The Tax Disputes and Litigation Review

Editor

Simon Whitehead

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THE TAX DISPUTES AND LITIGATION REVIEW

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THE TAX DISPUTES AND LITIGATION REVIEW

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EDITOR'S PREFACE

The objective of this book is to provide tax professionals involved in disputes with revenue authorities in multiple jurisdictions with an outline of the principal issues arising in those jurisdictions. In this, the first edition, we have concentrated on the key jurisdictions where disputes are likely to occur for multinational businesses.

Each chapter provides an overview of the procedural rules that govern tax appeals and highlights the pitfalls of which taxpayers need to be most aware. Aspects that are particularly relevant to multinationals, such as transfer pricing, are also considered. In particular, we have asked the authors to address an area where we have always found worrying and subtle variations in approach between courts in different jurisdictions, namely the differing ways in which double tax conventions can be interpreted and applied.

Perhaps it is merely a perception from a jurisdiction whose Prime Minister has publicly vilified a multinational for complying with the national tax laws, but tax avoidance seems to have become the new international evil. As such, this book provides an overview of each jurisdiction's anti-avoidance rules and any alternative mechanisms for resolving tax disputes, such as mediation, arbitration or restitution claims.

We have attempted to give readers a flavour of the tax litigation landscape in each jurisdiction. The authors have looked to the future, and have summarised the policies and approaches of the revenue authorities regarding contentious matters, addressing important questions such as how long cases take and situations in which some form of settlement might be available.

We have been lucky to obtain contributions from the leading tax litigation practitioners in their jurisdictions. Many of the authors are members of the EU Tax Group, a collection of independent law firms, of which we are members, involved particularly in challenges to the compatibility of national tax laws with EU and EEA rights. We hope that you will find this book informative and useful.

Finally, I would like to acknowledge the hard work of my colleague Federico Cincotta in the editing and compilation of this book.

Simon Whitehead
Hage Aaronson
London
February 2013

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Chapter 1

TAX APPEALS TO THE EUROPEAN COURT OF JUSTICE

Paul Farmer[1]

I THE EUROPEAN COURT

i Access through national courts

European Union law has primacy over the national law of EU Member States. This applies to both primary EU law, in particular the Treaty on European Union and the Treaty on the Functioning of the European Union ('TFEU'), and secondary law, such as the EU legislation on VAT and excise duties.

For most tax cases involving EU law, access to the Court of Justice of the European Union ('the CJEU') is via the national courts. A tax appeal brought in the national courts of a Member State may raise a question concerning the interpretation of the provisions of EU law. This arises most commonly in cases where a taxpayer claims that national tax provisions are contrary to superior rules of EU law; for example, a claim that a corporation tax provision is contrary to Article 43 TFEU on freedom of establishment, or that a VAT provision is contrary to the EU VAT legislation. National courts, as courts of EU law as well as national law, have the obligation to ensure proper application of EU law in disputes falling within their jurisdiction. Under Article 267 TFEU a lower national court may, where a question of EU law is raised before it, refer the case to the CJEU in order to obtain a preliminary ruling on that question if it considers that it needs to be determined in order for the court to be able to give judgment. A national court may refer the matter to the CJEU at the request of the parties or on its own motion.[2] Lower courts have wide discretion whether to refer, and may do so even where they would otherwise be bound by a decision of a superior national court, including in connection with decisions given in the same proceedings.[3] Moreover, the lower courts' right to refer

1 Paul Farmer is a founding partner at Hage Aaronson.

2 Case C-210/06 *Cartesio* [2008] ECR I-9641, Paragraph 88.

3 Case 146/73, *Rheinmühlen – Düsseldorf v. Einfuhr-Und Vorratsstelle Getreide* [1974] ECR 139.

remains notwithstanding any decision of a superior court quashing a reference that they have made.[4]

Under Paragraph 3 of Article 267 TFEU, a national court against whose decision there is no judicial remedy under national law (i.e., the highest appellant court), is obliged to refer to the CJEU any question concerning the interpretation of EU law that is necessary to enable it to render judgment. Where a national supreme court has a discretion whether to hear an appeal from the lower courts, the supreme court acts as the final court for the purposes of Article 267 TFEU in hearing the application for permission to appeal.

The only cases where the obligation to refer does not apply are where the CJEU has already ruled on the question or on a materially identical question in a similar case, or where the correct application of EU law is so obvious as to leave no scope for any reasonable doubt (*acte clair*).[5] The threshold for *acte clair* is a high one. The national court 'must be convinced that the matter is equally obvious to the courts of the other Member States and to the Court of Justice'.[6]

Where a supreme court fails to make a reference, it may be open to a taxpayer to bring a case in damages in respect of that failure.[7] However, such a case must again be brought in the national courts and will succeed only if it is found that the failure to refer was manifest.

The obligation to refer is imposed on national supreme courts because, in most cases, individual taxpayers do not have direct access to the CJEU. Tax appeals against decisions of national tax authorities must be brought in the national courts using domestic remedies and procedures. It is for the national courts to apply EU law to the facts of the case after, where necessary, seeking guidance from the CJEU. Where they do so, the interpretative guidance given by the CJEU is binding on them.

An order for reference must meet the requirements of Article 267 TFEU. If it does not, the CJEU will lack jurisdiction and will decline to provide a response other than on the question of jurisdiction.[8] An important requirement for Article 267 to be engaged is that the reference must be from a court or tribunal that requires a ruling in order to determine a genuine dispute. Thus, the Court of Justice does not accept references from a body that does not meet the necessary standard of impartiality and independence from the decision maker whose decision is challenged. Under many continental systems, the first level of tax appeals is to a higher administrative authority that is not a court or tribunal for the purposes of Article 267. A reference can only be made when a further appeal is made to the courts.

While the CJEU largely leaves the national court to determine whether it needs a ruling, it will refuse to provide a ruling in extreme cases where the reference manifestly has no relevance to the facts or the dispute is clearly hypothetical.[9] It is nevertheless possible

4 See *Cartesio*, note 2, Paragraphs 88–98.

5 Case 283/81 *CILFIT v. Ministry of Health* [1982] ECR 3415.

6 Ibid, Paragraph 16.

7 Case C-224/01 *Köbler v. Republik Österreich* [2003] ECR I-10239.

8 Case C-516/99 *Walter Schmid* [2002] ECR I-04573.

9 Case 244/80 *Foglia v. Novello* [1981] ECR 3045.

for the Court to rule upon a reference where on the facts EU rights are not engaged at all, provided guidance on the interpretation of EU law is required by the national referring court in order to give its judgment. This will arise, for example, where a national provision applies in both a domestic and an EU context, and the correct interpretation of EU law will inform the interpretation to be given in a domestic context.[10]

The order for referral from the national referring court must be accompanied by sufficient factual and legislative material to enable the Court of Justice to understand the context in which the issue for determination arises. However, it is only in the most extreme cases, where the absence of material would risk rendering the ruling hypothetical, that the Court will reject the order for reference for this reason.[11]

ii The CJEU: composition and procedure

The CJEU comprises a higher court (the Court of Justice) and a lower court (the General Court). Referrals for preliminary rulings from national courts are heard by the Court of Justice. Although not explicitly laid down, in practice there is one judge per EU country. The Court is assisted by eight advocates general whose job is to present non-binding opinions on the cases brought before the Court. The opinions are not binding on the Court, but provide an impartial view intended to assist it in coming to its decision. Each judge and advocate general is appointed for a six-year term, which can be renewed.

A judge and an advocate general are assigned to each case that is referred to the Court of Justice. Cases are dealt with in two phases: a written phase and an oral phase. In the written phase, the parties to the dispute before the national court, any EU Member State and the European Commission all have the right to submit written observations to the Court. There is no right to respond in writing to any submissions. The oral stage is a relatively short public hearing of the case. Depending on the complexity of the case, this can take place before a panel of three, five or 13 judges, or very rarely before the whole court. Those entitled to submit written observations can also appear at the hearing, regardless of whether or not they have in fact lodged written submissions.

Oral submissions before the Court of Justice are expected not to exceed 15 to 20 minutes, although on written application the Court can grant an extension to a maximum time limit of 30 minutes. It is also possible on written application to enable more than one advocate to appear, particularly when representations are to be made on behalf of more than one party, but all submissions must in principle be made within the same 15 to 30 minute time limit. The taxpayer must deliver oral submissions in the language of the case. The order of oral submissions is first the taxpayer, then the Member States in alphabetical order of country name in the language of the country, and finally the Commission. Reply submissions are possible, but are expected to be limited to a few minutes only.

The jurisdiction of the Court of Justice in preliminary ruling cases is limited to providing guidance on the interpretation of EU law. It has no jurisdiction to make findings of fact or national law. Where there are factual disputes or disputes as to the

10 Case C-28/95 *Leur Bloem* [1997] ECR I-04161.

11 Joined Cases C-320/90–322/90 *Telemarsicabruzzo v. Circostel* [1993] ECR I-393.

meaning of national legislation that are material to the Court's ruling, the Court generally endeavours to provide the national court with sufficient guidance to cover the respective positions.

After the hearing, and usually a few months later, the advocate general gives his or her opinion. There is no procedure as such for commenting on opinions. If, however, the advocate general makes a material error in understanding the national legislation or facts, it is possible to alert the Court to the error by writing to the registry, and very exceptionally parties have successfully sought a reopening of the oral procedure. Where such an error occurs, the advocate general may revise the opinion, or where the oral procedure is reopened, give a second opinion.[12] The possibility of alerting the Court to errors is not to be used by the parties as an excuse to seek to argue the case further.

Following the opinion, the judges deliberate on the case and give their judgment. The judgment is a single judgment, if necessary arrived at by majority decision.

The Court's Rules of Procedure,[13] which were substantially revised in 2012, allow the Court considerable flexibility in dealing with cases. It may, for example, dispense with an oral hearing or with the advocate general's opinion, and in very simple cases may simply issue a reasoned order rather than giving a full judgment. If a case follows its normal course, then judgment can be expected within two years of the referral being made by the national court.

iii Proceedings by the Commission

In addition to the preliminary ruling procedure under Article 267 TFEU, it is open to the European Commission to institute proceedings before the Court of Justice for a declaration that a Member State has failed to fulfil its obligations under EU law. These proceedings may also be started by another EU country, although this is comparatively rare. Where the Commission brings such an action, it must follow the procedure set out in Article 258 TFEU. This provides that it must first give the Member State concerned the opportunity to submit its observations on the supposed breach of EU law and, if the Commission is not satisfied, issue a formal reasoned opinion on the matter. If the Member State fails to comply with the opinion within the period laid down by the Commission, the Commission may then institute proceedings before the CJEU.

Where the Court finds that a Member State is in breach of EU law, the latter is obliged to amend its legislation to remedy the situation. If the Member State fails to do so, the Commission may bring a further action against the Member State seeking the imposition of a fine. A judgment of the Court under Article 258 TFEU may also provide the basis for claims by taxpayers through their national courts. However, while in bringing a case the Commission often acts upon complaints received by individual taxpayers or associations of taxpayers,[14] it is not directly concerned with the rights of individual

12 For example, Case C-35/98 *Staatssecretaris van Financiën v. BGM Verkooijen* [2000] ECR I-04071.

13 Official Journal of the EU (29 September 2012) L265/1.

14 The procedure for making such a complaint to the Commission is explained on its website, http://ec.europa.eu. An optional form for that purpose can also be found on the website.

taxpayers. The Commission's concern is purely with the prospective rectification of the national law. Even where the Commission brings a case, it is important for taxpayers to ensure that they make the necessary claims using domestic procedures within the time limits laid down by national law. While Commission action is not a substitute for making a claim using domestic remedies, it may nonetheless be helpful for taxpayers litigating in their national courts.

Commission action is delimited by a letter of formal notice sent by the Commission to the Member State concerned and the reasoned opinion issued by the Commission, which cannot be extended. Subsequent changes in the law thereafter are ignored.[15]

iv Direct access to the General Court

The main tax cases that are brought directly before the CJEU are those in which the taxpayer takes action not against the decisions of national tax authorities but against the Commission in order to seek the annulment of a Commission decision addressed to it or directly affecting it (for example, in the field of fiscal state aid or competition). Such cases are heard first by the General Court. From there, an appeal lies on a point of law to the Court of Justice. Appeals against such a decision must be brought within the two-month time limit laid down by Article 263 TFEU. Care must be taken, because if a litigant fails to bring an action in the General Court that was clearly open to it, there is a risk that it may be unable to challenge the validity of the decision in the course of national proceedings implementing the decision.[16]

II RECENT CJEU CASE LAW ON TAXATION

The numerous judgments that the CJEU gives in tax cases each year are predominantly concerned with the interpretation of the EU VAT and excise duty legislation, and the compatibility of national tax provisions with the Treaty state aid rules and fundamental freedoms.

i VAT

VAT is a largely harmonised tax and unsurprisingly, therefore, accounts for many of the tax cases each year. These tend to concern the interpretation, against a particular factual background, of specific provisions of the principal VAT Directive (2006/112/EC), for example, the provisions on exemptions, definition of taxable persons and economic activity, the right to deduct input VAT, the taxable amount, special schemes such as the scheme for travel agents and so forth.

In interpreting the Directive the Court has regard in particular to the scheme of the Directive and to the aim of fiscal neutrality that underlies it.

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15 For example, Case C-38/10 *European Commission v. Portuguese Republic.*

16 Case C-188/92 *TWD Textilwerke Deggendorf* [1994] ECR I-833. See also Case C-222/04 *Cassa di Risparmio di Firenze* [2006] ECR I-289.

There are, nevertheless, two important general themes in recent VAT case law that merit particular mention:

a First, following its judgment in the field of agriculture in *Emsland-Stärke*,[17] the Court received a series of references from national courts asking about the application of the doctrine of abuse of law in the field of VAT.[18] In those cases, the Court introduced the doctrine into the VAT area and set out the circumstances in which taxpayers' arrangements were to be considered abusive, with the consequence that taxpayers were precluded from relying on the Directive. The Court held that the conditions for abuse were met where:

- notwithstanding the fact that the conditions laid down by the Directive and the national implementing legislation formally applied, the taxpayer's arrangements resulted in a tax advantage contrary to the purpose of the legislation; and
- it was apparent from a number of objective factors that the essential aim of the arrangements was to obtain a tax advantage.

b A second recurring issue is the compatibility of Member States' implementation of the VAT Directive with general principles of EU law, such as legal certainty, proportionality and effectiveness. For example, a number of recent cases have raised the question of whether compliance requirements and the burden of proof imposed on taxpayers are proportionate, and whether the means available to taxpayers or their customers to assert their right to repayment of unlawfully levied taxes provide an effective remedy.[19]

ii State aid

The CJEU has also given judgment in a number of cases concerning fiscal state aid. Of particular note is the 2011 judgment in the *Gibraltar* case.[20] One of the difficult issues in the field of fiscal state aid is to determine whether a tax regime is to be considered as offering advantages selectively to a particular category of undertakings. In the *Gibraltar* case, the Court, overturning the judgment of the General Court, held that rules imposing payroll and business property occupation taxes on companies, although apparently

17 Case C-110/99 *Emsland-Stärke* [2000] ECR I-11569.

18 Case C-255/02 *Halifax* [2006] ECR I-1609; Case C-419/02 *BUPA Hospitals* [2006] ECR I-1685; Case C-223/03 *University of Huddersfield* [2006] ECR I-1751; Case C-103/09 *Weald Leasing* [2010] ECR I-13589; Case C-277/09 *RBS Deutschland Holding* [2010] ECR I-13805.

19 See, for example, Case C-94/10 *Danfoss and Sauer-Danfoss*, judgment of 20 October 2011; Case C-591/10 *Littlewoods Retail and Others*, judgment of 19 July 2012; Case C-588/10 *Kraft Foods Polska*, judgment of 26 January 2012; Case C-107/10 *Eenel Maritsa Iztok and 3AD*, judgment of 12 May 2011; Case C-302/07 *JD Wetherspoon* [2009] ECR I-1467; Case C-499/10 *Vlaamse Oliemaatschappij*, judgment of 21 December 2011.

20 Joined Cases C-106/09 P and C-107/09 P, Appeals by the European Commission against the judgment of the General Court in proceedings brought by the United Kingdom in respect of a state aid decision concerning Gibraltar. See also the judgment of 21 June 2012 in Case C-452/10 P, *BNP Paribas and BNL v. Commission*.