ups will be commented in the sense of future use of current policy elements in a CCCTB or CCTB-policy environment, implying a harmonized system of taxation for companies opting for the CCCTB or the CCTB, as well as a non-harmonized status quo environment. Since the coexistence of harmonized and non-harmonized environments implies coordination between EU and Member States' jurisdictions, such a dual system will require strong coordination measures in addition to harmonization of substantive law. Proposed changes to anti-abuse measures also take note of the status quo and potential developments at Member State or EU level in response to the BEPS. The policy development propositions take

currently exist in EU capital and taxation regulation, I use the term "policy elements" for regulatory premises I discern from EU regulation and case law of the European Court of Justice. For this reason, the term "EU capital and/or taxation policy" is used only with regard to suggested alternatives and innovations I propose in later chapters.

into account the fact that whatever the changes in the area of direct taxation may be, they *will* affect the current balance of powers between the Member States and the European Union.

Several prominent academics (Martín Jiménez, Pistone, Wattel, as referred to later in this book) and practitioners have proposed solutions for the future EU policy building on separate aspects of the combined appreciation of the fundamental freedoms and direct taxation. They have tested background concepts of both sides of this liberalization-taxation regime such as discrimination (Birk, Banks, Gribnau, Lang, Meussen, Peters, Santa-Bárbara Rupérez, Saddiki, Van den Berge, Vanistendael, Van Raad and Wattel, as referred to later in this book), and commented on the influence of Community (now EU) law on direct taxation, tax treaties and avoidance of double taxation (Cordewener, Decoq, Farmer, Hofstätter, Hohenwarter, Kofler, Lang, Le Gall, Lehner, Loukota, Lyal, Panayi, Pistone, Sánchez Jiménez, Schneeweiss, Schuch, Soler Roch, Staringer, Teixeira, Van Thiel, Wattel and Whitehead, as referred to later in this book). However, there is no coherent examination in the literature of certain underlying elements of the current EU liberalization-taxation regime and their use in a future EU policy. This thesis is intended to fill this gap, following up on the existing groundwork made by legal practice and academia. Proposed developments respect the logic of existing policy elements as far as possible, but take inspiration also from sources external to the European Union.

In view of the many legal and non-legal obstacles within the European Union which define its less-than-optimal approach to all-EU taxation solutions – first, political unwillingness of Member States to proceed towards decisive tax harmonization, second, lacunae remaining in European regulation of direct tax matters meaning there is no possibility to bridge obstacles in the sense of juridical double taxation by reference to EU fundamental freedoms and finally, the nature of legal interpretation by the European Court of Justice –, it is important to consider a wider context in terms of EU potential future policy, i.e. the context of current and potential future activities within the OECD.

Recently, the OECD's activities with regard to occurrences of gaps exploited by companies that avoid taxation in their home countries by shifting their activities abroad to low or no tax jurisdictions increased dramatically.¹⁹ The OECD activities resulted in the Action Plan on Base Erosion and Profit

19. BEPS Action Plan, *supra* n. 15.

Sharing (the BEPS Action Plan),²⁰ the organization's reply to "... a concern [of a number of countries] about how international standards on which bilateral tax treaties are based allocate taxing rights between source and residence States". The BEPS Action Plan promises that the actions defined in its context "... will restore both source and residence taxation in a number of cases where cross-border income would otherwise go untaxed or would be taxed at very low rates, [whereas] these actions are not directly aimed at changing the existing international standards on the allocation of taxing rights on cross-border income".²¹ The BEPS Action Plan addresses the need for new standards of international taxation, realignment of substance and form in international taxation and promises to build on transparency, certainty and predictability.²²

In view of the above, discussions and implementation proposals of the BEPS prove that OECD member countries, and among them EU Member States that are members thereof, are willing to draw rules for the exercise of their tax sovereignty in cross-border situations, which is noteworthy in view of their reticence within the *cadre* of the European Union. On the example of hybrid mismatches it may be implied that one jurisdiction will have to take notice of tax treatment applied in another jurisdiction for the purpose of determining the tax treatment applicable to a given cross-border situation at the level of each jurisdiction concerned. Independent of the fact that the BEPS are intended to address cases of international tax abuse originating mostly from disparities in international taxation, the BEPS methodology may lead to jurisdictions no longer exercising their powers in isolation. In this sense, the BEPS introduce novel methodology on how jurisdictions may exercise their tax powers in the context of obligatory international anti-tax abuse coordination. In view of this very modern approach to the exercise of taxation powers, I also analyse possible application of the BEPS methodology in light of the current European law as well with regard to currently proposed amendments of applicable EU regulations.

Three areas of focus

After a note on its methodology and premises, this book concentrates on three issues.

Since one is more likely to understand a system and provide for its improvements if one studies its separate elements statically and their interactions

20. Id.

21. Id., at p. 11.

22. Id., at pp. 13-14.

dynamically, this account will start off by examining the basic characteristics of capital movements in the European Union (chapter 2), and then comment on basic and complex contradictions between such characteristics and regulation of taxation in EU law (chapter 3). This should help understand the basic elements and contradiction of the coexistence, at the EU level, of fundamental freedoms and taxation in terms of a future consolidated capital policy and development in terms of anti-abuse policy (chapter 4).

In particular, chapter 2 starts by exposing the current EU *capital liberalization regime*, its objectives and effects, focusing specifically on the *concept of capital, assets and liabilities*. Interpretations (definitions) and policy elements identified are compared to concepts of the International Accounting Standards and International Financial Reporting Standards including related interpretations (IAS and IFRS, together referred to as IAS, unless specified otherwise), adopted also at the EU level. This is necessary due to the fact that the IAS represent a harmonized regulation of capital transactions at the EU level in the sense that they provide for uniform definition of capital in terms of its value as well as methods for evaluation of assets and liabilities. Therefore, the IAS may be an important element of future EU capital policy.

Next, the EU regime so defined is compared and contrasted with capital regimes established by the OECD and the World Trade Organization (WTO). This part builds on the analysis of EU legislation, case law of the European Court of Justice, and international regulation as elaborated by the OECD and the WTO, by employing teleological and historical methods of interpretation.

Chapter 3 analyses case law of the European Court of Justice in order to discern policy elements of the EU taxation regime. These include premises developed in the Court's case law concerning, among others, jurisdiction of Member States in direct taxation matters, fiscal territoriality, taxation symmetry, equal treatment in taxation matters, and effective fiscal surveillance. The chapter underlines contradictions between different premises. In particular, because the Court interprets national taxation regulation by means of EU law and EU fundamental freedoms, certain policy elements are shared by both capital liberalization and taxation policies. However, they may have different effects in the area of capital liberalization as compared to taxation, due to their different nature.

Having examined the principles that the European Court of Justice uses to analyse both capital transactions and taxation as defined in earlier chapters, chapter 4 tests how certain of the common features of the EU regulation

of capital and taxation are applicable in terms of a future EU policy in the area of capital transactions and direct taxation. Such a future policy will be defined by the coexistence of CCCTB or CCTB-harmonized and non-harmonized environments. The coexistence will have to imply both harmonization measures for balancing out transaction costs occasioned because of such coexistence and strong coordination tools for securing cooperation and exchange of information between EU and Member States' jurisdictions.²³

Features of the current EU substantive regulation of capital and taxation that will be most important in the future are non-restriction and non-discrimination. These two principles will be decisive as substantive legal elements in the future EU policy because, first, certain tax areas will remain under Member State regulation (which corresponds to the status quo in terms of taxation regulation), while other matters will possibly be harmonized by a future EU taxation policy in terms of the CCCTB or the CCTB, and, second, eventual tax harmonization will necessarily be limited. The principles of non-restriction and non-discrimination will need to be complemented by a coordination mechanism and a system of prevention of double taxation, the latter including measures for prevention of discrimination as well as abuse and tax evasion, both in relations between Member States and between those and third countries. Measures of coordination and prevention of double taxation in the context of the CCCTB or the CCTB will need to be enacted by the EU legislator on the basis of currently existing coordination mechanism but will need to take into consideration intricacies of the CCCTB or the CCTB system.

Once the possible framework of an EU policy is defined, chapter 4 looks towards the BEPS context. The BEPS initiative is discussed in terms of its methodological value for the interpretation of balances of taxation powers of Member States and the premises of coordination, non-discrimination and abuse, defined in chapter 3 as interpretative pillars of future EU taxation policy. It is important to note that the BEPS actions may define actual terms of future international (and thus also EU) taxation policy, whereas the European Union may develop its own anti-abuse regulation in parallel. Introducing the BEPS methodology into interpretation of the European Court of Justice may lead to a change in paradigm as to the exercise of tax

23. Tax harmonization would inevitably be of a limited extent. Generally, on the limited nature of tax harmonization, see J.M. de la Villa, *La Armonización Comunitaria en el Ámbito de la Imposición Directa, Su Problemática Jurídico-Contable y Su Incidencia en España*, (Instituto de Planificación Contable, Fábrica Nacional de Moneda y Timbre, 1988), at para. 2, at p. 11. Coordination mechanism will need to be adopted in line with current EU regulation on information exchange, commented in later chapters.

jurisdiction of EU Member States and help provide for an alternative to the Court's appreciation of tax matters through lens of EU fundamental freedoms and entitlement to such freedoms in particular.

1.1. Sphere of EU capital transactions

1.1.1. Scope of the study

Interaction of the EU freedom of capital transactions and direct taxation can be described by referring to the case law of the European Court of Justice, interpreting articles 43, 56, 58 and 49²⁴ of the Consolidated version of the Treaty establishing the European Community (Treaty),²⁵ now (without substantial modifications) articles 49, 63, 65 and 56 of the Consolidated version of the Treaty on the Functioning of the European Union (TFEU),²⁶ EU legislation in the area of direct taxation, the EU-adopted IAS and proposals of the European Commission for a future CCCTB regime, or, alternatively, proposals for a CCTB regime. In order to describe this body of law, I use the term the "EU capital transactions regime". To this, one must also add proposals for directive amendments and future regulation in the area of fight against fiscal fraud, which are specifically referred to throughout this account.

The most important source to establish such a capital transactions regime is the case law of the European Court of Justice which, due to the lack of EU

24. See K. Lenaerts & L. Bernardeau, *L'encadrement communautaire de la fiscalité directe*, 43 Cahiers de Droit Européen 1/2, pp. 19-109 (2007). The principle of non-discrimination has been given effect in the fundamental freedoms (*lex specialis*): the right of establishment (see the judgments NL: ECJ, 12 Apr. 1994, Case C-1/93 *Halliburton Services/Staatssecretaris van Financiën* [1994] ECR I-1137, ECJ Case Law IBFD, at para. 12; DE: ECJ, 29 Feb. 1996, Case C-193/94 *Skanavi and Cryssanthakopoulos* [1996] ECR I-929, at para. 21; and NL: ECJ, 13 Apr. 2000, Case C-251/98 *C. Baars v. Inspecteur der Belastingen Particulieren* [2000] ECR I-2787, ECJ Case Law IBFD, at para. 24 and later judgments) and the free movement of capital. With regard to former art. 6 of the Treaty establishing the European Community (Consolidated version), OJ C 224 (1992) (EC Treaty), see the judgments in *Halliburton Services* (C-1/93), at para. 12; GR: ECJ, 29 Apr. 1999, Case C-311/97 *Royal Bank of Scotland* [1999] ECR I-2651, ECJ Case Law IBFD, at para. 20; and in *Baars* (C-251/98), paras. 23 & 25.

25. European Union – Consolidated Versions of the Treaty on European Union and of the Treaty establishing the European Community (Consolidated text), Consolidated Version of the Treaty establishing the European Community, OJ C 321E (2006) (Treaty).

26. Consolidated versions of Treaty on European Union and the Treaty on the Functioning of the European Union (Consolidated versions), OJ C 83 (2010) (TFEU). See also the Treaty on the Functioning of the European Union (Consolidated version), OJ C 115 (2008).

legislation with regard to direct taxation,²⁷ interprets the subject area by analysing interactions between the EU freedoms and direct taxation. It is only to the extent to which exercise, by Member States, of (non-harmonized) direct taxation rules may have an impact on the EU fundamental freedoms that they come within the scope of law of the European Union.²⁸ The Court's case law contains references to capital movements, establishment, services and taxation, where of interest to this discussion are in particular elements of EU capital transactions regime and direct taxation as discernible through the Court's interpretation of *the freedom of establishment and the free movement of capital*.

This discussion concentrates on *corporate (non-personal) capital transactions* including dividends.

1.1.2. Methodology of the study

The European Court of Justice examines capital movements and taxation from the sole perspective of EU law in general and EU fundamental freedoms in particular, which means that the Court discusses the freedoms and their inhibitions due to taxation. Therefore, *a conglomerate vision of capital liberalization and taxation* as it currently exists will be taken in the examination of both the EU capital regime and premises developed in the case law of the Court concerning direct taxation. Such an approach is best presented graphically.

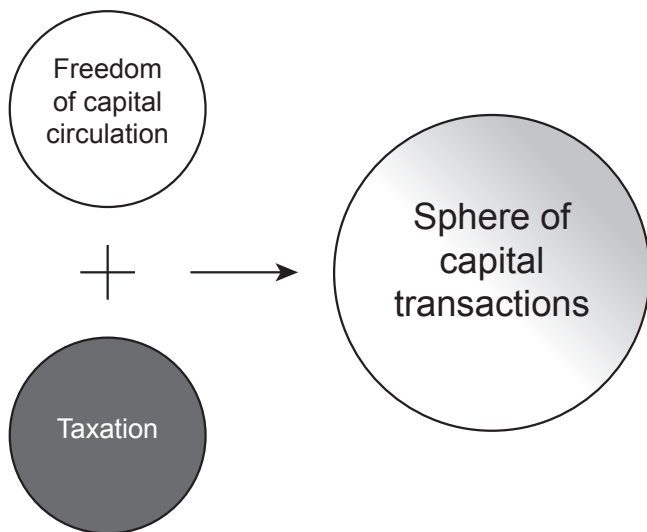
27. The subject matter of the following directives is harmonized at the European level: Council Directive 2009/133/EC of 19 October 2009 on the Common System of Taxation Applicable to Mergers, Divisions, Partial Divisions, Transfers of Assets and Exchanges of Shares Concerning Companies of Different Member States and to the Transfer of the Registered Office of an SE or SCE between Member States (Codified Version), OJ L310 (2009), EU Law IBFD; Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (Recast), OJ L 345 (2011), EU Law IBFD; Convention 90/436/EEC on the elimination of double taxation in connection with the adjustment of transfers of profits between associated undertakings, OJ L 225 (1990), EU Law IBFD; Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments, OJ L 157 (2003), and Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States, OJ L 157 (2003), EU Law IBFD. See also J. John, *New EU Strategy for "Relaunch of the Single Market" – Fresh Start for the CCCTB?*, 22 *Journal of International Taxation* 3, pp. 16-17 (2011), also available at: <http://search.proquest.com>; J. J. Tobin, *CCCTB or Not To Be?*, 40 *Tax Management International Journal* 5, pp. 292-295, also available at: <http://search.proquest.com> (2011).

28. DE: Opinion of Advocate General Léger, 22 Nov. 1994, Case C-279/93 *Finanzamt Köln-Altstadt v. Schmacker* [1995] ECR I-225, at para. 25.

From a graphical perspective, rights that include the freedom of capital transactions as a concept would most appropriately be represented in the form of a sphere. Such a sphere on its own would represent the freedom of capital transactions in its purest state, that is, the unimpaired freedom of capital movements as may exist in modern economic societies.

There are obstacles to such a freedom, graphically presented by section of the sphere with other spheres. The section of spheres vital for this discussion is the interaction of the freedom of capital transactions and (direct) taxation.²⁹ In this sense, a graphical representation of the section of the sphere of capital transactions with the sphere of taxation would correspond to a sphere of lighter and darker areas (figure 1). Lighter tones indicate the resulting sphere's features promoting capital transactions. Darker tones of the sphere correspond to features (partly or fully) inhibiting such transactions.

Figure 1 Sphere of capital transactions



Such a graphical presentation is essential to understanding the premise of this discussion, namely that the reality of *the freedom of capital movements at the level of the European Union is to be found in its essential connection*

29. Such an approach may be considered a type of economic-analysis-of-law approach; on economic analysis of tax harmonization, see D. Dosser, *Economic Analysis of Tax Harmonization*, in *Fiscal Harmonization in Common Markets, Volume I: Theory*, pp. 1-145 (C.S. Shoup (ed.), Columbia University Press, 1967).

to taxation. However, in order to analyse the capital and taxation phenomena existing in the EU market and the underlying policies they imply, it is crucial to understand both the genesis of the resulting collision as well as characteristic of the respective spheres prior to such collision. Therefore, after examining the characteristics of the primary spheres, the resulting system, this light-dark sphere, will be taken as a whole as a subject of this study.

1.1.3. Spheres of capital transactions and taxation – The concept of capital and policies revolving around it

An important terminological premise of this thesis that allows for the parallel approach to capital liberalization and taxation is *the concept of “capital”* as defined in law of the European Union.

In particular, it is possible to discuss the capital-taxation overlap in law of the European Union as a whole because its poles, capital movements and taxation and their policy elements, revolve around this concept. Graphically speaking, the concept of capital is the core of the black-and-white sphere as presented above. Other two key concepts are (*non-*)*discrimination* and (*non-*)*restriction*, which will be commented on with direct reference to the European Court of Justice’s interpretation of these terms.

At the EU level, the concept of capital as set out in article 67 of the Treaty establishing the European Economic Community (EEC Treaty)³⁰ [formerly article 56 of the Treaty, now article 63 of the TFEU] is further specified in Directive 88/361.³¹ Capital in terms of net assets is explained in the IAS.

30. Treaty establishing the European Economic Community (EEC), of 25 Mar. 1957, OJ C 26 (1988), entered into force on 1 Jan. 1958 (EEC Treaty).

31. Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the [EEC] Treaty, OJ L 178 (1988). The Directive was adopted on the basis of arts. 69-70, para. 1, of the EEC Treaty, arts. 67-73 of the EEC Treaty having been replaced by arts. 73b-73g of the EC Treaty, arts. 56-60 of the Treaty, and ultimately by arts. 63-66 of the TFEU. The Directive defines capital movements in a non-exhaustive manner; *see*, inter alia, the judgments AT: ECJ, 16 Mar. 1999, Case C-222/97 *Trummer and Mayer* [1999] ECR I-1661, at para. 21; NL: ECJ, 23 Feb. 2006, Case C-513/03 *van Hilten-van der Heijden*, ECJ Case Law IBFD, at para. 39; UK: ECJ, 12 Dec. 2006, Case C-446/04 *Test Claimants in the FII Group Litigation* [2006] ECR I-11753, ECJ Case Law IBFD, at para. 179; and FI: ECJ, 7 Nov. 2013, Case C-322/11 *K ECLI:EU:C:2013:716*, ECJ Case Law IBFD, at para. 20. The Directive also regulates capital movements in the European Economic Area (EEA). *See* Agreement on the European Economic Area (OJ L 1, of 3 Jan. 1994, p. 3) (EEA Agreement). In this sense, *see also* FR: Opinion of Advocate General Jääskinen, 29 Apr. 2010, Case C-72/09 *Rimbaud* [2010] ECR I-10659, paras. 7, 8 & 26-28.

The concept of capital is put forward in Directives 2009/133 (repealing Directive 90/434), 2003/48 and 2003/49 in the context of direct corporate taxation, as well as substantive law defining a system for tax authority coordination,³² while Directive 2011/96 (repealing Directive 90/435) and Convention 90/436 concern coordination on the subject of double taxation with regard to direct taxation in the sense of designation of Member States' jurisdictions. In the context of indirect taxation, capital is discussed, most significantly for this discussion, in Directives 69/335 and 77/388.³³ This regulation is complemented by interpretation of the concept of capital and capital movements in the case law of the European Court of Justice.

1.1.4. The concept of capital

Generally speaking, the concept of capital may be defined in different manners.³⁴ It can be analysed from *economic (market)*, *regulatory* or *tax perspectives*, each of which differ with regard to goals they promote.

The market and regulatory perspectives on capital define it according to various forms of securities, assets and liabilities in financial markets,³⁵ thus

The provisions of the Directive should, for the purposes of the EEA Agreement, be read in line with Agreement on the European Economic Area - Annex XII - Free movement of capital - List provided for in Art. 40 (OJ L 1, of 3 Jan. 1994, p. 420).

32. Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second para. of Art. 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent, OJ L 26 (1977), EU Law IBFD, and its amendments, concern capital indirectly; they regulate public limited liability companies by means of a corporate statutory law approach.

33. Council Directive 69/335/EEC of 17 July 1969, concerning indirect taxes on the raising of capital, OJ L 249 (1969), Terminated, EU Law IBFD, as amended by Council Directive 74/553/EEC of 7 November 1974 amending Article 5(2) of Directive 69/335/EEC concerning direct taxes on the raising of capital, OJ L 303 (1974), EU Law IBFD. Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes, OJ L 145 (1977), EU Law IBFD. Also, Maydell (2008), *supra* n. 1, at p. 77, at footnote 230. Although value added taxation is not subject of this debate, it is noteworthy to mention its harmonization at the EU level.

34. In economic theory, capital is one of the three factors of production, the others being land and labour. *See*, for example, on the freedom of capital movements, J.M. Keynes, *The Collected Writings of John Maynard Keynes* (30 Volumes), (E. Johnson & D.E. Moggridge (eds.), Macmillan & Cambridge University Press (1971-89), 1989), and N. Naldi, *Keynes on the Nature of Capital: A Note on the Origin of the General Theory's Chapter 16*, 8 European Journal of the History of Economic Thought 3, Routledge, pp. 391-401 (2001), pp. 391-401.

35. For capital in financial markets, for instance, *see* B. Porteous & P. Tapadar, *Economic Capital and Financial Risk Management for Financial Services Firms and Conglomerates*

promoting the *commercial* aspect of capital, which is associated with the objective of *liberalization of capital transactions or maintaining of capital value*.³⁶

If market and regulatory perspectives on capital follow the same basic idea, the tax perspective on capital is different. It focuses on the *value of capital transactions* in a particular jurisdiction and during given time periods for the purposes of tax calculation. Here, the concept of capital depends on whether the relevant taxation is levied directly on the entities paying or receiving capital (direct taxation) such as in case of corporate tax or capital gains tax, or if taxes are collected by an intermediary from the entity who bears the ultimate economic burden of the tax (indirect taxation) such as sales tax or value added tax. One may thus describe the concept of capital for purposes of taxation as looking at taxable value occurring or resulting from (taxable or tax-relevant) transactions. The concept thus combines the transaction-based approach to taxable or tax-relevant transactions with the focus on taxable *values*. This makes the concept of capital for tax purposes straightforward in comparison to its many definitions within capital policy, which is explained by the straightforward economic character of taxes.³⁷

Since this account comments also on the accounting standards, it is useful to underline that in terms of *financial reporting*, capital can be divided into physical³⁸ or financial capital.³⁹ There are two consequential concepts of capital that an entity may adopt according to its needs and for purposes of balance sheet compilations.⁴⁰ Under the financial concept, capital “such as invested money or invested purchasing power” is “synonymous with the net assets or equity of the entity”.⁴¹ Under the physical concept, capital “such as operating capability, ... is regarded as productivity capacity of the entity based on, for example, units of output per day”.⁴² Since the choice of two

(Finance and Capital Markets Series, Palgrave Macmillan, 2005), R.E. Bailey, *The Economics of Financial Markets* (Cambridge University Press, 2005), and G. Fuller, *The Law and Practice of International Capital Markets* (Butterworths Law, 2007).

36. Id.

37. B. Ardy & A.M. El-Agraa, *Tax Harmonization*, in The European Union, Economics & Policies, 7th ed., ch. 14, pp. 238-255 (A.M. El-Agraa (ed.), Financial Times Prentice Hall, 2004), pp. 238-239.

38. Inter alia in P. Schreyer, *Capital Stocks, Capital Services and Multi-Factor Productivity Measures*, OECD Economic Studies No. 37, 2003/2, pp. 163-184 (2004), at p. 165.

39. Inter alia defined in International Accounting Standards Board, *International Financial Reporting Standards IFRS 2012 (Red book) 2 volumes*, IFRS Foundation (8 Mar. 2012) (2012) (IFRS).

40. IFRS, *supra* n. 39, paras. F-102-F-103.

41. IFRS, *supra* n. 39, at para. F-102.

42. Id.

concepts depends on the need of the user of financial statements, the financial concept of capital will be adopted if the users of financial statements are primarily concerned with maintenance of nominal invested capital or the purchasing power of invested capital.⁴³ Of interest to this discussion is the financial concept of capital.

Furthermore, *the value and activity measures* for capital movements for the purposes of liberalization and capital for purposes of taxation may not be the same. Should financial reporting and capital evaluation be made for purposes of screening capital movements (sphere of capital policy), such reports will be commercially based, engulfing a large spectre of capital movements. However, financial reporting for purposes of taxation will focus on the selection of taxable transactions,⁴⁴ its value depending on complex (tax) accounting measurements.

1.1.5. Capital policy – Disparities ab initio

The EU capital transactions regime is predominantly based on promoting *capital movements* and the freedom of capital transactions rather than focusing on *value for commercial or taxation purposes*; however, elements of both such policy poles are present, the elements contradicting in certain aspects.

Such combined and somewhat contradictory approach to capital at the EU level is explained by (commercial) capital transaction and taxation rules as used at the level of the European Union having evolved quite separately, each focusing around a different perspective on the capital involved. In contrast to the *multilateral nature of trade agreements* encompassing capital in terms of transactions and capital as a factor of production within international and EU trade, rules on direct taxation are decided either *unilaterally or negotiated bilaterally*.⁴⁵

In addition, while having similar goals and underlying principles such as *reciprocity and non-discrimination*, trade agreements are said to be useful to escape the “Prisoner’s Dilemma”, while tax treaties should prevent

43. IFRS, *supra* n. 39, at para. F-103. The concept of capital maintenance links concepts of capital and profit.

44. See in this sense, CCCTB Directive Proposal 2011, *supra* n. 9, at p. 6.

45. M. Daly, *The WTO and Direct Taxation*, World Trade Organization Discussion Paper No. 9 (2005), pp. 16-17.

aggressive tax planning and tax evasion.⁴⁶ Thus, while *policy on capital transactions and the freedom of capital* is concentrated on (different concepts of) capital, its value enhancement and its *efficient use* (the concept of which may differ with regard to the underlying capital concept selected), *taxation policy* evaluates such movements by defining a value portion charged as a *price for their circulation*⁴⁷ and *redistributes monies* so collected.⁴⁸

Building blocks of the EU capital transactions regime are defined in Directive 88/361, predominantly concentrated around the idea of promotion and liberalization of capital transactions. However, this predominantly *transactions-based* system contains a reference to *assets and liabilities underlying capital transactions*, which urges a reading in combination with IAS and its concepts of assets and liabilities. The baseline capital policy if one may call it so thus contains a combination of two very different approaches to capital which may lead to logical and interpretative inconsistencies.

In addition, definitions of capital and capital transactions contained in different EU legislative sources may vary, which mostly corresponds to different perspectives from which capital is regulated.

While the EU capital transaction legislation may have enrooted inconsistency and various approaches to capital regulation, the European Court of Justice will use the very same terminology for purposes of approaching (very different) questions of (direct) taxation. This makes capital policy at the EU level quite endemic and very complex.

Such a variety of approaches to capital policy may cause differentiation between similar types of capital and capital movements, which may result in different levels of their legal protection. This not only represents a practical problem in transactions involving third-country elements, but also

46. Daly (2005), *supra*, at p. 17 & footnote 49. Inter alia J. Gowa, *Bipolarity, Multipolarity, and Free Trade*, 83 American Political Science Review 4, pp. 1245-1256 (1989), also available at: <http://www.jstor.org/pss/1961667>, argues that the prisoner's dilemma representation does not reflect the most critical aspect of free trade agreements in an anarchic international system, i.e. security externalities.

47. Ardy & El-Agraa (2004), *supra* n. 37, pp. 238-255.

48. According to J. Snell, *Non-Discriminatory Tax Obstacles in Community Law*, 56 International and Comparative Law Quarterly, pp. 339-370 (2007), at p. 357, the concepts of the EU freedom of movement and *taxation* are essentially different; the former conceptualized to ensure *economic efficiency* while the latter concentrated on the idea of *distribution*.

inconsistency with the EU principle of equal treatment in circulation as well as in tax matters.⁴⁹ In the words of Handoll (2006, at page 11, paragraph 73), “categorisation of a given movement as ‘capital’, ‘payments’, ‘goods’ or ‘services’ is no mere academic exercise”, since a different classification results in a “distinct regime with its own personal and substantive spheres of operation, including possible derogations”,⁵⁰ even though within the European Union, the test of whether a national measure is restrictive and justified will essentially be the same regardless of the freedom that the European Court of Justice deems to be predominantly concerned.⁵¹ Clarification of basic terms and premises in relation to EU capital policy is necessary also for another reason: certain authors believe that international tax standards are or should be influenced by the EU law.⁵² If serious developments were to be undertaken in that direction, a clear understanding and a strong systematization within the EU system is essential.

In addition to the contradiction regarding capital policy’s building blocks, there is a difference, at the EU level, between the two sets of rules also with regard to *jurisdiction in terms of power* over the subject matter. Currently, if policies concerning freedom of capital movements and establishment are within the jurisdiction of the European Union and interpreted by the European Court of Justice, jurisdiction with regard to taxation is bifurcated. While indirect taxation is harmonized at the EU level,⁵³ direct taxation in

49. Capital transactions not categorized under the concepts regulated by EU law will not benefit from the EU regime. Similarly, should transactions involving third states and their residents be classified under the freedom of establishment and the free provision of services, such transactions cannot benefit from the protection under those fundamental freedoms, strictly reserved for intra-European Union transactions. Classification under the freedom of establishment or the free movement of capital is thus very important both for circulation and taxation contexts. See, inter alia, M. Dahlberg, *Direct Taxation in Relation to the Freedom of Establishment and the Free Movement of Capital* (EUCOTAX Series on European Taxation Vol. 9, Kluwer Law International, 2005).

50. J. Handoll, *Capital, Payments and Money Laundering in the European Union* (Richmond Law & Tax Ltd, 2006), at p. 11, at para. 73.

51. M. O’Brien, *Case C-452/04, Fidium Finanz AG v. Bundesanstalt für Finanzdienstleistungsaufsicht, judgment of the Court of Justice (Grand Chamber) of 3 October 2006, [2006] ECR I-9521*, 44 Common Market Law Review 5, pp. 1483-1499 (2007) (2007a), at p. 1495.

52. For instance, see Raingeard de la Blétière (2008), *supra* n. 14. Clarification is of great importance in terms of definition of non-discrimination between residents and non-residents; in this sense, M. Lang, *Non-Discrimination, What Does History Teach Us?*,

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