# EU Tax News – July/August 2021

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## *CJEU Developments*

### Belgium – CJEU Referral regarding the tax treatment of the reversal of write-downs on shares after a transfer of seat from Luxembourg to Belgium

In a judgment of 25 June 2021, the Belgian Supreme Court referred a question to the CJEU for a preliminary ruling regarding the tax treatment of the reversal of write-downs on shares after a transfer of seat from Luxembourg to Belgium (*C-414/21*, *VP Capital*).

Prior to the transfer of its registered office, a Luxembourg company booked write-downs on its Dutch shareholding and on a portfolio of shares. Due to a tax loss position, the write-downs could not actually be deducted in Luxembourg. The company moved its registered office to Belgium (without maintaining a permanent establishment in Luxembourg) and reversed the write-downs after the immigration. The Belgian tax authorities, followed by the Court of Appeal of Antwerp in a judgment of 4 September 2018 (no. 2016/AR/2064), refused to exempt the reversal of the write-downs and to file a preliminary ruling to the CJEU.

Upon appeal of the taxpayer, the Belgian Supreme Court judged that the reversal of the write-downs had to be considered as an expressed but unrealized capital gain, which can only be exempted if it is non-distributable is respected (i.e. allocation to a separate liability account not available for distribution). However, a Belgian company which has recorded write-downs on shares in Belgium is not taxed on the reversal of those write-downs, provided that the write-downs had not been previously deducted from its Belgian taxable income, without needing to be non-distributable. According to the taxpayer this difference in treatment constitutes an infringement of the freedom of establishment.

Wondering whether the *Aures Holdings* case (*C-405/18*, 27 February 2020) could be applicable in the present case and taking into account the argument of the taxpayer invoking that this judgment is not compatible with the decision in the *Bevola and Jens W. Trock* case (*C-650/16*) rendered by the Grand Chamber of the CJEU, the Belgian Supreme Court decided to ask the CJEU whether the tax regime described above is in conformity with the freedom of establishment.

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### Belgium – CJEU Judgment on the partial loss of tax advantages resulting from foreign income exempted by a treaty

In a judgment of 15 July 2021 (*C-241/20*), the CJEU ruled that the free movement of workers has been infringed in a case where a Belgian resident individual lost personal tax advantages due to exempt foreign income. The Belgian resident individual earned the majority of his taxable income in Luxembourg in the execution of an employment performed in Luxembourg. The Belgian resident individual enjoyed personal tax advantages in Luxembourg based on Article 24, §4 of the Belgium-Luxembourg double tax treaty, which differ from the Belgian tax reductions that he would have been entitled to if all his income had come from Belgium. The Belgian resident individual also received rental income in respect of an apartment owned by him in Luxembourg. As the Belgian sourced income was too low, the Belgian resident individual lost a large part of the Belgian tax-free amount of that income and other personal tax advantages (such as a tax reduction for long-term savings, that is to say, premiums paid under an individual life insurance contract, and a tax reduction for costs incurred in energy savings).

With this new judgment, the CJEU clarifies its previous case law (cf. case [C-174/18]) in relation to the partial loss of tax advantages resulting from foreign income exempted by a treaty. The fact that the taxpayer does not receive significant income in Belgium is not relevant since Belgium is able to grant the specific tax advantages. It is also of no relevance that Luxembourg grants a tax reduction of which the amount is at least equivalent to the tax advantages lost by the taxpayer in Belgium. Furthermore, the loss of tax advantages due to foreign immovable property income that is exempted (with reservation of progression) based on a double tax treaty is not compatible with the free movement of capital.

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**Spain – AG Opinion on the infringement of the free movement of capital by the obligation to declare foreign assets**

On 15 July 2021, Advocate General (AG) Saugmandsgaard Øe delivered his Opinion in case *C-788/19* , *European Commission vs Spain*, an infringement procedure related to the obligation imposed on tax residents in Spain to declare some of their assets and rights located abroad (obligation fulfilled through the "model 720") and, in particular, to the following consequences associated with a breach of the said obligation: (i) the classification of assets as unjustified capital gains and their inclusion in the general tax base regardless of the date of acquisition of the assets in question, (ii) the imposition of a proportional fine of 150%, and (iii) the imposition of fines of a fixed amount. The AG proposes to the CJEU to partially uphold Spain's appeal, since, in his view, the European Commission has not provided a complete demonstration of the alleged infringement. According to the AG's Opinion, the Spanish provision would infringe the free movement of capital, both in the EU and in the EEA, when applied to new bank accounts (i.e. bank accounts opened after 1 January 2016) that are under the scope of Directive 2011/16 (DAC), but for other types of assets the European Commission have not demonstrated that the application of the contested provisions implies a disproportionate restriction of the free movement of capital.

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## *National Developments*

**Italy – Italian tax authorities tax ruling on dividend withholding tax exemption requirements under the EU-Swiss Agreement**

On 6 August 2021, the Italian tax authorities published an innovative ruling (n. 537/2021) concerning the conditions under which a Swiss company may benefit from the dividend withholding tax exemption under Art. 9 of the EU-Swiss Agreement laying down measures similar to the ones provided for in the EU Parent-Subsidiary Directive and the EU Interest-Royalties Directive.

*The taxpayer's ruling request*

The Applicant - an Italian resident company wholly owned by a Swiss company as from 1 August 2020 – requested from the Italian tax authorities whether its parent company could benefit from the dividend withholding tax exemption provided by Art. 9 of the EU-Swiss Agreement, notwithstanding the fact that the two-year minimum holding period requirement was to have not (yet) been met at the time of the prospective payment of dividends by the Applicant.

The Applicant acknowledged the Italian tax authorities position on the matter – by analogy with their consolidated positions, already taken in the past, with respect to the similar withholding tax exemption provided for in the EU

Parent-Subsidiary Directive – is that the application of the dividend withholding tax exemption directly at source (i.e., at the time of the payment of dividends) cannot be granted before the two-year minimum period has elapsed. In this circumstance, following the CJEU judgment in *Denkavit* (*Joined Cases C-283/94, C-291/94 and C-292/94*), the taxpayer can only request a reimbursement of the withholding tax suffered once the minimum holding period is met. According to the Applicant, however, the abovementioned past position of the Italian tax authorities on the matter should not apply in the case at issue, following from the fact that the Applicant was admitted to the Italian cooperative compliance programme which establishes - consistently with the OECD cooperative compliance framework – an enhanced collaboration between the admitted taxpayer and the Italian tax authorities.

*The Italian tax authorities' ruling*

As a preliminary point, the Italian tax authorities underlined that, in accordance with the Vienna Convention on the interpretation of international treaties, the tax provisions of the EU-Swiss Agreement – having the aim of providing to Swiss parent companies benefits similar to those given to EU parent companies through the EU Parent-Subsidiary Directive - must be interpreted consistently with the mentioned Directive and that, on the basis of the CJEU judgment in *Denkavit: "it is for the Member States to draw up rules for ensuring compliance with this minimum period, in accordance with the procedures laid down in their domestic law"* and that "*on no view are those States obliged under the Directive to grant the advantage immediately on the basis of a unilateral undertaking by the parent company to observe the minimum holding period*".

Following the above, on a general basis, the Italian tax authorities reaffirmed in the ruling under analysis their consolidated position that a parent company receiving dividends (both under the EU Parent-Subsidiary Directive and the EU-Swiss Agreement) can benefit from the dividend withholding tax exemption directly at source only in cases where the holding in the distributing entity has been already maintained for the minimum holding period. The rationale for this is due to the difficulties which the Italian tax authorities would otherwise encounter in activating effective controls on the fulfilment of the requirement on the basis of a mere "commitment" by the receiving parent company.

Notably, however, with specific reference to the ruling's case, the Italian tax authorities upheld the Applicant's argument and acknowledged that the Italian cooperative compliance programme is characterised by the adoption of enhanced forms of communication and cooperation between the Italian tax authorities and taxpayers "*based on mutual reliance*". On this ground, the Italian tax authorities shared the Applicant's view on the possibility for the Swiss parent company to receive the dividend payment without the application of dividend withholding tax, subject to its commitment to fulfil the holding period after the dividend distribution or, in case of failure to meet the two-year holding requirement, to remit to the Italian tax authorities the tax which was not withheld at the time of the dividend payment.

With this ruling, for the first time, the Italian tax authorities have admitted the possibility for a Swiss parent company – which did not yet fulfil the minimum holding period in the distributing domestic entity - to benefit directly at source from the dividend withholding tax exemption given under Art. 9 of the EU-Swiss Agreement, subject to the further condition that the distributing Italian entity is admitted to the Italian cooperative compliance programme. In the opinion of the writers, on the basis of the Italian tax authorities' arguments, the same benefit (but subject to the same above further condition) should also apply to dividend payments under the scope of the EU Parent-Subsidiary Directive and – moreover – to interest payments under the scope of the EU Interest-Royalties Directive.

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**Spain – ATAD transposition act enters into force**

On 11 July 2021, Law 11/2021 ("the Law") on measures to prevent and combat tax fraud, transposing Council Directive (EU) 2016/1164 of 12 July 2016, which lays down rules against tax avoidance practices that directly affect the functioning of the internal market ("ATAD"), entered into force, thereby amending various taxes and gambling regulation. The main measures from an international tax viewpoint are the following:

Exit tax - for those cases where the exit of the entity or asset is to an EEA country (except for Liechtenstein, that does not have a bilateral exchange of information agreement with Spain) the current wording of the corporate income tax law provides for deferral of the payment of exit tax until the date of transfer of the assets and liabilities to third parties. Effective for fiscal years starting on or after 1 January 2021, the Law, in order to adapt the domestic legislation to ATAD, eliminates the option to defer the payment and foresees the possibility to make the payment in installments over five years. Likewise, the Law itself regulates situations that cause the loss of the right to make the payment by installments (for example, transfer of assets to a third State).

Controlled Foreign Company rules (CFC) - effective for fiscal years starting on or after 1 January 2021, the Law adapts the Spanish legislation to ATAD. The main amendments in relation to the CFC rules are:

- CFC rules are to be applied to passive income obtained by foreign permanent establishments, which currently is not included as CFC income.
- The Law abolishes the current exception from applying CFC rules to foreign holding entities that meet certain requirements (i.e. holding entities owning at least a 5% interest in subsidiaries for at least one year, with the purpose to manage and administer such participation having the correspondent human and material resources).
- The Law broadens the categories of passive income.

The current concept of "tax haven" is replaced by "non-cooperative jurisdiction". The Spanish list of tax havens will be replaced by a list of non-cooperative jurisdictions, to be updated periodically based on, among other things, the relevant EU and OECD lists. Jurisdictions that permit tax bases without sufficient economic activity, that lack transparency, that do not exchange information on beneficial ownership, with nil or low taxation, or that facilitate tax fraud (by means of, for example, benefiting non-resident entities with respect to resident entities) will be considered for inclusion in the list of non-cooperative jurisdictions. It is relevant that the new list may include jurisdictions with a Double Tax Agreement in force with Spain. Together with the publication, the Spanish tax authorities have published FAQs clarifying certain aspects of the new legislation.

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**UK – Supreme Court judgment in Test Claimants in the FII Group Litigation v HMRC**

The UK Supreme Court gave judgment on 23 July 2021 ([2021] UKSC 31), for the third time, in the *Franked Investment Income* ("FII") group litigation, commenced in 2003. This concerns the incompatibility with Arts. 49 and 63 TFEU of the UK's imputation system of taxation of UK-resident companies on their foreign dividends received prior to 1 July 2009 (as contrasted with the blanket exemption of domestic dividends), and the remedies for that incompatibility.

The *FII* Group Litigation Order ('GLO') is one of three UK High Court GLOs regarding the UK's pre-July 2009 dividend taxation regime's incompatibility with EU law; it concerns the taxation of foreign dividends from participations conferring at least 10% of the voting power ('non-portfolio' holdings), and the main test claimant is the British & American Tobacco plc group. The other two current GLOs relating to corporate dividend taxation are:

(a) the *CFC and Dividend GLO* (concerning foreign dividends from 'portfolio' holdings, where the UK company holds less than 10% of the voting power), in which the test claimant is the Prudential Assurance group; and
(b) the *Foreign Income Dividends GLO* (concerning the "FIDs" regime introduced in 1994).

Between them, these issues have now been the subject of well over a dozen UK Tax Tribunal and UK High Court decisions, several UK Court of Appeal judgments, four UK Supreme Court judgments and three judgments of the CJEU on preliminary references (Case C-446/04 *FII* of 12 December 2006, C-35/11 *FII* of 13 November 2012, and C-362/12 *FII* of 12 December 2013). Moreover, there was also the earlier *ACT Group Litigation*, which itself was the subject of multiple judgments at all levels up to and including the UK House of Lords (the UK Supreme Court's predecessor court) and the CJEU (Cases C-397/98 and C-410/98 *Metallgesellschaft Ltd v IRC* and *Hoechst AG v IRC* of 8 March 2001). Each UK judgment typically runs to up to 100 pages – sometimes more.

The volume of litigation is explained first by the fact that the amounts of tax at stake are huge – thought to run to £tens of billions going all the way back to 1973 – and second by the fact that the entire UK system of taxation of UK companies' foreign dividends pre-July 2009 is under challenge.

The latest instalment from the UK Supreme Court holds, *inter alia*:

- in favour of the UK tax authorities (HMRC), that where advance corporation tax ("ACT"), levied contrary to EU law, was offset against mainstream corporation tax, requiring reimbursement on grounds of 'premature levy' (see Case C-397/98 *Metallgesellschaft*, para 88), the prematurity falls to be compensated only on a 'simple' basis of interest, not a 'compound' basis;
- in favour of the claimants, that where, under UK law, surplus management expenses were mandatorily offset against corporation tax on foreign dividends on which EU law would otherwise have required double tax relief credits ("DTR credits") to be granted for foreign tax, and UK law did not permit the DTR credits to be carried forward (with the result that they would be wasted), as contrasted with the treatment of UK dividends which were simply exempt, this contravened Arts. 49 and 63 TFEU for the reason in Case C-436/08 *Haribo* at paras 157-159. In these circumstances the remedy required by EU law is:

  (i) the reimbursement (on the basis of Case C-199/82 *San Giorgio*) of tax actually paid in later years as a result of the inability to carry forward the unused DTR credits; and
  (ii) to the extent that the inability to carry forward the unused DTR credits did not result in actual payment of tax, the unused DTR credits must be regarded as remaining available;

- in favour of the claimants, that the shareholder credits available to individual shareholders on payment of dividends did not fall to be set off against, so as to reduce, the amount of unlawfully charged ACT falling to be reimbursed by HMRC;
- in favour of the claimants, that the partial credit available to a US corporate shareholder under the UK/US Double Tax Treaty, on payment of dividends by the UK company sourced from foreign dividends, did not fall to be set off against, so as to reduce, the amount of unlawfully charged ACT falling to be reimbursed by HMRC; and
- in favour of the claimants, that in relation to third country 'non-portfolio' (>10% participation) dividends paid after 30 March 2001, when the UK DTR rules were very significantly amended, the Art.64 TFEU 'standstill' defence (for restrictions existing on 31 December 1993 in respect of movements of capital

involving 'direct investment') ceased to apply. Applying Case *C-302/97* *Konle v Austria*, paras 52-53, and Case *C-446/04* *FII*, paras 190-192 and 196, the standstill could only apply if the legislation had remained unchanged or had been amended to reduce the restrictions. Here, there had been material changes which did not reduce the restrictions. On the contrary, they could result in a significantly increased tax burden.

Unfortunately, this is still not the end of the litigation regarding the UK's pre-July 2009 dividend taxation's incompatibility with EU law. In its previous judgment in November 2020, the UK Supreme Court remitted to the UK High Court certain important issues regarding the statute of limitations; these are still to be heard. Furthermore, in June 2021, a number of important outstanding issues were heard by the UK First-tier Tribunal, on which the Tribunal's decision is awaited; doubtless, these issues will be appealed through the various levels of appeal, so it is likely that this litigation will in due course pass the 20-year mark before it is finally resolved.

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