IDENTIFICATION OF THE ABUSE OF TAX LAW (as reflected in the judgment of the EU Court of Justice of 17 December 2015 in case C-419/14 *WebMindLicenses*)

EVIDENCE OF THE ABUSE OF RIGHTS

- Conclusion of EUCJ (in Paragraphs 49 – 50): for the purposes of determining whether a licensing agreement arises from an abuse of rights in a cross-border case, to benefit from the lower VAT rates applicable in another Member State, the facts identified by the tax authorities do not appear decisive in themselves

- How to arrive at the conclusion of the abuse of rights? The application of a GAAR requires from the tax authorities to achieve high-level evidence

- The facts under consideration are as follows:
- the manager and sole shareholder of the licensor company was the creator of that know-how;
- that same person exercised influence or control over the development and exploitation of that know-how and over the supply of the services, which were based on it; and
- management of the financial transactions, staff and technical instruments necessary for the supply of those services was carried out by subcontractors

- How to arrive at the conclusion that the licensing agreement under discussion constituted a wholly artificial arrangement concealing the fact that the services at issue were not actually supplied by the company acquiring the licence, but were in fact supplied by the company granting it?

- Further issues are to be examined as follows:
- whether the establishment of the place of business or fixed establishment of the company acquiring the licence was not genuine;
- whether that company, for the purpose of engaging in the economic activity concerned, did not possess an appropriate structure in terms of premises and human and technical resources; and
- whether it did not engage in that economic activity in its own name and on its own behalf, under its own responsibility and at its own risk

- The effect of the judgment on Hungary: the EUCJ may discipline the Hungarian tax law practice that is simply based on GAARs and refers to poor evidence

- Constitutional background:
- deficit of legality (nullum tribute sine lege): there is poor understanding of the civil law contents of transactions;
- weakness in applying the principle of non-discrimination (prohibition of arbitrariness); and
- failure to apply the principle of non-confiscation (prohibition of non-proportionality)

LACK OF HARMONISATION IN IDENTIFYING TAX LAW ABUSE

- Conclusion of EUCJ (in Paragraph 54): the fact that VAT has been paid in a Member State in accordance with its legislation does not preclude an adjustment by the tax authorities of that tax in the Member State, in which the place where those services have actually been supplied is located

- Identification of abusive practice is possible simultaneously in different Member States – not coordinated?

EXCEPTIONAL OBLIGATION OF THE TAX AUTHORITIES TO COOPERATE WITH EACH OTHER

- Conclusion of EUCJ (in Paragraph 59): Regulation No 904/2010 must be interpreted as meaning that the tax authorities of a Member State, which are examining whether VAT is chargeable in respect of supplies of services that have already been subject to that tax in other Member States are required to send a request for information to the tax authorities of those other Member States when such a request is useful, or even essential, for determining that VAT is chargeable in the first Member State

- Lack of obligation to cooperate:

”… the fact that, both in Article 2(1) of that directive and in Article 5(1) of the administrative cooperation regulation, the Community legislature used the word ‘may’ indicates that, whilst those authorities have the possibility of requesting information from the competent authority of another Member State, such a request does not in any way constitute an obligation. It is for each Member State to assess the specific cases in which information concerning transactions by taxable persons in its territory is lacking and to decide whether those cases justify submitting a request for information to another Member State.“

C- 184/05 *Twoh International*, ECR 2007, p. I-7897, Para. 32

- Lack of individual taxpayer rights that would arise from the secondary EU law on the cooperation of the tax authorities:

”… European Union law, as it results in particular from Directive 77/799 and the fundamental right to be heard, must be interpreted as not conferring on a taxpayer of a Member State either the right to be informed of a request for assistance from that Member State addressed to another Member State, in particular in order to verify the information provided by that taxpayer in his income tax return, or the right to take part in formulating the request addressed to the requested Member State, or the right to take part in examinations of witnesses organised by the requested Member State.“

C-276/12 *Sabou*, ECR 2013, p. I-00000, Para. 46

- Developing international cooperation of the tax authorities that may encroach upon the sovereignty of nation states

”Although the provision for mandatory arbitration was a transformative addition to the OECD Model (2008), the OECD acknowledged that in some states, national law, policy or administrative considerations might not allow or justify the type of dispute resolution envisaged under article 25(5). The OECD also conceded that some states might only wish to include article 25(5) of the OECD Model (2008) in tax treaties with certain states.“

Michelle Markham, ”Seeking new directions in dispute resolution mechanisms: Do we need a revised mutual agreement procedure?“ *Bulletin for International Taxation*, Vol. 70 (January/February 2016), p. 83

RIGHTS OF DEFENSE

- Conclusion of EUCJ (in Paragraph 90): the tax authorities are not prevented from being able to use evidence obtained in a parallel criminal procedure that has not yet been concluded, by means of the interception of telecommunications and seizure of emails
– protection of citizens by the principle that personal data must be used instrumentally?
– it is not precluded that criminal and public administrative procedures to be followed in parallel to each other are not illegal

- Conclusion of EUCJ (in Paragraph 91): it is incumbent upon the national court which reviews the legality of the decision founded on evidence adjusting VAT to verify
- whether the interception of telecommunications and seizure of emails were means of investigation provided for by law and were necessary in the context of the criminal procedure; and
- whether the use by the tax authorities of the evidence obtained by those means was also authorised by law and necessary; and
- whether, in accordance with the general principle of observance of the rights of the defence, the taxable person had the opportunity, in the context of the administrative procedure, of gaining access to that evidence and of being heard concerning it

- Recognition of the fundamental rights of defence

”Fundamental rights form an integral part of the general principles of law the observance of which the Court ensures. For that purpose, it draws inspiration from the constitutional traditions common to the Member States and from the guidelines supplied by international treaties for the protection of human rights on which the Member States have collaborated or to which they are signatories …“

C-349/07 *Sopropé*, ECR 2008, p. I-10369, Para. 33

”Observance of the rights of the defence is a general principle of Community law which applies where the authorities are minded to adopt a measure which will adversely affect an individual.“

C-349/07 *Sopropé*, Para. 36

EU Charter of fundamental rights: Article 7 on respect for privacy, Article 8 on the protection of personal data, Article 41 on the right to good administration, Article 47 on the right to effective remedy and fair trial, Article 48 on the presumption of innocence and to the right of defence

- Limited application of BEPS action plan-relating measures to the EU?

- It is a question whether anti-abuse measures comply with the proportionality test of EUCJ, in particular in respect of the standard of ”wholly artificial arrangements“ as developed by EUCJ:
” The proposed anti-abuse rules (or best practices) do not seem to target wholly artificial arrangements, and they are often to be applied mechanically in a way that would likely be deemed disproportional by the Court of Justice.“ – OECD proposal: a principal purpose test (PPT rule) in Action Plan 6 on treaty benefits

C-196/04 *Cadbury Schweppes*, ECR 2006, p. I-7995, Para. 55

- The integrated OECD approach may be in conflict with the assessment of the EU freedoms from Member State to Member State:
”Furthermore, proposals that are dependent on taking into account the tax treatment in another Member State might not pass muster at the Court of Justice.“

– OECD may emphasise concerns as regards, e.g., a strictly territorial nexus test instead of applying an integrated approach to the substance of business activities carried on across the border, as reflected in Action Plan 5 on harmful tax practices, or OECD provides for transfer pricing documentation (in Action Plan 13) to be established upon a country-by-country approach

– e.g., the EU Court held in *Denkavit Internationaal* that restriction on the freedom of establishment by denying from non-French companies participation exemption for the dividends received cannot be justified by the fact that the Dutch parent may credit the French withholding tax against the Dutch one

C-170/05, ECR 2006, p. I-11949, Para. 49

- BEPS-measures may encounter the requirement of legal certainty as developed both at the levels of the EU and the Member States:
”While such measures may now, more than ever, be politically appealing and feasible, both the EU institutions and the Member States should resist the challenge of taking action without careful forethought and a detailed legal analysis. Such actions could generate legal uncertainty and damage the credibility of EU institutions, with no guarantee of reciprocal action by third countries.“

Christiana H.J.I. Panayi, ”The compatibility of the OECD/G20 Base Erosion and Profit Shifting proposals with EU law“ *Bulletin for International Taxation*, Vol. 70 (January/February 2016), p. 112