European Tax Report
Confédération Fiscale Européenne (CFE)

October - November 2010 / Edition 9

NEWS - DIRECT TAX

Council agrees on administrative cooperation directive

On 7 December 2010, the Ecofin Council reached a political agreement on the draft directive on administrative cooperation (COM(2009)29). The text shall be adopted without further discussion at the forthcoming Ecofin meeting.

Among the most discussed issues were the following:

- Requests for information to other member states will have to specify the identity of the person under investigation and the tax purpose for which the information is sought; these requirements that serve to avoid so-called „fishing expeditions“ (random collection of tax data without particular indications of fraud or evasion), are less strict than the respective OECD criteria.

- Automatic exchange of information will start in 2015 and initially include 5 categories of information.

READ MORE ***(click to open):***

Directive Proposal: EN FR DE

Council press release (7.12.10): EN

Commission requests Czech Republic and Sweden to end discriminatory pensions treatment

On 28 October 2010, the European Commission requested the Czech Republic and Sweden to amend discriminatory provisions with regard to the taxation of pensions.

In the Czech Republic, domestic pension insurance schemes receive a more favourable tax treatment than similar foreign schemes, limiting Czech taxpayers‘ freedom to choose foreign insurance schemes over domestic ones. Under Czech legislation, taxpayers can deduct their pension insurance contributions from their income tax base if contributions are paid to a pension fund established in the Czech Republic. In addition, if an employer, on behalf of its employees, pays into a pension insurance fund established in the Czech Republic, these contributions do not need to be included in the taxpayers‘ income tax base. In contrast, similar contributions paid to a foreign pension scheme are not deductible if paid by the taxpayer and are considered as taxable income if paid by the employer. The Commission considers that this regime is contrary the free movement of workers (Article 45 TFEU), to the freedom of establishment (Article 49 TFEU) and to the freedom to provide services (Article 56 TFEU).

In Sweden, according to the Commission, non-resident pension funds are subject to discriminatory dividends tax rules. Dividends paid to non-resident pension funds are subject to a withholding tax of 15% or 30% in Sweden, depending on whether Sweden has a double tax treaty with the country of establishment of the pension fund. Pension funds established in Sweden, however, are exempt from tax on dividends as well as from corporation tax. They are subject to a 15% tax based on a notional calculation of its profits. As a result of this system, the effective tax rate on Swedish-sourced dividends received by resident pension funds will in most cases be lower than the 15% tax on the gross dividend of non-resident pension funds. The Commission considers this to discriminate against non-resident pension funds and to be contrary to the free movement of capital laid down in Article 63 of the Treaty on the Functioning of the European Union (TFEU).

Both requests take the form of ‚reasoned opinions“ (second stage of an infringement proceeding). In the absence of satisfactory responses within two months, the Commission may refer these member states to the ECJ.

READ MORE ***(click to open):***

Press release: FR DE CS

Commission requests France to review two capping measures

On 28 October 2010, the European Commission has formally requested France to amend its legislation governing its tax shield (bouclier fiscal) and the capping of the solidarity tax on wealth (ISF - impôt de solidarité sur la fortune) in order to bring it into line with EU law, particularly in relation to the free movement of persons, workers and capital. The request takes the form of a reasoned opinion. If France fails to comply with the reasoned opinion within two months, the Commission may refer the matter to the ECJ.

The tax shield is a cap placed on the combined taxes paid by a taxpayer in France which is fixed at 50% of their income, the remaining amount being eligible for a refund. The Commission does not challenge the principle of this capping but objects to the fact that persons who are not resident for tax purposes in France cannot benefit from it, even if they earn most of their income in France and are primarily eligible to pay tax in that country. This limitation contravenes the free movement of persons and workers which is provided for under Articles 21, 45 and 49 TFEU. The same applied for a cap on the ISF to ensure that the total amount of the ISF and income tax combined does not exceed 85% of the tax household's taxable net income of the previous year which only applies to persons domiciled in France.

In addition, the calculation of taxes paid, which calculates the amount equating to 50% and any possible reimbursement, only takes into account the taxes paid in France. This is an obstacle to the free movement of capital provided for in Article 63 of the TFEU since it influences the investment decisions taken by French taxpayers who would, as a consequence, prefer to acquire securities yielding dividends that are taxed in France and included in the tax shield calculation, rather than purchasing equivalent securities for which they would pay tax in another EEA member state and which would not be taken into account in the tax shield calculation in the same way.

READ MORE *(click to open):*

Press release: **EN** **FR** **DE**

Commission asks Belgium to end discriminatory deduction of interest paid and Flemish residents tax reduction

On 28 October 2010, the European Commission has formally asked Belgium to end the discriminatory treatment of non residents working in the Flemish Region and of interest paid to other member states' financial institutions:

Under Belgian legislation, a flat rate tax reduction is granted to residents of the Flemish region. The reduction is not available to residents of another member state, who work in the Flemish region and earn all or virtually all of their income there. The Commission considers that the unequal treatment violates Articles 45 and 49 TFEU.

Furthermore, Belgian legislation authorises the deduction of interest as professional expenses only in so far as it does not exceed an amount corresponding to the market rate. Such deduction however is possible where the interest is paid to Belgian financial institutions. This difference is likely to restrict foreign institutions' freedom to provide services on the Belgian market and therefore, according to the Commission, contravenes Article 56 TFEU. The difference in treatment is also likely to restrict access for customers resident in Belgium to services provided by foreign financial institutions and therefore restricts the free movement of capital (Article 63 TFEU).

Both requests take the form of reasoned opinions, the second step in infringement proceedings and the last step before bringing a case before the ECJ.

READ MORE *(click to open):*

Press release: **EN** **FR** **DE** **NL**

Project on the transfer pricing aspects of intangibles - OECD meets with business commentators

OECD received almost 50 contributions from the public in response to its July 2010 call for comments on the scoping of the new project on the transfer pricing aspects of intangibles (see **European Tax Report 6/2010**, p.5) envisaged for 2011. These were discussed at a meeting the competent OECD working party held with commentators on 9 November 2010. The meeting documents were made publically available. The OECD indicated that it would release on the internet, probably in January 2011, information on the decisions that will be made on the scope of the project. The special session on the transfer pricing aspects of intangibles will start substantive discussions at its next meeting in March 2011 and hopes to be able to release a discussion draft for public comment towards the end of 2013.

READ MORE *(click to open):*

Press release: **EN** **FR**

Meeting documents: **EN**

NEWS - DIRECT TAX

Commission publishes study on emission trading taxation

The 76-page study published on 29 November 2010 examines current national practices with respect to emissions allowances in the EU and the countries with similar cap-and-trade systems. It analyses potential distortions resulting from national practices and identifies the best solutions. It deals with issues such as the tax treatment of allowances allocated for free, that of allowances originated as Clean Development Mechanism or Joint Implementation, and the tax treatment of penalties for non-compliance. It also examines the feasibility of various policy solutions at EU level.

READ MORE ***(click to open):***

Study on tax treatment of ETS allowances: **EN**

Commission refers Denmark, the Netherlands and Spain to ECJ over exit tax rules

On 24 November 2010, the European Commission decided to refer Denmark, the Netherlands and Spain to the Court of Justice for their exit tax on businesses which cease to be tax residents in these countries. Under national tax law in Denmark, the Netherlands and Spain, a business is taxed on its unrealised capital gains if it changes its residence, moves its permanent establishment or transfers its assets to another member state. However, comparable domestic operations are not taxed for unrealised capital gains that may arise.

The Commission considers these provisions to be incompatible with the freedom of establishment (Article 49 TFEU). The Commission had sent a reasoned opinion in March 2010 (see **European Tax Report 3/2010, p.5**) to which these member states did not react. The Commission considers that such taxation serves as a discriminatory penalty on companies wishing to leave these countries or to transfer assets abroad. The rules in question were likely to dissuade companies from exercising their right of freedom of establishment and did therefore constitute a restriction to the freedom of establishment (Article 49 TFEU).

READ MORE ***(click to open):***

Press release: **EN** **FR** **DE** **DA** **ES** **NL**

Commission asks Belgium to put an end to the discriminatory tax treatment of certain income from capital

On 24 November 2010, the European Commission has officially asked Belgium to review its tax system which imposes additional taxes on income from capital (dividends/interest) paid by foreign intermediaries to Belgian residents who invest abroad. Income from capital paid in Belgium to Belgian residents is subject to a withholding tax. This deduction at source means that Belgian residents do not have to mention these dividends and interest in their annual personal income tax declarations and are exonerated from further taxation. Income from capital paid abroad to Belgian residents must, however, be mentioned in their annual personal income tax declarations. Such income is taxed at a rate identical to that of the withholding tax which exonerates interest and dividends paid in Belgium from having to be declared. However, these revenues are subject to additional taxation. As a result, Belgian residents who invest abroad are taxed at a higher rate than those who invest in Belgium.

The Commission considers Belgium to be in breach of its obligations under Article 63 TFEU (free movement of capital) and Article 40 of the Agreement on the European Economic Area. Belgian legislation also allows Belgian residents to avoid this additional taxation by calling on the services of Belgian intermediaries only. This possibility is contrary to the principle of the freedom to provide services guaranteed by Article 56 TFEU.

The request takes the form of a reasoned opinion (the second step in EU infringement procedures). If no satisfactory response is provided within two months, the Commission may bring this matter before the EU Court of Justice.

READ MORE ***(click to open):***

Press release: **EN** **FR** **DE** **NL**

NEWS - DIRECT TAX

Commission refers Belgium to Court over discriminatory treatment of pension savings contributions

On 24 November 2010, the Commission referred Belgium to the EU Court of Justice as under Belgian income tax law, payments to individual pension accounts, collective pension accounts and insured savings only qualify for tax relief if they are paid in Belgium. Belgian authorities claim that this restriction is necessary to protect the security of the sums paid by the pension savers. The Commission considers this restriction to be disproportionate and discriminatory and therefore contravene EU rules on the freedom to provide services and the free movement of capital (Articles 56 and 63 TFEU). According to the Commission, EU legislation on mutual assistance and on life insurance should be sufficient to ensure that Belgians benefit from the same level of security whether they invest in domestic or foreign funds. The Belgian legislation acts as a deterrent to Belgian taxpayers accessing pension funds in other Member States and goes against the fundamental EU principles of the freedom to provide services and the free movement of capital. The Commission had sent a reasoned opinion to Belgium in March 2010 (see **European Tax Report 3/2010**, p.4).

READ MORE *(click to open):*

Press release: **EN** **FR** **DE** **NL**

NEWS - INDIRECT TAX

Commission presents green paper on the future of VAT

On 1 December 2010, the Commission presented its “Green paper on the future of VAT”, opening a public consultation (until 31 May 2011) which covers a large number of VAT-related issues with the aim of reducing the complexity of VAT rules and modernising VAT collection. Those issues are dealt with in 32 specific questions with room to address any other VAT-related improvement suggestions.

The Commission estimates that almost 60 % of the total administrative effort of undertakings is caused by VAT rules. Reasons for this were the different treatment of domestic and cross-border transactions and the multitude of member state options. In particular, the Commission would like to see a lower number of VAT exemptions and reduced rates, stating that presently, only two thirds of the total consumption was taxed at the standard rate. The VAT gap, the difference between the VAT that should be paid and the amount actually collected was 12%. This was mainly lost to fraud.

A VAT reform has been recommended in the Monti Report of May 2010 (see a summary in **European Tax Report 5/2010**. p.5) and also addressed in the Commission´s Single Market Act of 27 October 2010 (see this issue of the European Tax Report).

Place of taxation of cross-border transactions

As the Commission explains, the original idea of European VAT had been that in the long term, intra-community trade should be taxed in the country of origin. This idea had not been feasible in the past as it required further harmonisation of tax rates to avoid distortions of competition. The Commission observes that there has been some degree of approximation of VAT rates and technological development has enabled a clearing system that would guarantee that the revenues would be transferred to the country of consumption. On the other hand, exceptions have been introduced that deviate from the original idea of taxation in the supplier´s country of establishment, namely for services electronically provided from non-EU countries to consumers, for gas and electricity and for services.

Alternatively, a general reverse-charge mechanism could be introduced.

Tax exemptions and reduced rates

A reduction of VAT exemptions to broaden the tax base rather than increasing tax rates is discussed, in particular where historical exemptions are no longer valid thanks to technological progress. The Commission considers that the exemption of public bodies from VAT is likely to hinder outsourcing to private contractors, discussing the possibility of including all economic activities of public bodies in VAT, as a general rule. Other points mentioned concern the position of holding companies, financial, postal and insurance services and transport of persons.

Reduced tax rates were often used to pursue other policy objectives but caused compliance cost for enterprises that operate cross-border. Areas in which reduced VAT rates are applied could be harmonised or abolished. Digital products should not be disadvantaged compared to physical products.

NEWS - INDIRECT TAX

Input VAT deduction

The Commission asks whether the deduction of input VAT should be possible only upon payment and not already upon supply. This would give no liquidity advantage for a late-paying client and would lower VAT losses in case of client insolvency.

Other issues addressed are a one-stop system for the refund of VAT incurred in another member state and the later or partly use of goods for private purposes.

Cutting red tape

The Commission refers to the measures proposed by the Commission itself and by the High-Level Group of Independent Stakeholders on Administrative Burdens (also known as the Stoiber group).

Those were, among others,

- creating a one-stop-shop for all VAT-related questions in the country of establishment which would particularly facilitate B2C supplies;

- fully automated submission of VAT returns and listings;

- extending periods for VAT returns from a monthly or quarterly to a quarterly or annual basis, depending on the size of the undertaking;

- abolishing the annual summarising returns, corrections would then have to be made in the periodical returns;

- abolishing the option to ask for an intra-community acquisitions listing (as the intra-community sales listings and the VAT information exchange system would be sufficient) and no longer imposing the obligation to submit nil-listings on persons who do not make any intra-community supplies;

All High-Level Group suggestions can be found **here** (15 pages).

The Commission considers that a standard VAT return which would be available in all EU languages and optional for enterprises but which member states would have to accept could facilitate VAT reporting. Currently, member states may opt for introducing additional reporting obligations. Such optional obligations could be standardised which could facilitate the development of IT tools that could be used in all member states.

For small enterprises, the Commission sees a disadvantage in the rule that member states may only exempt persons established on their territory from VAT (see also case C-97/09 Schmelz in this issue of the European Tax Report).

For interrelated companies, the Commission addresses a VAT exemption of cross-border supplies.

Improving the collection of VAT through automated data transmission and other means

The Commission considers four different models that would make the collection of VAT more efficient and help fighting VAT fraud:

- The taxable person would instruct his bank to split a given amount he pays into a portion that would be transferred to the tax administration. Such possibility could be optional, protecting the customer who opts for it from the risk of not being able to deduct his input VAT in case his supplier is a VAT fraudster. According to ECJ case-law (C-439 and 440/04 Kittel), a customer who should have known about the VAT fraud cannot deduct input VAT.

- Mandatory electronic invoicing for all B2B supplies with automatic transmission of the data to tax authorities.

- The taxable person uploads pre-defined information in an agreed format to a secure data warehouse which can be accessed immediately or at very short notice by the tax authorities.

- The taxable person has his VAT compliance system certified by the tax authorities.

Relation between taxpayers and tax authorities

Although the Commission acknowledges that the organisation of the tax administration is solely the competence of the member states, it proposes the development of optional guidelines on the creation of a “tax partnership” between tax authorities and taxpayers and a system of prior rulings to enhance legal certainty.

Legislative instruments

To minimise irregularities related to the transposition of EU VAT rules, the Commission stresses the advantages of regulations over directives. The Commission could be given the power to take implementing decisions with the approval of the majority of member states, as the current system which requires unanimity in the Council was ineffective and left businesses with too little legal certainty. As an alternative, the Commission offers to publish (non-binding) interpretation guidelines.

NEWS - INDIRECT TAX

The Commission also asks whether it should be able to decide on individual derogations for prevention of tax evasion which would be faster than derogations formally granted by the Council.

READ MORE *(click to open):*

Press release: **EN** **FR** **DE**

VAT Green paper: **BG** **CS** **DE** **EL** **EN** **ES** **FI** **FR** **IT** **HU** **MT** **NL** **PL** **PT** **RO** **SK** **SL**

Related Commission working documents: **EN**

Council debates on VAT exemption of financial services

The Ecofin Council discussed the VAT exemption of insurance and other financial services at its 17 November meeting. Among the Commission´s proposals was a clarification in the definitions of exempt services and an opt-in possibility for VAT for economic operators (not member states). The Council asked the Commission to explore how financial services could become subject to VAT.

READ MORE *(click to open):*

Council press release: **EN** (see page 7 f)

ECJ rules: no VAT exemption for small undertakings established in another member state

On 26 October 2010, the ECJ rendered its decision in the preliminary ruling case C-97/09, Schmelz, which concerned a German national and resident who lets an apartment in Austria. From the income she receives, she would qualify for the small businesses exemption in VAT if she was an Austrian resident. The VAT Directive 2006/112/EC however does not allow member states to grant this exemption for persons not established on their territory. The Austrian court asked whether this was discriminatory and contrary to the fundamental freedoms of the TFEU. The ECJ found that the freedom to provide services (Art.56 TFEU) was lex specialis to the general non-discrimination clause (Art. 18 TFEU). The restriction of the freedom of services contained in the VAT Directive was justified as the aim of the exemption -simplification of rules for small undertakings- could not be reached otherwise.

Already advocate-general Juliane Kokott had pleaded that the current VAT rules could be interpreted in a way consistent with the Treaty, see also **European Tax Report 6/2010**, p-3.

READ MORE *(click to open):*

Text of decision: **EN** **FR** **DE**

Commission refers Ireland to ECJ over reduced VAT rate for horses and greyhounds

On 24 November 2010, the European Commission decided to refer Ireland to the EU's Court of Justice over its application of a 4.8% reduced VAT rate for supplies of horses and greyhounds, a rate not in line with Annex III of the VAT Directive 2006/112/EC. See also **European Tax Report 6/2010**, p.2.

READ MORE *(click to open):*

Press release: **EN** **FR** **DE**

Commission takes France to Court for failing to adjust its system for taxing electricity

On 24 November 2010, the European Commission decided to bring France before the EU Court of Justice for failure to comply with the Directive on the taxation of energy and electricity products (Directive 2003/96/EC). The Commission says France had not responded adequately to a reasoned opinion by the Commission in March 2010 (see **European Tax Report 3/2010**, p.3). The French electricity taxation system allows taxes to vary on a local basis, which means that consumers residing in one municipality do not pay the same taxes as consumers residing in another. Member states were obliged to change such provisions by 1 January 2009.

READ MORE *(click to open):*

Press release: **EN** **FR** **DE**

NEWS - INDIRECT TAX

Commission requests Spain to amend its reduced VAT rates for medical items

On 24 November 2010, the European Commission has formally requested Spain to amend its legislation which allows a reduced VAT rate for general medical equipment, appliances to alleviate animals' physical disabilities and substances used in the production of medicines. The VAT Directive allows member states to apply a reduced VAT rate for medical equipment, aids and other appliances but limits this option to equipment „normally intended to alleviate or treat disability" and which are „for the exclusive personal use of the disabled". Furthermore, the VAT Directive allows a reduced rate to be applied to pharmaceutical products „normally used" for health care, prevention of illnesses and as treatment for medical and veterinary purposes. It does not, however, cover medical substances used in the production of medicines, for which Spain also allows a reduced VAT rate. The Commission emphasizes that the EU legislation on reduced VAT rates must be strictly interpreted and applied, in order to avoid competitive distortions within member states and across the EU. The Commission's request takes the form of a „reasoned opinion" (2nd step of EU infringement proceedings). In the absence of a satisfactory response within two months, the Commission may refer Spain to the Court of Justice.

READ MORE ***(click to open):***

Press release: **EN** **FR** **DE** **ES**

Ecofin Council authorises four member states to apply reverse charge to VAT on mobile phones

On 22 November 2010, the EU Council of Economic and Finance Ministers (Ecofin) allowed Austria, Italy and Germany to shift VAT liability on the customer concerning domestic supplies of mobile phones, integrated circuits and components. This option applies until the end of 2013. An existing option granted previously to the UK was prolonged for the same period.

READ MORE ***(click to open):***

Council press release: **EN**

ADMINISTRATIVE COOPERATION AND FIGHT AGAINST TAX FRAUD

OECD Study on offshore voluntary disclosure

As the number of tax information exchange agreements has increased dramatically in the past year, a number of governments have given their non-compliant taxpayers an opportunity to return to legality through voluntary disclosure. The OECD points out that more than 14 700 taxpayers participated in a recent initiative in the United States, and in Germany more than 20 000 taxpayers made a voluntary disclosure resulting in reported additional revenue in the range of €4 billion (although in the German case, many taxpayers feared being prosecuted as a result of a much-disputed deal in which the German tax administration gained possession of confidential taxpayer data).On 27 October 2010, OECD published a 62-page study showing how 39 countries (all OECD members plus Argentina, China, India, Russia, and South Africa) deal with offshore tax evasion, comparing the case where a taxpayer has made a voluntary disclosure with the case where he has not. Issues addressed are penalties imposed, interest rates charged, risk of criminal prosecution and imprisonment and how voluntary disclosure laws and programs are designed, also from the private client advisers´ point of view.

READ MORE ***(click to open):***

OECD study: **EN**

OTHER EU POLICY

Single Market Act

On 27 October 2010, EU Commissioner Michel Barnier presented the Single Market Act, a package of 50 announced measures to improve the functioning of the EU single market, most of which have been mentioned in earlier documents already. The measures include the further implementation of the Services Directive (point 4), more climate focus on energy taxation (point 8), a proposal for a financial reporting reform (point 14), a CCCTB proposal (point 19) which the Commission intends to present in the first quarter of 2011, the announcement of the VAT green paper (point 20), electronic signatures and authentification

OTHER EU POLICY

(point 22), the evaluation of the current system on recognition of professional qualifications (point 33) and an extension of the instruments of "mutual evaluation", "single point of contact" and the IMI system introduced by the Services Directive and the Recognition of Professional Qualifications Directive to other internal market areas (points 44, 45 and 49).

READ MORE *(click to open):*

Single Market Act: **EN FR DE ES NL IT PT FI EL CS LV MT PL SK SL BG RO**

Press release: **EN FR DE ES NL IT PT FI EL CS LV MT PL SK SL BG RO**

PROFESSIONAL AFFAIRS

Commission refers Spain to ECJ over duty to appoint Spanish fiscal representatives

On 24 November 2010, the European Commission decided to refer Spain to the EU Court of Justice over its tax provisions on the appointment of fiscal representatives. The Commission considers that these rules which require certain non-resident taxpayers to appoint a fiscal representative in Spain result in discriminatory treatment and are contrary to the freedom to provide services as laid down in Article 56 of the Treaty on the Functioning of the EU. The Commission had sent a reasoned opinion to Spain in January 2010 (see **European Tax Report 1/2010**, p.5) to which Spain had not reacted.

Under Spanish law, a number of categories of taxpayers are obliged to appoint a resident tax representative in Spain. These are: foreign pension funds located in another member state but providing pension schemes in Spain, insurance companies from other member states operating in Spain, non-resident companies operating in Spain through a permanent establishment and non-residents who are subject to inheritance and gift tax in Spain.

READ MORE *(click to open):*

Press release: **EN FR DE ES**

IMPRESSUM

CONFEDERATION FISCALE EUROPEENNE

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Layout: Laëtitia Bois, Administrative Assistant