Advocate General finds Portuguese exit tax provisions in breach of the freedom of establishment (Commission v Portugal)

On 28 June 2012, Advocate General Mengozzi delivered his Opinion in the Commission v Portugal case (C-38/10) concerning the compatibility of the Portuguese exit tax provisions with the freedom of establishment provided for in Article 49 of the Treaty on the Functioning of the European Union.

Commission outlines concrete measures to tackle tax fraud and evasion

On 27 June 2012, the Commission issued a Communication on concrete ways to reinforce the fight against tax fraud and tax evasion including in relation to third countries setting out proposals as to how to strengthen existing measures and possible new initiatives for eliminating fraud and evasion in Europe.

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Then AG went on to analyze the arguments of Portugal, which considered that there was no breach of the freedom of establishment from the outset because the same principle and the same taxable events apply irrespective of whether the transfer of the registered office and effective centre of management takes place in Portugal or in another Member State. In that regard, the Portuguese Republic relied on Article 43(2) and (3) of the CIRC which provides that unrealised capital gains relating to assets are taxed, in the light of the market value of those individual assets, each time that the taxable person effects the ‘permanent connection of those assets to purposes other than the activity carried on’, that is to say, where those assets of the company are withdrawn from the taxable-income-generating economic activity which it carried on up to then. Taxation of capital gains is therefore applicable not only where they are effectively realised through a transfer for a consideration, but also in the case of unrealised capital gains whenever, outside the context of a sales transaction or negotiation and therefore without a consideration, assets cease to be connected, for whatever reason, to the exercise of the enterprise’s activity. AG Mengozzi rejected this argument. He considered that the Portuguese Government compares dissimilar situations in order to reject the existence of a difference in treatment as the situation of a company which, whilst transferring its place of management to another Member State, nevertheless carries on its economic activity in full using assets connected to that activity cannot be regarded as objectively similar to the situation of a company which keeps its place of management in Portugal, but whose assets are no longer connected to the taxable economic activity. The taxable event is different in each of these two cases. The effective comparison is that in a pure domestic situation where assets are assigned to the economic activity of a Portuguese company transferring its place of management within Portugal, the capital gains relating to those assets will be taxed only when they have effectively been realized whereas in a cross-border situations, there will be immediate taxation of unrealized gains. Therefore, he concluded that Article 76-A entails a restriction of freedom of establishment.

Top News

Advocate General finds Portuguese exit tax provisions in breach of the freedom of establishment (Commission v Portugal)

On 28 June 2012, Advocate General (AG) Mengozzi delivered his Opinion in the Commission v Portugal case (C-38/10). The case deals with the compatibility of the Portuguese exit tax provisions with the freedom of establishment provided for in Article 49 of the Treaty on the Functioning of the European Union (‘TFEU’). According to Articles 76-A to 76-C of the Portuguese Corporate Income Tax Code (CIRC), the following situations give rise to an immediate taxation of unrealised capital gains:

i) Assets of Portuguese companies transferring their registered office and effective management to another Member State (Article 76-A);
ii) Assets assigned to a Portuguese permanent establishment of a non-resident company in the case of the cessation of that company’s activity in Portuguese territory (Article 76-B); and
iii) Assets transferred out of Portuguese territory assigned to a Portuguese permanent establishment of a non-resident company (Article 76-C).

Regarding the first situation dealt under Article 76-A, AG Mengozzi started as a preliminary step by drawing a parallel with the previous judgment of the CJ in National Grid Indus case (see EU Tax Alert edition no. 99, December 2011). In that regard, it pointed out that, although there are differences in the legal context in the two cases – since the Netherlands applies the incorporation theory whereas Portugal does not – these do not result in different outcomes. This is because the Portuguese Commercial Companies Code authorizes companies governed by Portuguese law to transfer their effective centre of management to another country whilst retaining their legal personality, provided this is permitted by the legislation of that other country.
Regarding possible justifications to this restriction, namely the need to safeguard the balanced allocation of powers of taxation between the Member States, the AG is of the view that the Portuguese provisions are a disproportionate means to achieve that objective. With regard to possible alternative less restrictive measures, he considered that it is up to the Member State concerned to choose alternatives to such restrictive provision. In the AG’s view, regarding the deferral on payment combined with in interest as accepted in National Grid Indus case, he considered that the interest requirement associated with the deferred payment cannot be said to be discriminatory as argued by the Commission. In addition, he also referred to the possibility to combine the provision of a bank guarantee with the option of the deferred recovery of the tax debt. According to the AG, such possibility advanced in the National Grid Indus case seems to be envisaged as one of several possible alternatives and it should not be considered as a systematic requirement as it may have an equally restrictive effect as the immediate payment. In particular, he suggested that a guarantee should only be required if there is a genuine and serious risk of non-recovery of the tax claim and the amount of the required bank guarantee cannot correspond to the amount of the tax claim the payment of which is deferred.

As regards the second situation dealt under Article 76-B, AG Mengozzi reached a similar conclusion considering that, unlike the cross-border situation, the cessation of the activity of the national permanent establishment of a Portuguese company does not give rise to immediate taxation of unrealised capital gains relating to assets transferred to that company. Therefore, also in this case a restriction to the freedom of establishment was found to exist, but the justification was not proportional as, irrespective of the nature and the extent of the assets assigned to the permanent establishment, the cessation of its activity in Portugal gives rise, in all cases, to immediate payment of tax on unrealised capital gains relating to assets linked to that establishment.

Finally regarding the third situation provided in Article 76-C, AG Mengozzi concludes once again that the Portuguese provision constitutes a restriction of the freedom of establishment. Following the Commission’s observations, he once again focuses his analysis on the proportional character of the measure. In particular, he suggests that the argument of proportionality in this case may deserve a different analysis. AG Mengozzi considers that in this case, unlike the case of the transfer of a company’s place of management (first situation) or the cessation of a permanent establishment’s activities (second situation), the option of deferred recovery cannot be made subject to the provision of a bank guarantee, since the Member State in which the permanent establishment continues to be situated still retains fiscal sovereignty over it, even after the transfer of the assets. Consequently, the presence of that permanent establishment in the territory of the Member State ‘of exit’ can, in principle, sufficiently guarantee the recovery of the tax claim.

Commission outlines concrete measures to tackle tax fraud and evasion

On 27 June 2012, the Commission issued a Communication on concrete ways to reinforce the fight against tax fraud and tax evasion including in relation to third countries (COM(2012) 351 final). The Communication makes proposals as to how to strengthen current measures and sets out possible new initiatives for eliminating fraud and evasion in Europe.

The Commission explains that in the current economic climate where Member States need to cut expenditures and raise revenues in order to achieve fiscal consolidation, combating tax fraud and evasion is of higher importance than ever. Substantial amounts are lost from public finances due to tax evasion and avoidance, with the shadow economy estimated to be around one fifth of GDP on average, i.e., EUR 2 trillion. In a globalized economy, measures taken merely at the national level cannot be sufficiently effective; therefore, coordination at the EU level is indispensable.

The Commission has issued the present Communication upon the call of the European Council. The latter asked the Commission, in March 2012, to develop concrete ways to improve the fight against tax fraud and tax evasion.
As to the next steps, the Commission is to start working on developing the ideas set out in the present Communication. Before the end of 2012, it will present an Action Plan on fighting fraud and evasion, with specific measures that could be rapidly developed. In tandem, the Commission will also come forward with its initiative on tax havens and aggressive tax planning.

**State Aid/WTO**

**CJ upholds the General Court’s judgement on capital injections into a public undertaking by the State (EDF)**

On 5 June 2012, the CJ upheld the General Court’s (‘GC’) 2010 judgment annulling the Commission’s decision which declared, without applying the ‘private investor test’, that a waiver of tax claim by the French State in favour of Électricité de France (EDF) constituted State aid (C-124/10 P).

Électricité de France (EDF), which at the material time was a public undertaking wholly owned by the French State, was allowed a reclassification of a debt to the government into capital, together with a partial tax exemption of the debt release resulting in a savings in taxes of nearly EUR 889 million.

In its judgment, the CJ held that a measure is not to be treated as State aid if the aid recipient as a public undertaking could have obtained the same advantage in normal market conditions. Under the ‘private investor test’ it must be determined whether the State, in its capacity as a shareholder and not in the exercise of its public authority, conferred an economic advantage. For this, the Member State must present clear, objective and verifiable evidence of its actions having to be ascribed to its role of shareholder at that time and not retrospectively.

Even though in this case the transfer of debt into capital was facilitated by not having to pay taxes upon the debt release (the amount of which otherwise could have been used for an additional capital injection), the Commission should have verified whether a capital injection was done by France in normal market conditions regardless of the way the capital was provided. The CJ held that under
In its meeting of 22 June 2012, the Council on Economic and Financial Affairs (ECOFIN) discussed the following legislative proposals pending in the area of taxation:

- **Financial Transaction Tax (‘FTT’):** It held a policy debate on the proposed directive on the FTT (see EU Tax Alert edition no. 97, October 2011) on the basis of a Presidency paper suggesting ways forward on this dossier (introduction of an FTT on a step-by-step basis and examination of alternative means of regulating or taxing the financial sector). In the light of the views expressed, the Presidency concluded that support for an FTT as proposed by the Commission was not unanimous. It also noted that a significant number of delegations supported the idea of enhanced cooperation, which would allow a limited number of Member States to proceed amongst themselves. In this regard, the next steps will have to be taken by the incoming Cyprus Presidency.

- **Energy taxation:** It discussed a proposed directive on the taxation of energy products and electricity aimed at restructuring Directive 2003/96/EC on energy taxation (see EU Tax Alert edition no. 92, May 2011). The revision is aimed at bringing energy taxation more closely in line with EU energy and climate change objectives. The Presidency concluded that there was agreement amongst Member States that minimum tax levels should be laid down in the directive, taking as their reference points the energy content and CO2 emission levels of energy products. However, Poland maintained a reservation on calculating the minimum tax levels in the way outlined by the Presidency. The Presidency further concluded that Member States should retain maximum flexibility to determine the structure of their national energy taxes, and that provisions on the principle of proportionality might have to be deleted.
Advocate General opines that the *ne bis in idem* principle of the EU Charter of Fundamental Rights does not preclude the imposition of multiple penalties in national proceedings concerning the evasion of VAT (*Åkerberg*)

On 12 June 2012, Advocate General Cruz Villalón delivered his Opinion in the *Åkerberg* case (C-617/10) concerning the interpretation of the principle of *ne bis in idem* set out in the EU Charter of Fundamental Rights (*Charter*) with regard to Swedish tax procedural rules which allow the accumulation of administrative and criminal penalties in respect of the same tax offence. The case centres around two issues. The first is the determination of whether or not the CJ has jurisdiction to interpret the fundamental rights set out in the Charter in an essentially domestic scenario which involves the enforcement of a VAT claim in national administrative and criminal proceedings. Answering this question requires the interpretation of the term set out in Article 51(1) of the Charter, according to which, the fundamental rights contained in the Charter bind the Member States ‘only when they are implementing Union law’. If the answer to the first question affirms the Court’s jurisdiction, the second issue to be clarified by the Court in this case is the interpretation of the *ne bis in idem* principle included in Article 50 of the Charter, stipulating that ‘No one shall be liable to be tried or punished again in criminal proceedings for an offence for which he or she has already been finally acquitted or convicted within the Union in accordance with the law’. In particular, the second question asks whether such principle excludes the imposition of both administrative and criminal penalties for the same conduct involving the evasion of VAT obligations.

As to the facts of the case, the taxpayer, a self-employed fisherman residing and working in Sweden, failed to provide tax information to the Swedish tax authorities for the fiscal years 2004 and 2005 which resulted in a loss of tax revenue, including VAT, for the Swedish State. In 2007, the tax authorities imposed an administrative fine on the taxpayer on the basis of the Swedish legislation relating to tax assessment, a part of which related to the evasion of VAT obligations.

Further, the Council approved:

- A report to the European Council on tax issues: further to the request the European Council made in March 2012, this report gives an overview of the work within the Council on legislative proposals, such as energy taxation, the Common Consolidated Corporate Tax Base (*CCCTB*), the FTT, the revision of the Savings Tax Directive and negotiating directives for revised Savings Tax Agreements with certain third countries. In addition, the report mentions the proposed amendments to the Interest and Royalties Directive (see EU Tax Alert edition no. 99, December 2011), the adoption of Council conclusions on the future of VAT (see EU Tax Alert edition no. 106, June 2012), adoption of new rules on Administrative Cooperation in relation to Excise Duties, tax coordination within the Code of Conduct Group and possible other areas for future coordination. The report also shows that the Council’s work over recent months has focused on ways to improve the fight against tax evasion and tax fraud.

- A report on tax issues in the framework of the Euro Plus Pact: finance ministers from the signatory countries approved a report in the framework of the Euro Plus Pact (see EU Tax Alert edition no. 91, April 2011). The Euro Plus Pact includes a specific section on the coordination of tax policies, calling for a structured dialogue between the participating Member States. The present report welcomes the work carried out during the Danish Presidency on the Commission’s proposals for a CCCTB, energy taxation and an EU-wide FTT. It calls on the incoming Presidency to carry on this work, with a particular focus on avoidance of harmful tax practices, combating tax fraud and tax evasion, the exchange of best practices and international coordination.

Finally, the Council adopted Conclusions on the Code of Conduct, endorsing a report of the Code of Conduct Group on the progress of its work achieved during the Danish Presidency.
evasion of VAT. The fine subsequently became final. In 2009, the Public Prosecutor initiated criminal proceedings against the taxpayer, pursuant to the Swedish legislation on tax offences, in front of the Haparanda District Court based on the same facts as those that had been subject to the administrative procedure. The District Court stayed the proceedings and referred several questions to the CJ for a preliminary ruling inquiring whether or not the accumulation of administrative and criminal penalties in such a case is in violation of the ne bis in idem principle as set out in Article 50 of the Charter as well as the corresponding right included in Article 4 of Protocol No 7 of the European Convention on Human Rights (‘ECHR’).

As regards the jurisdiction of the CJ, first, the Advocate General pointed out that the Charter defines the ‘implementation of Union law’ as the condition for reviewing Member State actions in the light of the fundamental rights contained therein, which is different from the formulations that had been used by the CJ in the case law before the Charter obtained binding force (‘field of application of Union law’ or ‘scope of Union law’). The Advocate General proposed that all these expressions should be construed uniformly as expressing the common requirement that Union law must have a presence at the origin of the exercise of public authority by the Member State in order for the Member State action to be reviewable under the EU fundamental rights. According to the Advocate General, in the context of the constitutional structure of the Union it is, as a rule, for the Member States to control the acts of their public authorities in the light of their constitutional order and their international obligations. It occurs only as an exception to that main rule that the Union assumes responsibility for enforcing fundamental rights vis-à-vis national authorities. In order for the Union to have such a competence, it is not sufficient for Union law to be at the origin of the exercise of public authority but the Union must have a specific interest in guaranteeing the respect for fundamental rights itself in the case concerned. In the case at hand, the VAT Directive is the piece of Union law, which formed the basis for the imposition of penalties by the Member State. Although this may, in principle, legitimise the transfer of the responsibility of guaranteeing fundamental rights from the Member State to the Union, the specific circumstances of the case do not reinforce such a conclusion. The Swedish system of tax penalties is a general system applicable to infringements of all sorts of tax obligations. It has not been adopted with reference to the VAT Directive let alone in transposition thereof; it serves the enforcement and collection of VAT claims in the same way as that of any other tax claims. Therefore, in the view of the Advocate General, the degree of connection between Union law (i.e. the VAT Directive) and the exercise of public authority of the State is too weak to form a sufficient basis for a clearly identifiable interest on the part of the Union that could justify the assumption of the responsibility by the latter of guaranteeing respect for the ne bis in idem principle. Hence, the Advocate General concluded that the situation at hand did not involve ‘implementation of Union law’. Accordingly, he proposed that the Court declare that it lacked jurisdiction to answer the questions referred by the Swedish court.

However, the Advocate General also proposed an alternative answer regarding the substantive issue if the Court decided that it did have jurisdiction; that issue is whether the ne bis in idem principle in Article 50 of the Charter precludes a Member State from imposing both an administrative and a criminal penalty for the same offence. The Advocate General pointed out that such dual punishment appears to be widespread practice in the Member States. On the other hand, the case law of the European Court of Human Rights excludes the accumulation of administrative and criminal penalties for the same offence on the basis of the ne bis in idem principle as set out in Article 50 of the Charter precludes a Member State from imposing both an administrative and a criminal penalty for the same offence. The Advocate General pointed out that such dual punishment appears to be widespread practice in the Member States. On the other hand, the case law of the European Court of Human Rights excludes the accumulation of administrative and criminal penalties for the same offence on the basis of the ne bis in idem principle as set out in Article 4 of Protocol No 7 of the ECHR (see Zolotukhin v Russia, judgment of 10 February 2009 (No 14939/03, ECHR 2009)). This would suggest that the same interpretation is to be adopted under the Charter having regard to the provision, which prescribes that the rights which are also included in the ECHR will have the same scope and meaning as their equivalents (Article 52(3) Charter). In contrast to this, the Advocate General suggested to interpret Article 50 of the Charter autonomously. He justified this by the fact that Protocol No 7 of the ECHR has not been ratified by several Member States, and other Member States have made reservations.
or declarations relating to Article 4 thereof. This shows that the prohibition of double punishment when applied to administrative sanctions, on the one hand, and criminal penalties, on the other, is actually not part of the common constitutional traditions of the Member States. In such a situation, the level of protection of a right under the Charter granted by the CJ does not have to match the one which prevails under the ECHR based on the case law of the European Court of Human Rights. The independent interpretation of Article 50 of the Charter led the Advocate General to conclude that such provision does not preclude the Member States from bringing criminal proceedings relating to facts in respect of which a final penalty has already been imposed in administrative proceedings, provided that the criminal court is in a position to take into account the prior existence of an administrative penalty for the purposes of mitigating the criminal penalty to be imposed by it. He proposed to leave it up to the Swedish national court to assess whether or not such ‘offsetting’ is permitted under its national law.

Finally, the Advocate General addressed the question whether the requirement developed by the Swedish Supreme Court that in order to disapply a national provision which is incompatible with the Charter the provision of the Charter at hand must be sufficiently clear is contrary to EU law, specifically the principle of primacy and direct effect. He opined that such requirement is not contrary to EU law as long as it does not hinder the national courts in exercising the powers of interpretation and disapplication assigned to them under Union law.

UK court refers preliminary question to the CJ concerning group relief in a consortium of companies (Felixstowe Dock)

On 15 February 2012, the UK First-tier Tribunal (Tax Chamber) referred a question for a preliminary ruling to the CJ in the *Felixstowe Dock* case (C-80/12).

**Facts**

Hutchison Whampoa is a worldwide group of companies headed by Hutchison Whampoa Limited, a Hong Kong resident company. Some of the UK subsidiaries of the group claimed group relief in respect of losses made by one member of the group, Hutchison 3G UK Limited (‘the Surrendering Company’). At the time, the Surrendering Company was owned by a consortium of companies through the intermediate holding company, Hutchison 3G UK Investment Sarl, a company resident in Luxembourg. Under the applicable UK law, in order for the group relief to be available, a link company must exist which in the case at hand is Hutchison 3G UK Investment Sarl. It is further required by the relevant legislation that the link company is itself able to make a relief claim. For that purpose the condition is that the link company should be a UK resident or a non-resident with a UK permanent establishment. Since this requirement was not met in the case of Hutchison 3G UK Investment Sarl, the surrender of the losses by the Surrendering Company was rejected by the UK tax authorities.

In this context, the UK court referred the following question:

‘In circumstances where:

The provisions of a Member State (such as the United Kingdom) provide for a company (a claimant company”) to claim group relief for the losses of a company that is owned by a consortium (a consortium company”) on the condition that a company that is a member of the same group of companies as the claimant company is also a member of the consortium (a “link company”), and

The parent company of the group of companies (not itself being the claimant company, the consortium company or the link company) is not a national of the United Kingdom or any other Member State,

Do Arts. 49 and 54, TFEU preclude the requirement that the “link company” be either resident in the United Kingdom or carrying on a trade in the United Kingdom through a permanent establishment situated there?

If the answer to question 1 is yes, is the United Kingdom required to provide a remedy to the claimant company (for example, by allowing that company to claim relief for the losses of the consortium company) in circumstances where:
German court refers preliminary question to the CJ regarding discriminatory inheritance tax provisions (Welte)

On 18 April 2012, the Finance Court of Düsseldorf referred a question to the CJ for a preliminary ruling in the Welte case (C-181/12) regarding the compatibility with the free movement of capital of German inheritance tax rules which provide for different tax free amounts for residents and non-residents on the inheritance of land. Specifically, the national court asks:

‘Are Articles 56 and 58 of the Treaty establishing the European Community to be interpreted as precluding national legislation of a Member State on the charging of inheritance tax which, where land situated within the country is acquired through inheritance by a non-resident person, provides for a tax-free amount of only EUR 2 000 for the non-resident acquirer, whereas on the acquisition through inheritance a tax-free amount of EUR 500 000 would apply if at the time of the inheritance the deceased person or acquirer had a permanent residence in the Member State concerned?’

Polish court refers preliminary question to the CJ regarding the taxation of dividends paid to third-country investment funds (Emerging Markets Series)

On 23 April 2012, the Regional Administrative Court in Bydgoszcz referred a question to the CJ for a preliminary ruling in the Emerging Markets Series case (C-190/12) asking whether or not national tax rules which exempt dividends paid to investment funds established in a Member State while taxing dividends paid to investment funds resident in a third-country are compatible with the free movement of capital. In particular, the Polish court asks:

‘Does Article 56(1) EC (now Article 63 TFEU) apply to an assessment of the permissibility of the application by a Member State of provisions of national law which draw a distinction between the legal situation of taxable persons in such a way that they grant, as part of a general tax exemption, an exemption from flat-rate corporation tax on

the “link company” has exercised its freedom of establishment but the consortium company and the claimant companies have not exercised any of the freedoms protected by European Law,

the link(s) between the surrendering company and the claimant company consists of companies not all of which are established in the EU/EEA.’

German court refers preliminary questions to the CJ regarding valuation of shares in exchange of share transactions (DMC)

On 3 April 2012, the Finance Court of Hamburg referred questions to the CJ for a preliminary ruling in the DMC case (C-164/12) inquiring about the compatibility of the German rules on the valuation of shares in exchange of shares transactions with the freedom of establishment. In particular, the national court asks:

‘(1) Does Art. 43 of the Treaty establishing the European Community (now Art. 49 of the Treaty on the Functioning of the EU (TFEU)) preclude national legislation under which in case of a contribution of shares by co-entrepreneurs to a company the transferred shares must be valued at fair market value (which results in a capital gain for the contributor) to the extent that Germany at the time of contribution of this benefit in kind is not authorized to tax the gains on the new shares which the contributor receives in exchange for his share contribution?

(2) If the first question is answered in the negative: does Art. 43 of the of the Treaty establishing the European Community (now Art. 49 of the Treaty on the Functioning of the European Union) preclude the national legislation concerned if the contributor has the right to request an interest-free tax deferral of tax due on the realized capital gains, in which case the tax due on the gains may be paid in annual instalments of at least one fifth under the condition that a guarantee is provided for the payment in instalments?’
In case C-421/11, Péter Dávid, a Hungarian contractor, carried out several construction works. In order to be able to perform the activities, Dávid contracted subcontractors. The VAT invoiced by the subcontractors was deducted by Dávid. The Hungarian tax authorities conducted tax audits at the two subcontractors. One subcontractor seemed to have no employees or materials to actually perform the invoiced services and had only copied an invoice from a third party, who also had no employees or adequate materials. The other subcontractor seemed to be in liquidation and there were no persons available to be contacted for further details, nor could the liquidator provide any documents proving that the subcontractor had actually performed services to Dávid. Based on the tax audits at the subcontractors, the tax authorities doubted if actual services, and if so which services and for what price, were supplied to Dávid. Furthermore, the tax authorities argued that Dávid had not taken the required precautions. Consequently, the tax authorities denied the VAT refund.

Mahagében and Dávid went to court and the referring courts stayed the procedures and decided to ask preliminary questions of the CJ. The referring courts inquired if the right to deduct input VAT could be rejected if the taxpayer did not have any other document, than the invoice, proving that the issuer of the invoice owned the goods and supplied or transported the goods to the taxpayer. Furthermore, the question arose whether or not the Hungarian VAT legislation was in conformity with the principle of neutrality and the principle of proportionality if the taxpayer, in order to effectuate its right to deduct input VAT, had to prove that the issuer of an invoice qualified as a taxpayer, that the issuer of the invoice had handled legitimately, that the issuer had bought the goods and that the issuer of the invoice had complied with all its VAT obligations such as filing VAT returns, declaring VAT and actually remitting VAT due.

In its judgment, the CJ declared that the Hungarian VAT practice is not in line with the EU VAT Directive when that practice refuses to taxpayers the right to deduct input VAT relating to services rendered to them, based on the argument that the issuer of the invoice, or one
of its subcontractors, committed irregularities while the tax authorities did not have to prove that the taxpayer, whose right to deduct input VAT is rejected, knew or had to know that its incoming services were part of a fraud by the issuer or another party. Moreover, the CJ ruled that a national practice rejecting the right to deduct input VAT on the ground that the taxpayer did not investigate whether or not the issuer of the invoice actually qualified as taxpayer, owned the goods, could supply the goods and fulfilled all its obligations under the VAT legislation, is not in line with the provisions of the EU VAT Directive. Also not in line with the EU VAT Directive is a national practice that rejects the right to deduct input VAT based on the ground that the taxpayer, reclaiming the input VAT, had no other document, than the invoice, that could prove that the issuer acted legitimately while all other material and formal requirements for a refund for the taxpayer were met.

Time limit of six months for VAT refund requests by non-established taxpayers is mandatory (Elsacom)

On 21 June 2012, the CJ rendered its judgment in the Elsacom case (C-294/11).

Elsacom NV, a Dutch taxpayer, submitted a request for a refund of Italian VAT under the Eighth EU VAT Directive to the Italian tax authorities. The request concerned VAT paid to suppliers by Elsacom NV in 1999 and was submitted on 27 July 2000. The Italian tax authorities denied the request arguing that, based on Article 7(1) of the Eighth EU VAT Directive, the time limit for submitting such refund requests was six months after the year in which the VAT was charged to the taxpayer. Elsacom NV did not agree with this denial and went to the Provincial Court of Rome. The Provincial Court agreed with Elsacom NV and decided that the time limit of six months as mentioned in Article 7(1) of the Eighth EU VAT Directive was not mandatory but indicative. In the second appeal of the Italian tax authorities, the Italian Supreme Court decided to ask the CJ for a preliminary ruling on the question whether or not the time limit of six months provided by the Eighth EU VAT Directive was a mandatory limit or not.

Before the CJ, Elsacom NV first argued that the question referred by the Italian Supreme Court was inadmissible as the provision to be dealt with in the main proceeding was a matter of national law and not EU law. In its judgment, the CJ declared that it is in principle obliged to answer preliminary questions if the questions relate to the interpretation of EU law. As the case at hand deals with the interpretation of Article 7(1) of the Eighth EU VAT Directive, this criterion is met. As for the question in the main proceedings, the CJ considered that an indicative character of the time limit in the Eighth EU VAT Directive would undermine the aim of that Directive, which is the harmonization of the rules for refund of foreign VAT in the EU. If the time limit were only indicative, the Member States could easily still determine their own time limits. Furthermore, it would open the possibility that in Member States that refer in their national legislation only to the indicative rule of the Directive effectively no time limit would be applicable. That would conflict with the principle of legal certainty. Based on these considerations the CJ ruled that the time limit of six months has to be interpreted as being mandatory.

Advocate General opines that destruction of capital goods in view of VAT taxable transactions does not lead to an adjustment of deducted VAT on the acquisition of the goods (TETS Haskovo AD)

On 14 June 2012, Advocate General Kokott delivered her Opinion in the TETS Haskovo AD case (C-234/11).

In 2008, the capital of TETS Haskovo AD, a Bulgarian company, was increased by means of a non-cash contribution. The non-cash contribution included three buildings for energy production, which afterwards, were demolished by the company in 2010. The demolition was part of a plan to reconstruct and modernize a thermal power station on the land. The scrap metal was sold subject to VAT. Before the non-cash contribution, the buildings were owned by Finans inzhenering AD that had deducted tax in respect of the acquisition of the buildings.
In view of the demolition of the buildings, the Bulgarian tax authorities considered that this deduction had to be partially adjusted. Therefore, it issued a tax assessment to TETS Haskovo AD, the legal predecessor of Finans inzhenering AD. The Administrative Court of Varna had doubts whether the adjustment was in line with Articles 185 and 187 of the EU VAT Directive and decided to refer preliminary questions to the CJ.

The Advocate General took the view that an adjustment can be made if the buildings were no longer used for taxed transactions. However, according to the Advocate General, the use of the buildings was still linked to taxed transactions, because the scrap metal salvaged from the demolition was sold subject to VAT. In this regard, the Advocate General deemed it irrelevant that the purchase price of the buildings was higher than the proceeds of the scrap metal.

Moreover, the Advocate General considered that the demolition formed part of the facility’s modernization and ultimately served the purpose of providing VAT taxable energy services. Consequently, the Advocate General opined that an adjustment to the deducted input tax should not be made where the demolition relates to use for VAT taxable purposes. A national provision that provides for an adjustment under such circumstances is, according to the Advocate General, not compatible with the EU VAT Directive.

Advocate General opines that the provision of VAT number of the customer and proof that the customer fulfilled VAT obligations in the Member State of destination cannot be required for exempting intra-Community supplies (VSTR)

On 21 June 2012, Advocate General Cruz Villalón delivered his Opinion in the VSTR case (C-587/10).

A subsidiary of the German company Vogtländische Strasse-, Tief- und Rohrleitungsbau GmbH Rodeswisch (‘VSTR’) sold goods to a US company. The US company arranged for the transport of the goods from Germany to Finland. An EU VAT number was not provided by the US company to VSTR’s subsidiary, instead, the US company gave the number of its Finnish customer. VSTR’s subsidiary treated its supply to the US company as a VAT exempted intra-Community supply as the goods had been transported from Germany to Finland.

The German authorities argued that the VAT exemption did not apply due to the fact that the taxpayer could not produce the VAT number of the customer, the US company. The referring court doubted whether producing a correct VAT number of the customer can be set as a requirement for treating the supply as a VAT exempted intra-Community supply of goods. It therefore asked the CJ for clarification and also took the opportunity to ask the CJ whether or not it was of any importance in this case that the customer was established outside the EU and was not registered anywhere in the EU and whether it was of importance that the supplying taxpayer proved that a VAT return was submitted for the acquisition of the goods in the Member State of arrival.

In his Opinion, the Advocate General clearly concludes that the EU VAT rules preclude Member States from exempting intra-Community supplies only if the supplying taxpayer can produce a VAT identification number of the customer. Furthermore, the Advocate General is of the opinion that the fact that the customer is established outside the EU and is not registered anywhere in the EU does not make any difference in this respect. Moreover, the EU VAT rules does not allow Member States to apply the VAT exemption for intra-Community supplies only if the taxpayer proves that the customer has fulfilled its compliance obligations in the Member State of arrival.

Commission requests UK to stop applying the reduced VAT rate on energy saving materials

The Commission has sent a reasoned opinion (second step of the infringement procedure under Article 258 TFEU) to the UK requesting it to amend its VAT legislation with respect to the applicable VAT rate for the supply and installation of 'energy-saving materials'.
The Commission argues that the UK incorrectly applies a reduced VAT rate for the supply and installation of 'energy-saving materials'. The Commission is of the opinion that the goods and services for which a reduced VAT rate can apply are listed exhaustively in Annex III to the EU VAT Directive. The list does not include 'energy-saving materials', therefore, applying the reduced rate for this category of goods is a breach of EU VAT legislation. The Commission therefore has asked the UK to amend its rules. If the legislation is not brought into compliance within two months, the Commission may refer the matter to the CJ.

Commission requests France to limit the reduced VAT rate to domestic care services

The EU VAT Directive allows Member States to apply a reduced VAT rate to certain domestic care services that aim to provide help and care to young, elderly and needy persons. France however, applies the reduced VAT rate to a broader scope of services which includes, for example, gardening services, home lessons, computer assistance and the services of intermediaries operating in this sector. The Commission argues that such a broad interpretation of domestic care services is not in line with the rules of the EU VAT Directive and therefore, has asked France to amend its rules. The Commission’s request takes the form of a reasoned opinion. If the legislation is not brought into compliance within two months, the Commission may refer the matter to the CJ.

Customs Duties, Excises and other Indirect Taxes

Commission to take UK to the CJ over unpaid amounts of customs duties to EU budget

According to a press release of 21 June 2012, the Commission is taking the UK to the CJ over its refusal to compensate for duties its customs authorities had failed to collect in the past. An amount of GBP 15 million should have been paid to the EU budget.

The origins of the case date back to 2005/2006, when the UK customs authorities allowed imports of fresh garlic from the People’s Republic of China, erroneously stating that it was frozen garlic and subject to significantly lower import duties than fresh garlic. The Commission considers that in failing to collect the correct amount, the UK authorities did not act with all due care. The UK authorities, however, have refused to compensate for the missing amount by claiming that the customs took all necessary actions justified by the case.

The Commission is taking this legal action in order to protect the common EU interest. The Commission points out that fair treatment of all Member States must be ensured. If one Member State fails to deliver on its obligation to collect the common resources of the EU budget, the other Member States are forced to pay more as a result.

Commission calls on Portugal to change its excise duty rules for cigarettes

On 21 June 2012, the Commission officially asked Portugal to change its excise duty rules related to the marketing of cigarettes.
Bulgaria asked to review terms of bilateral agreement with the US

On 21 June 2012, the Commission formally asked Bulgaria to put an end to certain duty and tax relief provisions contained in a bilateral agreement with the US on technical assistance.

Prior to its accession to the EU, Bulgaria concluded a bilateral agreement with the US, which provides for duty and tax-free import of goods financed by US and for goods and services purchased on the Bulgarian market with the funds of the technical assistance programme.

None of the exemptions set out in EU legislation justifies the duty and tax relief applied by Bulgaria under this bilateral agreement. Once it had joined the EU, Bulgaria should have adjusted the terms of the agreement in question or, if that was not possible, should have withdrawn from this agreement.

The request takes the form of a reasoned opinion. If the legislation is not brought into compliance within two months, the Commission may refer the matter to the CJ.

Commission requests Hungary to end the excise duty exemption of pálinka

On 21 June 2012, the Commission requested Hungary to amend its legislation that grants an exemption from excise duty to fruit distillates (pálinka) under certain conditions.

Hungary exempts pálinka from excise duty when it is produced by households or distilleries for personal use, up to a maximum of 50 litres a year. Excise duties for alcohol are harmonised under EU legislation (Directive 92/83/EEC). Under that Directive, Hungary is allowed to grant a 50% reduction of the normal excise rate to pálinka produced by distilleries, for personal use, up to 50 litres a year. The exemption applied by Hungary to the production of pálinka therefore goes beyond what is allowed under EU legislation.

The request takes the form of a reasoned opinion. If the legislation is not brought into compliance within two months, the Commission may refer the matter to the CJ.

In Portugal, a time limit for the sale of cigarettes is laid down, linked to the fiscal stamp on the packaging. Cigarettes cannot be sold any later than three months after the end of the year that they are released for consumption. Under EU law (Directive 2008/118/EC), excise duty on tobacco products must be charged at the rate applicable on the date on which they are released for consumption. There is no provision under EU legislation which allows Member States to add supplementary duty to this release-date tax rate, or to limit the distribution of tobacco products for fiscal reasons. The Portuguese sales-and-marketing prohibition is clearly disproportionate to any fraud-tackling objective. It also runs contrary to the provisions of Directive 2008/118/EC, under which Member States must ensure that tax markings do not create obstacles to the free movement of excise goods.

The Commission's request takes the form of a reasoned opinion. If the rules are not brought into compliance within two months, the Commission may refer the matter to the CJ.
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