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ECJ CASES

Germany – A-G Opinion on non-profit organisations: Stauffer case ([C-386/04](#))

Centro di Musicologia Stauffer (Stauffer) is a charitable foundation under Italian law resident in Italy. Stauffer owns business property in Germany and receives rental income. It has neither a branch nor any permanent office space or a subsidiary in Germany. Stauffer objected to its rental income being subject to German Corporate Income Tax (GCIT) in 1997 and argued that a German charitable foundation would not have been subject to GCIT with respect to the rental income.

In her opinion of 15 December 2005, the Advocate-General (A-G) concluded that the fundamental freedoms are applicable to the facts in question since the tax exemption is not a social advantage but a statutory tax exemption. Since Stauffer had no permanent office space in Germany the freedom of establishment was not applicable. The free movement of capital, however, was.

The A-G observed that the differential treatment of resident and non-resident charitable foundations constitutes an unjustified breach of the free movement of capital, but only where Germany recognises the charitable status of the non-resident foundation according to national law. Since the referring court had already determined the charitable status of Stauffer, the A-G considered Stauffer to be comparable with a German charitable foundation. As a result, Stauffer should not be subject to GCIT with respect to the rental income.

The outcome of the case will be especially relevant for foreign pension funds deriving investment income from other Member States sources. If the ECJ rules in favour of Stauffer such pension funds may benefit from tax advantages granted to comparable domestic funds. See EUDTG Newsalert [NA 2005 – 18](#).

-- Caroline Naumburg and Juergen Luedicke, Germany; juergen.luedicke@de.pwc.com

Germany - ECJ Judgement on cross-border legal mergers in Germany: SEVIC Systems AG case ([C-411/03](#))

SEVIC Systems AG (SEVIC) is a company with its seat in Germany. It concluded a merger agreement with Security Vision Concept SA (SVC), a company with its seat in Luxembourg. Under the agreement all assets and liabilities of SVC were transferred to SEVIC and SVC was dissolved without being liquidated. Sec.1(1) of the German Restructuring Act, however, only allows for mergers between companies with their seat in Germany.

In its judgement of 13 December 2005, the ECJ emphasised that any difference in the treatment of companies in relation to whether the merger is of a cross-border or an internal nature constitutes a restriction of the right of establishment within the meaning of Art. 43 and 48 EC, which can be permitted only if it pursues a legitimate objective compatible with the EC Treaty and is justified by imperative reasons in the public interest. Whilst it cannot be excluded that the restriction in question may be justified, it can only be allowed where it is appropriate for ensuring the attainment of the objectives pursued and must not go beyond what is necessary to attain them. To refuse generally, in a Member State, the registration of a merger between a company established in that

State and one established in another is in any case disproportionate. Art. 43 and 48 EC thus preclude registration in the national commercial register of the merger in question from being refused in general in a Member State where one of the two companies is established in another Member State, whereas such registration is possible where the two companies participating in the merger are both established in the territory of the first Member State.

As a result of the ECJ's judgement, Germany can no longer justify its failure to implement the Merger Directive 90/434/EEC (tax) on the grounds that cross-border legal mergers are not possible in Germany. See EU DTG Newsalert [NA 2005 – 17](#).

-- Caroline Naumburg and Juergen Luedicke, Germany; juergen.luedicke@de.pwc.com

Germany: Imputation credit on foreign dividends – A-G Opinion in Meilicke case (C-292/04)

Meilicke was a German resident individual who received dividends from Dutch and Danish companies in the years 1995 through 1997. No imputation credit was granted on the dividends, as the former German imputation system only allowed for an imputation credit on dividends from German companies. The claimants (the heirs of Meilicke) objected to the denial of an imputation credit and argued that this constitutes a breach of the free movement of capital, as it makes the investment in foreign companies less attractive than in German companies.

In his opinion of 10 November 2005, the A-G concluded that, as in the ECJ's judgement in the September 2004 [Manninen](#) case, the granting of an imputation credit only on dividends from domestic companies is an unjustifiable breach of the free movement of capital enshrined in Art. 56 of the EC Treaty. He further opined that the foreign underlying tax actually paid has to be credited.

The A-G went on to give a proposal for a temporal restriction of the forthcoming ECJ judgement. He proposed to limit the effect of the judgment to dividends paid after 6 June 2000 when the ECJ judgement in [Verkooijen](#) was published. This judgement was the first to deal with the free movement of capital and direct taxation. Before this, the implications of the free movement of capital on direct taxes were uncertain. Accordingly, the right to an imputation credit on foreign dividends received after this date remains intact. However, the A-G equally proposed that taxpayers who received dividends before 6 June 2000 and safeguarded their positions before the Meilicke referral was published in the EU Official Journal can still benefit from the judgment.

Apart from the many questions that arise from the Opinion, e.g. why should Germany enjoy preferential treatment compared to Finland who were not granted a temporal restriction in the Manninen judgement on (basically) the same issue, the Opinion gives an indication of how taxpayers are expected to behave if they want to benefit from an ECJ judgement in the future.

If the ECJ follows the Opinion and introduces temporal restrictions on its judgements, it is advisable for taxpayers to safeguard their positions under domestic procedural law in respect of claims based on EC Law before a national referral regarding this very question is published in the Official Journal. See EU DTG Newsalert [NA 2005 – 13](#).

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Italy – ECJ decides on State aid to Italian banks for merger transactions (C-66/02, C-148/04)

The Italian Law n. 461/1998 (the so-called "Legge Ciampi") introduced a tax relief in order to facilitate the restructuring of the Italian banking system by way of mergers between banks and other similar acquisitions. The tax relief mainly consists of the reduction of the income tax rate (IRPEG) from 37/36% to 12.50% for the banks that execute a merger or a similar restructuring transaction. Italian banks utilised the above-mentioned regime from 1998 to 2000.

On 11 December 2001, in Decision [2002/581/EC](#), the European Commission stipulated that the Legge Ciampi constituted State aid which was incompatible with the EC Treaty and it requested that the Italian Government suppress the regulations and recover from the beneficiaries the aid granted, including interest. The Italian Government appealed for a cancellation of the Commission's decision before the ECJ.

On 15 December 2005, the ECJ delivered its judgement in case C-66/02. The ECJ confirmed the preliminary conclusions of the A-G and decided that the tax benefits granted to the Italian banks involved in mergers or acquisitions by Law n. 461/1998 was liable to distort competition. Also, the ECJ affirmed the necessity to proceed to the recovery of the amounts from the final beneficiaries.

On the same day, in a separate but similar case, Case C-148/04, the ECJ affirmed, thus confirming the previous conclusions of the A-G (C-148/04), the incompatibility of the Legge Ciampi with the EC Treaty. In this case, the Italian Bank Unicredito S.p.A. had asked the ECJ to verify the validity of the Commission's Decision 2002/581/EC in C-66/02.

-- Claudio Valz, Italy; claudio.valz@studiopirola.com

Portugal - EC refers Portugal to ECJ over tax treatment of capital gains arising from transfer of immovable property: EC v Portugal case ([C-345/05](#))

The European Commission referred the Portuguese Republic to the ECJ concerning the provision of Article 10(5) of the Personal Income Tax Code ("Código do Imposto sobre o Rendimento das Pessoas Singulares"), which exempts from taxation capital gains arising from the transfer of immovable property intended for the taxable person's own and permanent residence or for that of a member of his family, subject to the condition that the proceeds of the sale of the immovable property are reinvested in the purchase of immovable property situated in the Portuguese territory. The Commission considers that the condition requiring the reinvestment of the proceeds of the sale of such immovable property in other immovable property situated in Portuguese territory clearly constitutes an impediment to the fundamental freedoms guaranteed under Art.18, 39, 43 and 56(1) EC Treaty and under articles 28, 31 and 40 of the EEA Agreement, namely the free movement of persons and capital and the right of establishment.

-- Leendert Verschoor and Jorge Figueiredo, Portugal; jorge.figueiredo@pt.pwc.com

Portugal - Supreme Court asks ECJ for preliminary ruling on stamp tax on increase of capital: Optimus – Telecomunicações S.A. v Portuguese Tax Authorities case ([C-366/05](#))

On 1 July 1984, the increase of capital in cash of a Portuguese company was exempt from stamp tax based on article 145 of the stamp tax table. Decree-Law Nr 322-B/2001 of 14 December 2001, introduced stamp tax on the increase of capital. The taxpayer opposed a payment of stamp tax on a capital increase in 2002. The Supreme Court referred the following questions to the ECJ:

- 1) Should Article 7 (1) of [Directive 69/335/EEC](#) of 17 July 1969, with the wording given by [Directive 85/303/EEC](#) of 10 June 1985 in respect of indirect taxes on capital increases, be interpreted restrictively as to the obligation for Member States to exempt certain transactions when it concerns transactions that under the wording of the Directive before 1985 can be exempt or subject to a reduced rate, and in particular does this mean only the transactions foreseen in Article 4 (2) and Article 8 and that additionally on 1 July 1984 were in such a situation?; and
- 2) Should Article 7 (1) of the same Directive, in relation to indirect taxes on capital increases and Article 10, be interpreted in a way that they prevent taxation of stamp tax based on national legislation, like Decree-Law Nr 322-B/2001 that introduced Nr 26 "Capital Contributions" in the general stamp tax table, in respect of the increase of capital in cash of a joint stock company

under Portuguese law, when on 1 July 1984, such an increase of capital was subject to stamp tax but was however exempted?

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Sweden – Referral to ECJ for discriminatory capital gains deferral provisions on home sales

According to Swedish tax law a resident individual may benefit from a deferral of capital gains tax on the sale of an owner-occupied dwelling if the seller has acquired or intends to acquire a new dwelling in Sweden. The deferral is, however, not granted if the original or replacement dwelling is not situated in Sweden. The Commission considers that this constitutes a restriction for residents of other Member States to emigrate to Sweden and for Swedish residents to emigrate to another Member State. As a consequence, on 16 December 2005, the Commission decided to refer Sweden to the ECJ for these discriminatory deferral rules. The Commission holds that the territorial limitations of the tax relief violate EC Treaty rules on the right of residence, the free movement of workers, the freedom of establishment and the free movement of capital and the corresponding provisions of the EEA Agreement and that the discrimination could not be justified by the need to prevent cross-border tax evasion.

-- Gunnar Andersson, Sweden; gunnar.andersson@se.pwc.com

United Kingdom – ECJ judgement in Marks and Spencer Plc v Halsey case (C-446/03)

On 13 December 2005, the ECJ held that the UK's restricting group relief to losses made by UK resident subsidiaries (or UK permanent establishments) is inconsistent with the EC Treaty freedom of establishment where such losses cannot be used either by carry back, current year relief against other local profits, or carry forward either by the EU (non-UK) subsidiary or another legal person.

The ECJ dismissed the UK's argument that non-UK resident and UK resident subsidiaries were not in comparable tax situations. Regarding justification, the Court accepted that the preservation of allocation of taxing powers between Member States, the prevention of double relief and the risk of tax avoidance where a multinational seeks to offset losses against the highest tax rate profits, taken together allow a Member State generally to deny cross-border loss relief. However, where there is no local loss relief whatsoever, whether by carry back, current relief or carry forward, a denial of cross-border loss relief is disproportionate.

The judgement did not contain a temporal restriction.

It cannot be ruled out that other claimants with fact patterns different from those of Marks & Spencer suffering only a timing disadvantage regarding utilisation of EU foreign subsidiaries' losses might nonetheless have a claim in damages or restitution.

The judgement may have implications for most of the other 17 Member States who have group relief, Organschaft, tax grouping or tax consolidation rules.

Companies and groups who have not so far claimed where subsidiaries' losses cannot be used locally should now do so as soon as possible not only in the UK but also in other Member States, before Member States move to tighten time limits or otherwise constrain claims. Companies with claims not meeting the M&S criteria should not necessarily withdraw them pending clarification of the judgement and a possible wider reading thereof.

The Commission will reissue a paper on cross-border loss relief in 2006 in tandem with their ongoing work with 20 of the 25 Member States on the Common Consolidated Corporate Tax Base. See EUDTG Newsalert [NA 2005 – 16](#).

-- Peter Cussons and Chloe Paterson, United Kingdom; peter.cussons@uk.pwc.com

United Kingdom – CFC: Oral hearing before Grand Chamber of ECJ in Cadbury Schweppes Plc case ([C-196/04](#))

On 13 December 2005, the oral hearing of the Cadbury Schweppes Plc and Cadbury Schweppes Overseas Limited v the Commissioners of Inland Revenue UK CFC (Controlled Foreign Company) case took place before the Grand Chamber of the ECJ. Submissions were made by ten other Member States and the European Commission in addition to the UK and Cadbury.

Counsel for Cadbury submitted that the UK's CFC provisions were a breach of the EC Treaty which could not be objectively justified, and that they are protectionist, anti-competitive and hinder the freedom of establishment. In addition to breaching Articles 43, 48, 49 and 56, they may also breach Article 2 EC regarding competition. As to the breach of the EC Treaty, the attribution of a foreign subsidiary's profits to its UK parent dissuades the establishment of such a subsidiary or subsidiaries in the other Member State. In this case, the Irish subsidiaries of Cadbury (CSTI and CSTS) are fully subject to tax in Ireland (albeit at the 10% IFSC tax rate), where a legitimate corporate income tax regime is in place. The UK CFC rules simply export the UK tax rate to profits realised in other Member States and non EU countries over which the UK may not exercise any taxing right. (This submission appears to assume that as a matter of EC Law, the Bricom Court of Appeal decision viz that an amount equivalent to corporation tax levied on a UK parent in respect of a Dutch subsidiary was not corporation tax on the Dutch subsidiary's profits should not be followed). Moreover, the application of the UK CFC provisions to Cadbury is not neutral, as Cadbury is disadvantaged as compared to a UK parent of a UK subsidiary. In particular, the UK CFC regime does not normally attribute the losses of CFCs to the UK parent but rather ordinarily only attributes profits. In summary, the UK ignores the existence of the Irish tax regime and Cadbury's right to choose to have the relevant companies taxed by Ireland.

Counsel for Cadbury then rehearsed the various exemptions from UK CFC: exempt activities, motive test and de minimis (the quoted subsidiary exemption was apparently not mentioned at this stage). He then went on to address differences of views between Cadbury and the UK Government as to the facts in relation to Cadbury's Irish subsidiaries, CSTS and CSTI. The UK had asserted in its written submissions that CSTS and CSTI do not have any premises in Ireland nor any directors or employees. Counsel for Cadbury stated this was wrong, as CSTS and CSTI share employees, directors and physical premises with another (Irish) company in the Cadbury group.

Such arrangements are expressly approved in the UK CFC exempt activities test. Indeed, Cadbury (with HMRC) appeared before the UK Special Commissioners to request them to give a direction on the facts to the ECJ prior to the oral hearing. The latter declined to do this, but did however issue a statement in which they recorded that Cadbury's Counsel rejected statements by the UK Government that the functions of CSTS and CSTI were wholly internal to the group, that they were established purely for fiscal purposes and not for any broader commercial or economic purpose, and that they were established solely in order to avoid UK tax, and that neither company had any real economic substance, such that the activities of CSTS and CSTI were "entirely surplus to CS's commercial operations and added nothing to those performed in the UK, so that there was no commercial justification for CSTS and CSTI to have made the profits that they did from intra-group lending."

The Special Commissioners, in their note of hearing of 9 December 2005, state (Paragraph 8) "we would summarise the difference (as regards the facts and what inferences flow from them) as essentially that Mr Ghosh is saying that CSTS and CSTI are carrying on a commercial operation and lending money, which, solely for tax reasons, the group chose to do by establishing them as Irish companies and conducting their business in the IFSC centre in Ireland. Mr Ewart, on the other

hand, is saying that CSTS and CSTI are not established for any commercial purpose but solely to avoid UK tax and their activities are entirely superfluous to the group's commercial operations. In other words, because CSTS and CSTI were admittedly established in Ireland for tax purposes".

The Special Commissioners state (Paragraph 9) "we take a natural stance on this difference. Our understanding at the time in finding the facts set out above was closer to Mr Ghosh's understanding than to Mr Ewart's. In particular in describing the business of CSTS and CSTI in paragraph 7 (3) above, we then understood it to be accepted (contrary to Paragraph 50 of the UK's Written Observations) that a commercial operation was carried on by them." The Special Commissioners go on to state (Paragraph 9) "all we wish to do is to emphasise that we have not at this stage found as facts the statements contained in the UK's Written Observations. We accept that the UK has made this clear in Paragraph 42 of the Written Observations but the subsequent references (Paragraphs 48 and 50 of the UK Written Observations) to matters appearing to be common ground, or not in dispute, might suggest to the ECJ that there is more agreement on such matters than there is". Counsel for Cadbury added in his opening submissions that the loss of tax revenue to the UK which the UK CFC regime seeks to counter is not sufficient to justify the resulting breach in EC rights that Cadbury have suffered. He rejects the UK Government's argument that Cadbury is abusing its treaty freedoms, insofar as in the eyes of the UK Government abuse appears simply to be "not being taxed by the UK".

Given the Special Commissioners stance on the facts it is difficult to see how it could be held that Cadbury's Irish Treasury Operations are a "wholly artificial arrangement" (Paragraph 57 of Marks & Spencer judgment). Also, per Counsel, the UK CFC legislation is not sufficiently narrowly tailored and is disproportionate i.e. goes beyond that necessary to achieve any desired policy objective.

Presumably the most likely acceptable underlying policy objectives would be those recently approved in the [M&S judgement](#) viz the allocation of taxing powers coupled with the prevention of tax avoidance.

Counsel made the point that some of the UK exemptions are arbitrary e.g. the excluded countries regulation is subject to unilateral variation by the UK (and, indeed, Ireland was removed in entirety from the list of approved territories in 2002). Counsel concluded that the UK's real complaint was that the Irish IFSC regime effectively amounted to illegal State aid. However, this was a matter which should (and indeed has) been dealt with prospectively through the EU's State aid procedure, rather than via the UK's implementing and maintaining "illegal" legislation (i.e. unenforceable under the European Communities Act 1972, if found to be in breach of the EC Treaty and incapable of objective justification).

UK Government's submissions

Counsel for the UK Government asserted that the Cadbury situation amounted to "trafficking in profits" (referring back to the A-G's Opinion in Marks & Spencer where reference was made to "trafficking in losses"). He asserted that in Cadbury's case what one had was UK profits being disguised as Irish profits. He did however accept that the UK (CFC rules) must not go too far, and that EU groups of companies may consider tax rates when considering the establishment of companies. He went on however to say that businesses of such companies must be genuine and there must be bona fide economic activity in the host state.

Here the Special Commissioners' Paragraph 9 clarification ("we then understood it to be accepted ... that a commercial operation was carried on by them") should be helpful to the ECJ. In conclusion, Counsel for the UK suggested that Member States, when assessing whether an entity is artificial or abusive, should have regard to the level of physical presence in the foreign country i.e. number of employees, the existence of physical premises; the real substance of the business i.e. the experience and the expertise on hand in the company in the foreign country (this appears

to be very similar to the OECD attribution of profits Key Economic Risk Takers or KERTs test); the economic value added by the company and the motive for establishment in the foreign country. Counsel for the UK asserted that the current UK CFC provisions adhere to the above criteria.

Submissions made by Member States and the Commission

Belgium and Ireland, neither of whom have CFC legislation and Spain (which has CFC legislation but which is not applied intra-EU) as well as the Commission supported Cadbury. Belgium and Ireland basically contended that the UK CFC legislation breached the EC Treaty and was incapable of justification. Spain observed that their CFC legislation was not similar to the UK legislation on CFCs. Moreover, a Member State's CFC provisions are EC Treaty compatible if and only if the ECJ finds that such CFC provisions only catch artificial situations (presumably a reference to the wholly artificial arrangement test in Marks & Spencer).

The Commission submitted that Member States may have CFC rules but they cannot do just whatever they like. Similar to Spain, the Commission focused on what is artificial, which should be the target of a Member State's CFC provisions. Provided, therefore, that there was a real business objective/activity undertaken in the subsidiary's Member State, the motive for establishing in that particular Member State becomes totally irrelevant. The Commission observed that the UK seemed to be saying that if something was capable of being done in the UK it must be done in the UK. The Commission then posed the question as to whether the ECJ should either give some indication of elements that should be taken into consideration when assessing artificiality or leave it to the national courts to decide what is wholly artificial. The Commission suggested the former, focusing on the elements suggested by the UK (physical presence, quality of expertise/experience of staff and economic value added – the latter being the least important of the three elements in the Commission's view) but that motive should be wholly irrelevant. The Commission added that in their view, abuse of rights does not arise in the Cadbury case.

Denmark, Finland, France, Germany, Italy, Portugal and Sweden, all having their own CFC regime, supported the UK Government. Germany, however, endorsed the Commission's proposal for the 3 criteria to be adopted by national courts in determining artificiality.

Questions of the ECJ

The representative of the UK was asked "how objective is your application of the motive test, bearing in mind that it is supposed to focus on whether tax avoidance is the sole purpose or one of the main purposes of establishment? For example if there is no doubt that bona fide Treasury/Financial Services are being pursued in Ireland, for the benefit of the group as a whole, what would be the conclusion under the motive test? The representative for the UK, after being asked the question a second time, apparently replied "I am instructed that, from time to time, genuine Treasury/Finance companies pass the motive test. In assessing such companies, we take into consideration premises, personnel, value added and motive."

No date was announced for the delivery date of the A-G's Opinion at the oral hearing.

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(The author gratefully acknowledges the assistance of, in particular, Dorsey and Whitney's London office in relation to what was said at the oral hearing. Any views expressed are, however, those of PwC, who take sole responsibility for the above summary.)

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NATIONAL DEVELOPMENTS

Finland – Finnish Government's response to the ECJ's Marks & Spencer ruling

Soon after the M&S judgement was handed down by the ECJ on 13 December 2005, the Ministry of Finance announced that there was no need for quick amendments to the Finnish legislation. This announcement was much anticipated, as there were concerns about whether the Finnish group contribution system would be abolished completely on short notice. This would have had significant effect on the tax positions of Finnish groups. It still remains unsure however if the M&S judgement will after all have implications for the Finnish group contribution system even before the pending Esab case ([C-231/05](#)) is decided, which is not expected before the end of 2006.

-- Jarno Laaksonen, Finland; Jarno.Laaksonen@fi.pwc.com

Finland – Clarifications relating to tax treatment of European Companies (SE/SCE)

On 16 December 2005, the Finnish Parliament approved new legislation implementing EU [Directive 2005/19/EC](#) on the transfer of the registered office of a European Company ('Societas Europaea') or a European Co-operative Society ('Societas Cooperativa Europaea'). The legislation entered into force on 1 January 2006 and is in accordance with the EU Directive.

-- Jarno Laaksonen, Finland; Jarno.Laaksonen@fi.pwc.com

Ireland - Abolition of capital duty on issue of shares

The Irish Budget Statement on 7 December 2005 included an announcement of the abolition (with immediate effect) of capital duty on issue of shares ([Directive 79/267/EEC](#)). This duty had been reduced to 0.5% in 2005 and has now been abolished, for shares issued on or after 7 December or for other transactions subject to capital duty. Although the main taxpayers actually impacted by the changes are public companies and companies in the regulated sectors with mandatory capital levels, the abolition also improves the attractiveness of Ireland's holding company regime, since it enables Irish holding companies to be established without up-front capital duty costs.

Mary Walsh, Ireland; mary.walsh@ie.pwc.com

Italy – Italian Tax Authorities deem Italian CFC legislation compatible with EU law

On 12 December 2005, by resolution n. 170, the Italian Tax Authorities expressed their opinion in relation to the applicability of the CFC legislation to the International Trading Company (limited liability company governed by Maltese law). The interpretation of the Tax Authorities, notwithstanding the entry of Malta into the EU on 1 May 2004, confirmed the applicability of the CFC legislation to Maltese companies according to the Malta Financial Services Centre Act, the Malta Merchant Shipping Act and the Malta Freeport Act, expressly foreseen by the Italian Law prior to the entry of Malta into the EU, and, furthermore, extended the CFC regime to the International Trading Companies and, in general, to all of the other Maltese companies which benefit from similar tax advantages.

The opinion of the Italian Tax Authorities could be in contrast with Articles 43, 49 and 56 of the EC Treaty (freedom of establishment, freedom to provide services and freedom on the movement of capital within the EU). A referral can be made to the pending Cadbury ([C-196/04](#)) and Vodafone ([C-203/05](#)) cases on this subject.

-- Claudio Valz, Italy; claudio.valz@studiopirola.com

Netherlands – Dutch dividend withholding tax may be abolished gradually in near future

In November 2005, the Dutch State Secretary for Finance Joop Wijn made an interesting statement in the Dutch Parliament about the impact of EC Law on Dutch dividend withholding tax. He announced that he is considering the gradual abolition of dividend withholding tax in the Netherlands in order to attract foreign capital and to meet the requirements imposed by EC Law. The gradual abolition is amongst others inspired by the recent developments in this field: the Fokus Bank case ([E-1/04](#)) and the pending Amurta case ([C-379/05](#)), which has recently been referred to the ECJ by a Dutch Lower Court. It can be concluded from these developments that it is contrary to EC Law to impose a more burdensome taxation on non-resident shareholders as compared to resident shareholders.

Mr. Wijn specifically mentioned foreign pension funds, which does not meet the requirements of the EC Treaty. A Dutch pension fund receiving a dividend from a Dutch resident company is eligible for a refund of Dutch dividend withholding tax, whereas a foreign pension fund receiving the same dividend cannot claim this refund. Mr. Wijn even seems to suggest that he is willing to find a solution for foreign pension funds that are currently in a disadvantageous position because of the Dutch legislation.

Mr Wijn has not published any particular plans yet. It is therefore not clear what exactly will happen and when. The statement is, however, an important signal towards foreign investors about the drive of the Dutch Government to be in line with the developments in the EU. The statements are particularly interesting for foreign pension funds: it follows from these statements that the Ministry of Finance seems to acknowledge that the levy of Dutch dividend withholding tax on distributions to foreign pension funds is in breach of the EC Treaty. In PwC's view it can be taken from these statements that a refund of these taxes should be granted to foreign pension funds that have requested a refund within the applicable statutory limitations. This indicates once more how important it is to safeguard rights by filing (pro forma) refund requests and making sure that statutory limitations do not bar claims for past years.

-- Marcel Jakobsen and Cees Peters, Netherlands; marcel.jakobsen@nl.pwc.com

Netherlands – State Budget 2006 - Abolition of capital duty on issue of shares

Capital contributions to companies with a capital divided into shares are no longer subject to capital duty. The relevant act was abolished per 1 January 2006. Preceding the abolition, the capital duty rate amounted to 0.55%. To the extent that the 5-year claw-back period applying to tax-exempt share-for-share mergers has not expired on 1 January 2006, the claw-back provision shall no longer be invoked.

-- Irma van Scheijndel, Netherlands; irma.van.scheijndel@nl.pwc.com

Netherlands – Lower Court judgement on non-deductible costs related to non-EU participations (case BK-04/01386)

In the Bosal case ([C-168/01](#)) the ECJ has ruled that the Dutch corporate tax provision which excluded financing costs on tax exempt participations to the extent these costs relate to non-resident participations was in breach of EU Law. The ECJ decision only affects costs on EU participations, because it was based on the freedom of establishment (Art. 43 EC). On 1 November 2005, a Dutch Lower Court judged in a case in which the taxpayer claimed deduction of costs made for its US participation and argued that the non-deductibility of these costs is incompatible with the free movement of capital (Art. 56 EC). The taxpayer held an interest of 29.6% in the US company and its control in the company only consisted of using its voting rights connected with the shares.

The Court first established that a participation in the capital of a non-EU company must be regarded as a capital movement as meant in Art. 56, irrespective of the size of the participation owned and including the costs unconditionally connected with the participation. The Court then held that the non-deductibility of the costs restricted the free movement of capital. Nevertheless, the Court was of the opinion that the restriction was allowed under the standstill clause as laid down in Art. 57 (1) EC. The relevant tax provision already existed on 31 December 1993. The fact that the provision had been amended afterwards - the non-deductibility of costs was extended to currency exchange losses - was of no relevance. The taxpayer had not actually suffered currency exchange losses in respect of its US participation, and even if he should have had such losses, the amendment of the tax provision did not affect its main purpose. Also, the Court rejected the taxpayer's argument that the tax provision on the non-deductibility of participation costs was of a general nature and could, therefore, not be regarded as exclusively applying to the specific capital movements as meant in Art. 57 (1) EC. Finally, contrary to the taxpayer, the Court qualified the costs relating to a non-EU participation as a direct investment in the meaning of Art. 57 (1) EC.

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Portugal - State Budget 2006 and changes to thin capitalisation rules

The Portuguese Government has presented its State Budget for the year of 2006, which among other measures saw the introduction of relevant changes to the thin cap rules. The rules currently in force establish that where the indebtedness of a Portuguese taxpayer towards a non-resident entity with whom special relations ("associated enterprise") exist, is deemed excessive (when the debt exceeds twice the equity, i.e. a 2:1 ratio), the interest paid on the part of the debt that is considered to be excessive will not be deductible for the purpose of assessing taxable income.

Based on the changes introduced by the State Budget 2006, the thin capitalisation rules will not be applicable whenever the financing is provided by an entity, which is resident in Portugal or another EU Member State. Although the thin capitalisation rules foresee an exemption of the application of the rules if the company is able to demonstrate that its overall capital structure/indebtedness level has been established at arm's length, which could eventually have been invoked by the Portuguese Authorities to argue that the rules are not discriminatory or that the Portuguese rules are different from the German thin capitalisation rules that were considered to be violating EU law (Lankhorst-Hohorst case, [C-324/00](#)), it has been considered that the rules are violating EU law and as such are changed effectively as of 1 January 2006. For completeness sake, it should be noted that the thin capitalisation rules will always be applicable in case the non-resident entity is resident in a black listed country or territory ("tax havens"), even if it is demonstrated that the overall capital structure/indebtedness level has been established at arm's length.

The Portuguese Government has also proceeded with the transposition of Council Directive [2005/19/EC](#) of 17 February 2005, amending Directive 90/434/EEC (Merger Directive) and Council Directive [2004/56/EC](#) of 16 November 2004, amending Directive 77/799/EEC (Mutual Assistance).

-- Leendert Verschoor and Jorge Figueiredo, Portugal; jorge.figueiredo@pt.pwc.com

Portugal - Amendments of taxation of dividends

The Portuguese Government has recently published Decree-Law 192/2005, dated 7 November 2005, which introduces a single withholding tax rate of 20% on dividends distributed to both resident and non-resident shareholders (currently, the rates are 15% for dividends paid to resident recipients and 25% for dividends distributed to non-resident shareholders). Furthermore, foreign source dividends, like domestic dividends, derived by a resident individual, are also subject to a tax rate of 20%. The taxpayer may however opt to include the dividends in taxable income and treat the 20% as a payment on account of personal income tax. In this case, the foreign dividends are aggregated in taxable income together with other sources of income, in the amount of 50% of the

gross amount received from Portuguese or eligible EU companies, or the full amount if the dividends are stemming from a non-EU country. The new regime applies from 1 January 2006.

-- Leendert Verschoor and Jorge Figueiredo, Portugal; jorge.figueiredo@pt.pwc.com

Spain - Contributions to employment pensions elsewhere in the EU now tax deductible

The Spanish Parliament has enacted Act 22/2005, which introduces a significant amendment to the tax treatment of non-Spanish EU pension schemes in Spain. Contributions to pension schemes managed by institutions for occupational retirement provision that are established in an EU Member State other than Spain shall now be deductible and give rise to a tax credit in the Corporate Income Tax of a Spanish sponsoring undertaking. Additionally, income arisen from such pension schemes shall give rise to a tax allowance in the Personal Income Tax of the beneficiary.

These amendments to the Corporate Income Tax Act and the Personal Income Tax Act follow from the ECJ ruling issued on 3 October 2002 in the Danner case (C-136/00), which stipulates that Art. 49 of the EC Treaty is to be interpreted as precluding the national tax legislation of a EU Member State from restricting or disallowing the deductibility for income tax purposes of contributions to voluntary pension schemes paid to pension providers in other EU Member States, while allowing such contributions to be deductible when they are paid to occupational retirement institutions in that Member State, if that legislation does not at the same time preclude taxation of the pensions paid by the abovementioned pension providers. The amendment is also based on the EU's Communication on the removal of tax obstacles to cross-border employment pension schemes ([COM \(2001\) 214](#)) and Council [Directive 2003/41/EC](#) on the activities and supervision of institutions for occupational retirement provision. See EUDTG Newsalert [NA 2005 – 13](#).

-- R. Mullerat, C. Concha and D. Benito, Spain; carlos.concha.carballido@es.landwellglobal.com

Spain - Amendment to the EU Parent-Subsidiary Directive

Act 22/2005 of the Spanish Parliament, which implements the amendments to the EU Parent-Subsidiary Directive ([2003/123/EC](#)) of 22 December 2003 into Spanish law, passed on 19 November 2005. The most significant feature of the implementation is that its effects are backdated to 1 January 2005, which was the original implementation deadline.

-- R. Mullerat, C. Concha and D. Benito, Spain; carlos.concha.carballido@es.landwellglobal.com

United Kingdom - Overseas Pension Schemes: new Draft Regulations

On 17 November 2005, the UK's HM Revenue & Customs published draft regulations on UK pension schemes regarding categories of country and requirements for overseas pension schemes and recognised overseas pension schemes). These changes are part of the major revision to the UK laws on the taxation of pension schemes consolidating the current 8 different pension regimes into 1 and this overall tax simplification and these changes take effect from 6 April 2006 ("A Day"). The relevant issue is that before A Day, contributions to unapproved pension schemes, including overseas pension schemes, were generally a taxable benefit in kind on the employee but if the employee paid UK income tax on the contribution then the company could seek a UK corporate tax deduction. After 6 April 2006, contributions to such schemes will not be a taxable benefit in kind on employees (but there could be tax if contributions to overseas pension schemes exceeded £215,000 per year) but the company will not be able to get a corporate tax deduction for contributions to non-registered schemes until the benefit is paid from the scheme to the employee, usually at the time of retirement. By contrast, a contribution to a UK registered scheme would be eligible for a corporate tax deduction, to the same extent as other business expenses, at the time it was paid, subject to some special rules spreading tax relief for large increases in contributions. However in certain circumstances an employer can also get a corporate tax deduction in the UK at the time of payment for contributions to a foreign pension scheme. This new system for giving

relief is called "Migrant Member Relief" and replaces a system called "corresponding acceptance" (which gave relief to the employee from the benefit in kind tax).

For the draft regulations see: <http://www.hmrc.gov.uk/pensionschemes/overseasschemes2005.pdf>
-- Tim Sexton and Peter Cussons, United Kingdom; peter.cussons@uk.pwc.com

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EU DEVELOPMENTS

EC welcomes ECJ judgement in Marks and Spencer case

On 13 December 2005, EU Tax Commissioner Kovács welcomed the ECJ ruling in the Marks & Spencer case on cross-border loss relief saying: "Today the Court took a position that is supported by the Commission regarding the application of the principle of freedom of establishment for cross-border loss relief." The Commission is planning to present a Communication on cross-border loss relief to Parliament and Council in the first half of 2006 that will take account of the ECJ ruling.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

EC issues paper on tax policy and EU competitiveness and growth

At the end of October 2005, the Commission published a Communication on the tax priorities for the coming 4 years in support of the EU's revamped Lisbon Strategy. In the field of direct tax, the most significant plans are the Commission's intention to present a formal Proposal for a new Directive on Cross-border loss relief to the European Parliament and the Council in the first half of 2006 taking into account the ECJ ruling in the Marks & Spencer case, and a formal Proposal for an Common Consolidate Corporate Tax Base in 2008. [Click here](#) to view the Communication.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

EU Tax Commissioner Kovács outlines future of EU tax policy

On 8 December 2005, EU Tax Commissioner Kovács gave a speech on the future of EU tax policy at the Meridian Hotel hosted by PricewaterhouseCoopers in London. [Click here](#) for the speech.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

EC consults with business and academics on CCCTB

Meanwhile, on the Common Consolidate Corporate Tax Base (CCCTB), the Commission's CCCTB Working Group held its fifth meeting on 7 and 8 December 2005, which included a one-day consultation with representatives from the academic and business worlds on the work, progress and future programme of the CCCTB Working Group and in particular on general principles, assets and tax depreciation and capital gains on depreciable assets, liabilities, provisions and reserves and taxable income. The sixth meeting of the CCCTB WG is planned for early March 2006. [Click here](#) for more details.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

EU Internal Market Commissioner McCreevy speaks out against tax harmonisation

EU Internal Market Commissioner McCreevy gave a speech to the European Business Initiative on Taxation ([EBIT](#)) in Brussels on 10 November 2005, entitled: "Tax harmonisation? No thanks". In his speech, McCreevy emphatically opposes tax harmonisation in Europe saying that is not on the

agenda, nor that it will be. However, this is not at all in agreement with the Commission's official line and plans to present a proposal for a Common Consolidated Corporate Tax Base to Parliament and Council in 2008. The speech at EBIT has caused a stir inside the EC and even led to an unusual official rebuttal of McCreevy by President Barroso. [Click here](#) for the EBIT speech.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

European Parliament welcomes CCCTB and Home State Taxation

On 13 December 2005, the European Parliament adopted a resolution in which MEPs (Members of European Parliament) welcome the idea of a Common Consolidated Corporate Tax Base (CCCTB) at European level. MEPs believe that the best way forward would be via an EU regulation creating a common tax base and using a method of apportionment among the Member States allowing companies to offset and consolidate their profits and losses globally throughout the EU. Yet, if the necessary unanimity for EU-wide action cannot be found, MEPs believe that the "enhanced coordination mechanism" option in the EU Treaty could be activated to allow some Member States to proceed with the CCCTB project, which would then only apply in the participating countries. MEPs advocate a gradual and - at least initially - optional system. MEPS also welcomed a proposed EC pilot scheme for SMEs on home country taxation to allow them to calculate the taxable revenue of a parent company and all its branches and subsidiaries in other Member States applying the tax rules of the home State. [Click here](#) for the EP resolution.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

EC adopts proposal for a Code of Conduct on Transfer Pricing documentation for associated enterprises in the EU

On 10 November 2005, the Commission adopted a proposal for a code of conduct on transfer pricing documentation for associated enterprises in the EU. The (non-binding) code has been developed on the basis of work in the EU Joint Transfer Pricing Forum and aims to standardise the documentation required from multinational groups by the tax authorities on the pricing of their cross-border intra-group transactions. The documentation would be optional for businesses and cover all group entities resident in the EU, including transactions between group entities resident in the EU and associated enterprises outside the EU. The documentation consists of a so-called "master file", a "blue print" of the company and its transfer pricing system that would be relevant and available to all EU Member States concerned, and "country-specific documentation" for each of the specific Member States concerned with the intra-group transactions, which would only be available to the relevant Member State. The code is expected to improve the quality of the information provided by businesses and taxpayers' compliance with transfer pricing documentation requirements in EU Member States thereby reducing the risk for businesses of double taxation and exposure to documentation-related penalties. At the same time it should lead to increased transparency regarding the group's transfer prices and thus facilitate the work of tax administrations. [Click here](#) for the full text of the proposed code of conduct

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EC publishes research paper on U.S., Canada experience with formulary apportionment and group taxation

The Commission has published a research paper with the title 'Formulary Apportionment and Group Taxation in the EU: Insights from the US and Canada'. Although EU Member States currently do not use formulary methods to distribute a Common Consolidate Tax Base across national boundaries, Canada and the U.S. have extensive experience which the paper suggests can be useful for the design of a potential apportionment system for the EU, the definition of the company group and the definition and scope of the tax base. [Click here](#) for the full report.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

EC publishes report on structures of tax systems in the EU

The Commission has presented the annual joint EC/Eurostat report on 'Structures of the taxation systems in the European Union' including statistics and economic analyses. [Click here](#) for details.

-- Bob van der Made, Belgium; bob.van.der.made@pwc.be

EC publishes working document of workshop on impact of ECJ case law on double taxation conventions between Member States and with third states

As part of an EC workshop with experts entitled "EC Law and Tax Treaties", which was held in July 2005, the Commission has published a working document on the impact of ECJ case law on double taxation conventions concluded between Member States and with third states. [Click here](#) for details.

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EU DIRECT TAX GROUP ACTIVITIES

EU Direct Tax Group and EFRP lodge complaints with the EC on dividend and interest taxation of pension funds

The EU Direct Tax Group of PricewaterhouseCoopers (EUDTG) and the European Federation for Retirement Provision (EFRP) have lodged 26 complaints with the European Commission regarding the discriminatory taxation of dividend and interest payments to foreign pension funds. The complaints concern the legislation of 18 different Member States considered as being in breach of the free movement of capital as laid down in the EC Treaty. The complaints are supported by a comprehensive study that has been prepared by PwC's EU Direct Tax Group. See for further details EUDTG Newsalert [NA 2005 – 15](#).

-- Marcel Jakobsen and Cees Peters, Netherlands; marcel.jakobsen@nl.pwc.com

EU Direct Tax Group launches new website

The EU Direct Tax Group of PricewaterhouseCoopers has launched its new website which can be found at: www.pwc.com/eudirecttax. The website contains useful information on the services the EUDTG provides to clients in the EU and EEA areas and Switzerland and details of local EUDTG contacts. In addition, it contains the latest information on and PwC analyses of ECJ cases and developments, and you can also find information on EBIT, a leading Brussels-based business representation on direct taxation which is facilitated by PwC.

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ABOUT THE EUDTG

The EUDTG is one of PricewaterhouseCoopers' Thought Leadership Initiatives and part of the International Tax Services Network. The EUDTG is a pan-European network of EU tax law experts and provides assistance to organizations, companies and private persons to help them to fully benefit from their rights under EU law. The activities of the EUDTG include organising tailor-made client conferences and seminars, performing EU tax due diligence on clients' tax positions, assisting clients with their (legal) actions against tax authorities and litigation before local courts and the ECJ. EUDTG client serving teams are in place in all 25 EU Member States, most of the EEA countries and Switzerland. See the EUDTG website for more information: www.pwc.com/eudirecttax.

For further information regarding the contents of this newsletter or the EUDTG in general, please contact the EUDTG Secretariat through Marcel Jakobsen (email: marcel.jakobsen@nl.pwc.com; tel.: + 31 10 407 5688).

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