International Tax Law: New Challenges to and from Constitutional and Legal Pluralism

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Preface

This book is a collection of academic papers that were presented and discussed at the 9th annual conference of the Group for Research on European and International Taxation (GREIT). The conference was held at the Law Faculty of the University of Münster, Germany, on 18 and 19 September 2014. During two days of intense scholarly debate, different aspects of constitutional and legal pluralism in the field of international taxation were analysed; the framework for the discussion was set by a keynote on the theoretical foundations and fundamental implications of the concept of pluralism. Several contributions explored in which respect, and to what extent, national, international or supranational provisions of international tax law are subject to constitutional requirements of a different legal pedigree. As is the hallmark of GREIT research, much of the analysis was pioneering work and certainly went beyond the now well-established fundamental freedom scrutiny of tax systems of the EEA Member States. In a similar fashion, recent phenomena of legal pluralism were scrutinized; in this context, the papers focused on parallel tax regimes at different layers of legislation and governance. During debate, the need for legal reconciliation and institutional coordination became palpable. At the time of the conference, the OECD BEPS project was already in full swing, which also heavily influenced the deliberations of participants. Finally, possible developments of a *Europe à deux vitesses,* also in the field of international taxation, were outlined.

I am thankful to my friends and colleagues Ana Paula Dourado, Cécile Brokelind, Pasquale Pistone and Dennis Weber, who initiated the GREIT project and who entrusted me with hosting the 2014 conference. I am furthermore grateful for all others who have contributed to the academic success of this conference and to the publication of this book, as speakers, authors and panel chairs and members. I also wish to warmly thank Hanna Datzer for her invaluable support and the perfect organization of the conference, as well as for assisting me in my role as editor of this book. She and the entire team of my Institute for Tax Law were fully dedicated to making the 9th GREIT event a lasting contribution to tax law research, and to providing all attendees with many enjoyable moments also beyond the academic debate.

I gratefully acknowledge the generous support of the conference and the publication of this book by our sponsors, the Deutsche Forschungsgesellschaft (DFG), PwC and IBFD.

full implementation of anti-BEPS measures will constitute a platform for a significant improvement in the exercise of taxing powers in cross-border situations also within the European Union.

However, several doubts exist as to whether the Actions of the BEPS project fully comply with the supremacy of EU law. Such doubts arise in particular in the context of attempts to mechanically apply the reaction to base erosion and profit shifting without a substance analysis – which is essential for EU law to enact a proportionate reaction to undesirable practices. Also, the author does not believe that a shift to partly artificial arrangements can be effectively enacted in the European Union in the absence of clear guidance from the Court of Justice of the European Union.

Chapter 9

The Meaning of Aggressive Tax Planning and Avoidance in the European Union and the OECD: An Example of Legal Pluralism in International Tax Law

Ana Paula Dourado

9.1. OECD recommendations and EU law: Reciprocal influences

OECD recommendations have been assessed in light of EU constitutional law as international legal standards. In the absence of EU harmonization, the EU fundamental freedoms in the Treaty on the Functioning of the European Union (TFEU) are to be interpreted in light of those standards, and therefore they are to be validly used and followed by EU Member States. Examples in case law are related to (i) the allocation of taxing powers between the source and the residence states which, in the absence of harmonization, are to be based on tax treaties (e.g. *Gilly*, *Futura*, *Van Hilten*)[1] and (ii) tax treaty solutions which may constitute valid justifications of restrictions on the fundamental freedoms (e.g. case law on outbound dividends).[2]

This chapter will consider whether and to what extent OECD recommendations are also to be assessed as interpretive standards and as standards for the creation of EU (binding) law and EU recommendations.

As the OECD includes many EU Member States, and also because the European Union and the OECD are observers at each other's meetings, there have been reciprocal influences between EU law and OECD

1. FR: ECJ, 12 May 1998, Case C-336/96, *Gilly v. Directeur des services fiscaux du Bas-Rhin*, (1998) ECR I-02793, para. 31, ECJ Case Law IBFD. Indirectly, *see* LU: ECJ, 15 May 1997, Case C-250/95, *Futura Participations SA and Singer v. Administration des contributions*, (1997) ECR I-02471, para. 22, ECJ Case Law IBFD; NL: ECJ, 23 Feb. 2006, Case C-513/03, *Heirs of M.E.A. van Hilten-van der Heijden v. Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, (2006) ECR I-01957, para. 48, ECJ Case Law IBFD.

2. *See*, e.g. FR: ECJ, 14 Dec. 2006, Case C-170/05, *Denkavit Internationaal and Denkavit France (Denkavit II)*, (2006) ECR I-11949, paras. 43-45, ECJ Case Law IBFD; NL: ECJ, 8 Nov. 2007, Case C-379/05, *Amurta SGPS v. Inspecteur van de Belastingdienst/Amsterdam*, (2007) ECR I-9569, paras. 79-84, ECJ Case Law IBFD.

recommendations and tax treaties. In fact, EU law has also played a role in influencing OECD recommendations.

Reciprocal influences between OECD recommendations and EU law could be observed in the 2003 Savings Directive[3] and in the 2011 Mutual Assistance Directive,[4] as amended. The Savings Directive has, to a certain extent, implemented the 1998 OECD report on harmful tax competition[5] and was at the forefront of the current international standard on automatic exchange of information and the recent OECD Standard on Automatic Exchange of Information (Common Reporting Standard and Competent Authorities' Agreement (CAA)).[6] In turn, the 2011 Mutual Assistance Directive has implemented the international standard on exchange of information, as designed by the 2006 OECD Manual on Exchange of Information,[7] the 2002 OECD Model Agreement on Exchange of Information on Tax Matters and the 2005 OECD Model Convention (OECD Model) version of article 26, and was at the same time at the forefront of multilateral automatic exchange of information (leaving aside the US Foreign Account Tax Compliance Act (FATCA)).[8] In Commission Implementing Regulation 1353/2014, which sets forth rules for implementing certain provisions of the Mutual Assistance Directive, the latter has in turn been subject to OECD and FATCA influences.[9]

Moreover, the amendment to the Parent-Subsidiary Directive as regards hybrid mismatch arrangements and double non-taxation[10] represents a

3. Council Directive of 3 June 2003 on Taxation of Savings Income in the form of Interest Payments (2003/48/EC) as amended by Council Directive 2014/48/EU of 24 March 2014.
4. Council Directive 2011/16/EU of 15 February 2011 on Administrative Cooperation in the Field of Taxation and repealing Directive 77/799/EEC.
5. OECD, *Harmful Tax Competition: An Emerging Global Issue* (OECD 1998).
6. *OECD Standard for Automatic Exchange of Financial Account Information, Common Reporting Standard*, 13 February (OECD 2014).
7. OECD Committee on Fiscal Affairs, *Manual on the Implementation of Exchange of Information Provisions for Tax Purposes* (2006).
8. A.J. Soriano, *Toward an Automatic but Asymmetric Exchange of Tax Information: The US Foreign Account Tax Compliance Act (FATCA) as Inflection Point*, 40 Intertax 10 (2012), at 540; I. Grinberg, *Taxing Capital Income in Emerging Countries: Will FATCA Open the Door?*, 5 World Tax J. 3 (2013), at 325.
9. Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC. Commission Implementing Regulation (EU) No. 1353/2014 of 15 December 2014 amending Implementing Regulation (EU) No. 1156/2012 laying down detailed rules for implementing certain provisions of Council Directive 2011/16/EU on administrative cooperation in the field of taxation.
10. At the meeting of ECOFIN without discussion of 8 July 2014: amendment to Directive 2011/96/EC. Under the adopted amendment, which modifies art. 4(1)(a) PSD, the EU Member State where the parent company is located shall "refrain from taxing such profits to the extent that such profits are not deductible by the subsidiary, and tax such

multilateral implementation of one of the proposals in BEPS Action 2. The Commission Recommendation on aggressive tax planning, regarding the introduction of a general anti-abuse rule (GAAR) in the Member States, the GAAR for the Parent-Subsidiary Directive, the ATAD Proposal of 28 January 2016, as well as BEPS Actions 2 to 4 and 6 reflect the same spirit, even if the contents and methodology do not overlap.

9.2. Legal pluralism and the fall of the national tax state

Due to free movement of capital and the euro crisis, the concept of the tax state is facing serious risks in EU Member States, although EU tax governance is far from being achieved and global tax governance is not institutionalized. Thus, so far, no alternative has been found to replace the tax state.[11] In contrast, in the context of the 2008 financial crisis, the G20 has managed to put forward global tax standards, to then be legally considered by the OECD. The European Commission has made efforts to be at the forefront of the process, proposing amendments to the Savings Directive, the Mutual Assistance Directive and the Parent-Subsidiary Directive, presenting two Recommendations, one regarding measures intended to encourage third countries to apply minimum standards of good governance in tax matters and the other one on aggressive tax planning and the ATAD Proposal.[12]

Both the OECD and the European Union normally take advantage of national legal rules that are considered to be best practices, but are in some cases innovative (or have to be innovative, due to their cross-border purpose, object and scope). Examples of innovative rules include: (i) the linking rules in the case of double non-taxation due to hybrid mismatch arrangements; (ii) the recently introduced changes to the EU Parent-Subsidiary Directive

profits to the extent that such profits are deductible by the subsidiary." This amendment links the tax treatment in the state of the parent company with that of the subsidiary. As such, the changes aimed at hybrid loan arrangements could affect certain group financing arrangements where such arrangements are not already limited under domestic rules. Many member states already have introduced broader anti-avoidance rules to tackle hybrid loan arrangements and/or already deny exemption for deductible distributions. All remaining Member States will have to implement the new anti-hybrid rule within their domestic legislation by 31 December 2015.
11. Before the 2008 financial crisis, *see* P. Genschel & S. Uhl, *Der Steuerstaat und die Globalisierung*, in *Transformationen des Staates?* (S. Leibfried & M. Zürn eds., 2006), at 92-117.
12. Recommendations C(2012) 8805 of 6.12.2012 and C(2012) 8806 of 6.12.2012, respectively; and Proposal for a Council Directive laying down rules against tax avoidance practices that directly affect the functioning of the internal market, 28.1.2016, COM (2016) final.

that may have as their inspiration existing domestic switch-over rules; (iii) automatic exchange of information as provided under the Savings Directive, relying on the beneficial owner (which has a different meaning and plays a different role from that in articles 10, 11 and 12 of the OECD Model); and (iv) paying agents concepts.

The OECD and European Union also have a worldwide influence in proposing global standards, suggesting that tax law concepts and practices are to be adopted universally. This suggestion has been put forward by the Global Forum in respect of information exchange. In its view:

> [t]he international standard, which was developed by the OECD in co-operation with non-OECD countries and which was endorsed by the G20 Finance Ministers at their Berlin Meeting in 2004 and by the UN Committee of Experts on International Cooperation in Tax at its October 2008 Meeting, requires the exchange of information on request in all tax matters for the administration and enforcement of domestic tax law without regard to a domestic tax interest requirement or bank secrecy for tax purposes. It also provides for extensive safeguards to protect the confidentiality of the information exchanged.[13]

9.3. The meaning of aggressive tax planning

Until the recent movement against base erosion and profit shifting (BEPS), tax planning has been considered legal under international tax law and also compatible with the fundamental freedoms under EU law. In fact, even if aimed at reducing the tax burden, tax planning complies with both (i) the purpose of the legislation (main objective test) and (ii) the complementary business purpose test (under international tax law)[14] or the genuine economic activity test (under EU law).[15]

In the context of the BEPS project of the OECD and G20, cross-border tax planning is acquiring an international meaning, related to an artificial

13. OECD, *Tax Co-operation 2009: Towards a Level Playing Field*, 2009, available at www.oecd.org, at 8.
14. For example, valid commercial reasons, as mentioned in the Action 6 Deliverable, under point 8 of the Commentary on the principal-purpose test. OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances – Action 6: 2014 Deliverable*, OECD/G20 Base Erosion and Profit Shifting Project (OECD Publishing 16 Sept. 2014), at 69, International Organizations' Documentation IBFD.
15. UK: ECJ, 12 Sept. 2006, Case C-196/04, *Cadbury Schweppes v. Commissioners of Inland Revenue*, (2006) ECR I-07995, paras. 54-55, ECJ Case Law IBFD.

shifting of profits, but not necessarily connected to the reasonably settled international or EU concepts of tax avoidance or abuse. Because policy statements and legal documents often make reference to tax planning, aggressive tax planning, tax evasion and tax avoidance as synonyms or overlapping concepts, it is not always clear whether aggressive tax planning is an autonomous concept, a tax policy concept or a legal concept.

Aggressive tax planning is envisaged as improper behaviour by the taxpayer, related to some global concept of tax morality. But more than the negative assessment of the taxpayer's behaviour, the new era involves the search by states for an adequate response to schemes that may be legal, but nevertheless endanger the survival of the tax state and the global notion of fairness. The above-mentioned concerns have led to calls for international collective efforts, as illustrated in the St. Petersburg G20 Leaders' Declaration of September 2013.[16] Reference is made to international tax planning in the G20 Tax Annex to the St. Petersburg G20 Leaders' Declaration,[17] whereas several OECD[18] and EU documents make reference to aggressive tax planning (e.g. the Commission Recommendation on aggressive tax planning).

In the context of the BEPS project, aggressive tax planning has been used in OECD and EU soft law instruments as a vague concept very much linked to a call for new policy developments and coordinated international action. Aggressive tax planning is generally described as the behaviour adopted

16. Paragraph 5 of the Tax Annex to the St. Petersburg G20 Leaders' Declaration reads as follows: "International collective efforts must also address the tax base erosion resulting from international tax planning. Base erosion and profit shifting (BEPS) relates chiefly to instances where the interaction of different tax rules result in tax planning that may be used by multinational enterprises (MNEs) to artificially shift profits out of the countries where they are earned, resulting in very low taxes or even double non-taxation. These practices, if left unchecked, undermine the fairness and integrity of our tax systems. They fundamentally distort competition, because businesses that engage in cross-border BEPS strategies gain a competitive advantage compared with enterprises that operate mostly at the domestic level. Fair, transparent and efficient tax systems are not only key pillars for sound public finances, they also provide a sustainable framework for dynamic economies. For these reasons, G20 Leaders identified the need to address BEPS as a priority in their tax agenda at the Los Cabos Summit in June 2012. Additionally, we must achieve better international coordination on taxes. In this regard, we must move forward in fighting BEPS practices so that we ensure a fair contribution of all productive sectors to the financing of public spending in our countries".
17. OECD, *Action Plan on Base Erosion and Profit Shifting* (OECD 2013), at 13, International Organizations' Documentation IBFD; OECD, *Neutralising the Effects of Hybrid Mismatch Arrangements – Action 2: 2014 Deliverable*, OECD/G20 Base Erosion and Profit Shifting Project (OECD Publishing 2014), at 24, International Organizations' Documentation IBFD.
18. E.g. OECD, *Action Plan on Base Erosion and Profit Shifting – Report:2013* (OECD 2013), at 13.

by multinationals as they explore existing opportunities to decrease the tax burden afforded by globalization and the interaction of tax rules in different jurisdictions. The indeterminacy as regards the meaning of aggressive tax planning induces one to conclude that the concept may cover both tax planning and tax avoidance, or merely tax planning – depending on the context. As argued below, aggressive tax planning is currently an umbrella concept that includes both international tax planning and tax avoidance.

There is a danger concerning international tax standards, such as the aim to combat aggressive tax planning. States may be tempted to introduce unilateral legislation that jeopardizes international concepts and may confuse the courts as to the real nature of that planning. The recent UK diverted profits tax, which seems to introduce a new unilateral concept of permanent establishment,[19] may well be an anti-abuse rule.

9.4. Aggressive tax planning in the European Union

Action against aggressive tax planning in the European Union is very much related to the OECD/G20 global call and, at both the EU and OECD/G20 level, this action complements the strong move towards multilateral and automatic exchange of information. The G20 Communiqué, issued by the meeting of finance ministers and central bank governors that took place in Moscow on 15-16 February 2013, assumes the commitment to developing measures that address BEPS and to vigorously expanding the practice of automatic and multilateral exchange of information.[20]

19. *See* H. Self, *Diverted Profits Tax: Give BEPS a Chance*, Tax J. (15 Dec. 2014), available at http://www.taxjournal.com/tj/articles/diverted-profits-tax-give-beps-chance-15122014.
20. "In the tax area, we welcome the OECD report on addressing base erosion and profit shifting and acknowledge that an important part of fiscal sustainability is securing our revenue bases. We are determined to develop measures to address base erosion and profit shifting, take necessary collective actions and look forward to the comprehensive action plan the OECD will present to us in July. We strongly encourage all jurisdictions to sign the Multilateral Convention on Mutual Administrative Assistance. We encourage the Global Forum on Transparency and Exchange of Information to continue to make rapid progress in assessing and monitoring on a continuous basis the implementation of the international standard on information exchange and look forward to the progress report by April 2013. We reiterate our commitment to extending the practice of automatic exchange of information, as appropriate, and commend the progress made recently in this area. We support the OECD analysis for multilateral implementation in that domain."

As a response to the G20 call for an action by the OECD against BEPS at the Los Cabos Summit in June 2012,[21] the European Commission defined aggressive tax planning in its Recommendation as consisting "in taking advantage of the technicalities of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability".[22] The Recommendation on aggressive tax planning refers to the necessity of addressing "instances in which a taxpayer derives fiscal benefits through engineering its tax affairs in such a way that income is not taxed by any of the tax jurisdictions involved (double non-taxation)", adding that "[t]he persistence of such situations can lead to artificial capital flows and movements of taxpayers within the internal market and thus harm its proper functioning as well as erode Member States' tax bases".[23] Action is called for to counter the engineering that leads to double non-taxation as such. The reference to artificial capital flows and movements of taxpayers is a prospective consequence of tax planning, and therefore does not imply a demonstration of this artificiality.

The Recommendation on aggressive tax planning also refers to the difficulty faced by Member States in protecting their national tax bases from erosion through aggressive tax planning, in the economic global context: "[...] especially due to the cross-border dimension of many tax planning structures and the increased mobility of capital and persons".[24] The Recommendation further clarifies that "[a]ggressive tax planning can take a multitude of forms. Its consequences include double deductions (e.g. the same loss is deducted both in the state of source and residence) and double non-taxation (e.g. income which is not taxed in the source state is exempt in the state of residence)".[25]

One can argue that aggressive tax planning has already been granted legal meaning in the European Union, as the risk of double deductions has been assessed by the Court of Justice of the European Union as a valid justification for a Member State to deny the deduction of cross-border losses.[26]

21. *See supra* n. 16.
22. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 2.
23. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 2.
24. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 2.
25. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 2.
26. *See* e.g. UK: ECJ, 13 Dec. 2005, Case C-446/03, *Marks & Spencer plc v. Halsey (Her Majesty's Inspector of Taxes)*, (2005) ECR I-10837, para. 47, ECJ Case Law IBFD.

The Recommendation suggests the adoption of legal rules in order to avoid double dipping. But the double deduction of losses can also be the consequence of transfer pricing mismatches. Moreover, double non-taxation, as described in the Recommendation, is a consequence of hybrid mismatch arrangements (hybrid instruments or hybrid entities).[27]

The Recommendation's broad definition of aggressive tax planning does not correspond to the concept of tax avoidance or abuse in EU law. According to the Court of Justice, an EU taxpayer is entitled to exercise a fundamental freedom or engage in operations in order to benefit from a more favourable tax regime[28] which is equivalent to the purpose of reducing tax liability. In contrast to the principle of abuse, aggressive tax planning also covers the existence of legal gaps or mismatches exploited in cross-border situations. Legal gaps must be dealt with by law, due to the principles of (i) no taxation without representation and (ii) separation of powers in tax law.

9.5. Tax avoidance in the European Union

In respect of non-harmonized direct taxes, abuse occurs in cases where a person attempts to circumvent domestic law provisions while, at the same time, taking improper advantage of the fundamental freedoms, by exercising the right to a fundamental freedom in an artificial manner. In these situations, abuse must be assessed in light of the fundamental freedoms (which constitute principles and therefore are inherently vague) and not in light of domestic law provisions, even if the latter are the object of circumvention:

> nationals of a Member State cannot attempt under cover of the rights created improperly to circumvent their national legislation. They must not improperly or fraudulently take advantage of provisions of Community law (Case 115/78 Knoors [1979] ECR 399, paragraph 25; Case C-61/89 Bouchoucha [1990] ECR I-3551, paragraph 14; and Case C-212/97 Centros [1999] ECR I-1459, paragraph 24).[29]

Another group of cases on abuse in direct taxes is related to interpretation of a Directive (partial harmonization), and these cases have more specifically

27. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 2.
28. UK: ECJ, 21 Feb. 2006, Case C-255/02, *Halifax plc v. Commissioners of Customs & Excise*, (2006) ECR I-1609, paras. 73-75, ECJ Case Law IBFD; *Cadbury Schweppes* (C-196/04), *supra* n. 15, paras. 34, 36, 37; UK: ECJ, 22 Dec. 2010, Case C-277/09, *Commissioners for Her Majesty's Revenue & Customs v. RBS Deutschland Holdings GmbH*, (2010) ECR I-13805, paras. 47-55, ECJ Case Law IBFD.
29. *Cadbury Schweppes* (C-196/04), *supra* n. 15, para. 35.

involved interpretation of article 15(1)(a) of the Merger Directive[30] (ex article 11(1)(a)). Abuse occurs where it appears that one of the operations referred to in article 1(a) (restructuring of companies) has tax evasion or tax avoidance as its principal objective or as one of its principal objectives. According to the Directive, the fact that the operation is not carried out for valid commercial reasons (such as the restructuring or rationalization of the activities of the companies participating in the operation) may constitute a presumption that the operation has tax evasion or tax avoidance as its principal objective or as one of its principal objectives.[31]

In both non-harmonized and partially harmonized direct tax matters, it is settled case law that unrebuttable presumptions of tax avoidance or tax evasion are not acceptable, as they are disproportionate. This implies that "the competent national authorities may not confine themselves to applying predetermined general criteria but must subject each particular case to a general examination of the operation in question".[32]

In respect of VAT it is the Sixth VAT Directive,[33] as amended, that is interpreted by the national courts and the EU Court of Justice. In VAT cases, the principle of abuse has been built up as an interpretive principle of the Sixth Directive, as amended. The departure point of this case law on VAT

30. EU Merger Directive (2009): Council Directive 2009/133/EC of 19 October 2009 on the Common System of Taxation Applicable to Mergers, Divisions, Partial Divisions, Transfers of Assets and Exchanges of Shares Concerning Companies of Different Member States and to the Transfer of the Registered Office of an SE or SCE between Member States (Codified Version), art. 15, OJ L310 (2009), EU Law IBFD.
31. On the meaning of abuse in the Merger Directive, *see* J. Englisch, *National Measures to Counter Tax Avoidance under the Merger Directive*, in *Movement of Persons and Tax Mobility in the EU: Changing Winds* (A.P. Dourado ed., IBFD 2014), at 213, 246-249, Online Books IBFD. *See also* NL: ECJ, 17 July 1007, Case C-28/95, *Leur-Bloem v. Inspecteur der Belastingdienst/Ondernemingen Amsterdam 2*, (1997) ECR I-4161, para 47, ECJ Case Law IBFD; PT: ECJ, 10 Nov. 2011, Case C-126/10, *Foggia – Sociedade Gestora de Participações Sociais SA v. Secretário de Estado dos Assuntos Fiscais*, (2011) ECR I-10923, paras. 34-35, 42, 45, 47-48, ECJ Case Law IBFD. *See* A.P. Dourado, *Portugal: The Foggia (C-126/10) and Amorim (C-38/11) Cases*, in *ECJ: Recent Developments in Direct Taxation 2011* (M. Lang et al. eds., Linde 2012), at 213-222; A.P. Dourado & J. Almeida Fernandes, *Portugal*, in *ECJ: Recent Developments in Direct Taxation 2010* (M. Lang et al. eds., Linde 2011), at 205-206.
32. *Foggia* (C-126/10), para. 37. *See also* Dourado, in *ECJ: Recent Developments in Direct Taxation 2011*, *supra* n. 31, at 213-222; Dourado & Almeida Fernandes, *supra* n. 31, at 205-206.
33. EU Sixth VAT Directive (1977): Sixth Council Directive of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment (77/388/EEC), OJ L145 (1977), EU Law IBFD.

is *Halifax*, in which abuse is deemed to have occurred if two elements are present:

- the accrual of a tax advantage the grant of which is contrary to the purpose of the legal provision; and
- the obtaining of a tax advantage as the essential aim of the transactions concerned.[34]

At this stage of EU law, the principle of abuse cannot be claimed to be a uniform or fully consistent principle applicable to all taxes. Inconsistencies also remain in respect of the same type of taxes and even in respect of the same legal issue, but future developments in EU legislation and in EU case law will most probably go in the direction of a single EU concept of abuse.[35] However, due to the specificities of the internal market and free movement of persons and capital in the European Union, it is not so clear that the OECD/G20 meaning of "avoidance" will lead to a global single concept of abuse.

Independently of future expected developments, the concept of tax avoidance in EU law requires some conditions and tests that do not correspond to the notion of aggressive tax planning. Whereas the latter corresponds to the simple taking advantage of the technicalities of one tax system or of mismatches between two or more tax systems, avoidance or abuse in light of EU law requires fulfilment of other conditions, as previously discussed.

9.6. Aggressive tax planning as an umbrella concept

From the examples mentioned above, one can conclude that an EU concept of abuse does not coincide with the concept of aggressive tax planning in the Recommendation on aggressive tax planning. However, the legal concept of

34. According to the ECJ in *Halifax*: "in the sphere of VAT, an abusive practice can be found to exist only if, first, the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth Directive and the national legislation transposing it, result in the accrual of a tax advantage the grant of which would be contrary to the purpose of those provisions [...].
[...] Second, it must also be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage. As the Advocate General observed in point 89 of his Opinion, the prohibition of abuse is not relevant where the economic activity carried out may have some explanation other than the mere attainment of tax advantages", Halifax (C-255/02), paras. 74-75.

35. A.P. Dourado, *A Single Principle of Abuse in European Union Law: A Methodological Approach to Rejecting a Different Concept of Abuse in Person Taxation*, in *Prohibition of Abuse of Law: A New General Principle of Law?*, (R. de la Feria & S. Vogenauer eds., Hart Publishing 2011), at 469-483.

tax avoidance or abuse can be covered by a broader concept, i.e. an umbrella concept.

Aggressive tax planning is not a legal concept allowing recharacterization for tax purposes of the legal structure or scheme adopted by the taxpayer. Nor does it expand the concept of avoidance, nor allow per se application of either a general anti-avoidance rule or a specific anti-avoidance rule. Aggressive tax planning calls for collective action by the Member States; it requires coordinated legislative action targeted at the improvement of anti-avoidance rules, and the adoption of either EU or domestic legislative measures to overcome legal gaps or mismatches.[36]

Notably, as mentioned, aggressive tax planning can also be identified as the risk of tax avoidance and – in this case – in the European Union, it can justify national measures that restrict the EU fundamental freedoms.

9.7. Aggressive tax planning in the OECD

According to the OECD,[37] BEPS "refers to tax planning strategies that exploit gaps and mismatches in tax rules to make profits 'disappear' for tax purposes or to shift profits to locations where there is little or no real activity but the taxes are low resulting in little or no overall corporate tax being paid".[38] The BEPS Action Plan handles tax avoidance and aggressive tax planning as distinct but complementary targets. Reference is made to

36. For the latter case, European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 2. *See* the same Recommendation, at 2-3 ("In 2012 the Commission carried out a public consultation on double non-taxation in the internal market. Since it is not possible to address all the issues covered by that consultation through one single solution, it is appropriate, as a first step, to deal with the issue which is linked to certain frequently used tax planning structures that take advantage of mismatches between two or more tax systems and often lead to double non-taxation.
States often undertake, in their double taxation conventions, not to tax certain items of income. In providing for such treatment, they may not necessarily take account of whether such items are subject to tax in the other party to that convention, and thus whether there is a risk of double non-taxation. Such risk may also occur if Member States unilaterally exempt items of foreign income, irrespective of whether they are subject to tax in the source state. It is important to address both situations in this Recommendation".). For a critical analysis of the indeterminacy of aggressive tax planning in the above-mentioned EC Recommendation, *see* M. Lang, *"Aggressive Steuerplannung": eine Analyse der Empfehlung der Europäischen Kommission*, 2 *Steuer und Wirtschaft International* (2013), at 62.

37. OECD, *Frequently Asked Questions: 2015 Final Reports*, OECD/G20 Base Erosion and Profit Shifting Project (OECD 2015).

38. OECD, *Frequently Asked Questions: 2015 Final Reports*, *supra* n. 37, para. 113.

artificiality, where it is asserted that "[f]undamental changes are needed to effectively prevent double non-taxation, as well as cases of no or low taxation associated with practices that artificially segregate taxable income from the activities that generate it".[39] One can argue that "artificial segregation of taxable income" corresponds to the abuse test used by the EU Court of Justice ("artificial schemes"), but the concerns underlying the BEPS Action Plan go beyond tax avoidance, covering legal gaps and mismatches, and corresponding to what the Commission Recommendation refers to as aggressive tax planning.

The above-mentioned double non-taxation referred to in the BEPS Action Plan is caused not just by tax avoidance, and this is clear in the reference to the need to "ensure the coherence of corporate income taxation at the international level".[40] In turn, the "realignment of taxation and relevant substance"[41] refers to the design as a whole of corporate taxes, and includes improvement of anti-avoidance provisions, but goes beyond it.

Thus, addressing BEPS also implies handling harmful tax regimes at both the OECD and the EU level.[42]

Careful interpretation will lead one to conclude that aggressive tax planning, as described in the above-mentioned Commission Recommendation on aggressive tax planning, is very much linked to the BEPS concept, and that avoidance is not necessarily present in BEPS behaviour. In paragraph 48, when it is asked whether BEPS strategies are illegal, the answers clarify that most schemes are not illegal and that "they just take advantage of current rules that are still grounded in a bricks and mortar economic environment rather than today's environment of global players which is characterised by the increasing importance of intangibles and risk management". In turn, avoidance is a concept focused on the behaviour of the taxpayer and not on the inadequacy of existing tax rules.

Furthermore, paragraph 49 adds that BEPS is caused by the inadequacy of corporate tax as a domestic tax in a cross-border environment, and that gaps are caused by the interaction of more than one legal system, which "result in income not being taxed anywhere". Finally, it is argued that BEPS leads

39. OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* n. 18, at 13.
40. OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* n. 18, at 13.
41. OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* n. 18, at 13.
42. *See* Recommendation regarding measures intended to encourage third countries to apply minimum standards of good governance in tax matters C (2012) 8805 EC.

to an inefficient allocation of resources by distorting investment decisions and to unfair results.[43]

Even clearer is paragraph 51, where aggressive tax planning is identified with BEPS. When the OECD asks "Why worry about BEPS now?", the answer is that "the OECD has been providing solutions to tackle aggressive tax planning for years".

If attention is now paid to some of the recommended solutions to BEPS, the conclusion is the same: linking rules as recommended in BEPS Action 2 go beyond the concept of tax avoidance or abuse, and are focused on recommending legislative action by the adoption of a series of linking rules that are targeted at avoiding gaps and mismatches.

The fact that aggressive tax planning is a broad concept, not necessarily coinciding with avoidance or abuse, is also illustrated by the increasing information duties that fall on the taxpayer regarding "aggressive tax planning arrangements". Under BEPS Action 12, it is recommended that states require their taxpayers to disclose aggressive tax planning arrangements, as follows:

> develop recommendations regarding the design of mandatory disclosure rules for aggressive or abusive transactions, arrangements or structures, taking into consideration the administrative costs for the tax administrations and business and drawing on experiences of the increasing number of countries that have such rules.[44]

9.8. Some measures to address aggressive tax planning

9.8.1. Subject-to-tax clause

EU and OECD/G20 concrete proposals to address BEPS reflect the same spirit, but do not coincide. For example the Commission Recommendation on aggressive tax planning proposes the adoption of a subject-to-tax clause aimed at dealing with double non-taxation:

> To give effect to point 3.1, Member States are encouraged to include an appropriate clause in their double taxation conventions. Such clause could read as follows:

43. *See* para. 50 Recommendation on aggressive tax planning, *supra* n. 12.
44. OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* n. 18, at 22.

> 'Where this Convention provides that an item of income shall be taxable only in one of the contracting States or that it may be taxed in one of the contracting States, the other contracting State shall be precluded from taxing such item only if this item is subject to tax in the first contracting State'.
>
> [...]
>
> Where, with a view to avoid double taxation through unilateral national rules, Member States provide for a tax exemption in regard to a given item of income sourced in another jurisdiction, in which this item is not subject to tax, Member States are encouraged to ensure that the item is taxed.
>
> For the purposes of points 3.1, 3.2 and 3.3 an item of income should be considered to be subject to tax where it is treated as taxable by the jurisdiction concerned and is not exempt from tax, nor benefits from a full tax credit or zero-rate taxation.[45]

The subject-to-tax clause in the Commission Recommendation does not distinguish between intended and unintended benefits. It is a general subject-to-tax clause[46] and seems to introduce the "duty to be taxed once" in the European Union.

The subject-to-tax clause in the Commission Recommendation is much broader than the actions suggested by BEPS Action 2, where linking rules are recommended in the case of hybrids.

9.8.2. Linking rules in BEPS Action 2

According to the OECD BEPS Action Plan,[47] Action 2 is to develop model treaty provisions and recommendations regarding the design of domestic rules to neutralize the effect of hybrid instruments and entities. Reference in the BEPS Action Plan is also made to (i) domestic measures that are restricted to hybrid instruments and entities, and may include changes to the OECD Model Tax Convention to ensure that hybrids are not used to unduly obtain treaty benefits; (ii) domestic law provisions that prevent exemption or non-recognition for a payment that is deductible by the payer; (iii) domestic

45. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 4.
46. For a critical analysis of the subject-to-tax clause recommended by the European Commission, *see* C. Marchgraber, *The Avoidance of Double Non-Taxation in Double Tax Treaty Law: A Critical Analysis of the Subject-To-Tax-Clause Recommended by the European Commission*, 23 EC Tax Rev. 5 (2014), at 293; M. Lang, *Aggressive Steuerplannung*, *supra* n. 36, at 64-65.
47. OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* n. 18.

law provisions that deny a deduction for a payment that is not includible in income by the recipient (and is not subject to taxation under controlled foreign company (CFC) or similar rules); (iv) domestic law provisions that deny a deduction for a payment that is also deductible in another jurisdiction; and (v) where necessary, guidance on coordination or tie-breaker rules if more than one country seeks to apply such rules to a transaction or structure.[48] Furthermore, the BEPS Action Plan mentions that the work on Action 2 will be coordinated with the work on interest expense deduction limitations, on CFC rules and on treaty shopping.[49]

The amendment in June 2014 to the Parent-Subsidiary Directive is a follow-up of point (i) (above) in the BEPS Action Plan (Action 2), illustrating the reciprocal influences between the OECD and Commission Recommendations.

9.9. The ATAD proposal

The ATAD proposal also comprises rules that are addressed at aggressive tax planning and avoidance. In its Explanatory Memorandum, there is an undifferentiated reference to both aggressive tax planning and avoidance.

According to the first paragraph of the aforementioned Memorandum, "[t]he European Council conclusions of 18 December 2014 cite 'an urgent need to advance efforts in the fight against tax avoidance and aggressive tax planning, both at the global and European Union (EU) levels'".

Furthermore, in its second paragraph, the Memorandum reads that "[t]he schemes targeted by this Directive involve situations where taxpayers act against the actual purpose of the law, taking advantage of disparities between national tax systems, to reduce their tax bill".

"Action against the purpose of law" is related to avoidance and not to aggressive tax planning. Reference to "the actual purpose of the law" is redundant and therefore adds no value to "the purpose of law". In turn, "taking advantage of disparities between national tax systems" is not avoidance, but allowed tax planning according to the CJEU settled case law (ICI, Emsland-Stärke, Centros, Cadbury Schweppes).[50]

48. OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* n. 18, at 15-16.
49. OECD, *Action Plan on Base Erosion and Profit Shifting*, *supra* n. 18, at 15-16.
50. ECJ, 16 July 1998, Case C-264/96, Imperial Chemical Industries plc [ICI] v. K. Hall Colmer [Her Majesty's Inspector of Taxes], (1998) I-04695, ECJ Case Law IBFD; ECJ,

In the Memorandum, aggressive tax planning is associated with distortion of business decisions in the internal market and with unfair tax competition (third paragraph of the Explanatory Memorandum).

The ATAD covers rules related to aggressive tax planning and to avoidance. For example, interest limitation (article 4), exit taxes (article 5), the switch-over clause (article 6), and the CFC rules in article 8(1), as well as the hybrid mismatches rule (article 10) aim to either address aggressive tax planning or even allocate taxing rights according to a fair principle of taxation, and are not necessarily linked to abuse.

9.10. Recommended general anti-abuse rules for EU Member States and the GAAR in the ATAD Proposal

The Commission Recommendation no. 8806 also proposes that multiple but common GAARs be adopted domestically by EU Member States in order to tackle domestic and cross-border "aggressive tax planning". It results from the above paragraphs that aggressive tax planning, in this context, is equivalent to tax avoidance or abuse:

> 4. General Anti-Abuse Rule
>
> 4.1. To counteract aggressive tax planning practices which fall outside the scope of their specific anti-avoidance rules, Member States should adopt a general anti-abuse rule, adapted to domestic and cross-border situations confined to the Union and situations involving third countries.[51]

In the Recommendation, GAARs were to be adopted domestically and not approved by an EU Directive. The Commission suggested that they are a key element against aggressive tax planning. The recommended GAAR has had an impact, since, for example, Greece, Italy and Poland recently introduced GAARs based on the EC Recommendation.[52] Moreover, the recommended multiple common GAARs are seen as an important tool against

16 March 2006, C-94/05, Emsland-Stärke GmbH v. Landwirtschaftskammer Hannover; ECJ, C-212/97, Centros Ltd v. Erhvers – og Selskabsstyrelsen – og Selskabsstyrelsen, (1999) I-01459, ECJ Case Law IBFD.

51. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 4.

52. Eleni Theocharopoulou, "Tax Avoidance Revisited: Exploring the Boundaries of Anti-Avoidance Rules in the EU BEPS Context", National Report Greece, EATLP Conference 2016, p. 1, http://www.eatlp.org/uploads/public/Greece%20(11%20November%202015).pdf;

abuse,[53] complementary to the EU anti-abuse rules that are part of EU directives harmonizing partial aspects of direct taxes, and do not overlap with them. In fact, the Recommendation excludes application of the proposed GAAR to the Merger Directive, the Parent-Subsidiary Directive and the Interest and Royalties Directive.[54]

In point 4.2, the Recommendation designs a draft GAAR, encouraging Member States to introduce it in their national legislation, in order to give effect to point 4.1:

> An artificial arrangement or an artificial series of arrangements which has been put into place for the essential purpose of avoiding taxation and leads to a tax benefit shall be ignored. National authorities shall treat these arrangements for tax purposes by reference to their economic substance.

Points 4.3 and 4.4 clarify point 4.2. Point 4.3 defines the term "arrangement" by using examples of legal or informal agreements that will result in an arrangement;[55] in turn, point 4.4 defines "artificial" as the lack of "commercial substance", adopting a substance-over-form test, broadly corresponding to the "pursuit of genuine economic activity" and "economic reality" in the

Giuseppe Zizzo, "Tax Avoidance Revisited: Exploring the Boundaries of Anti-Avoidance Rules in the EU BEPS Context", National Report Italy, EATLP Conference 2016, p. 8, http://www.eatlp.org/uploads/public/Italy%20(8%20Feb%202016).pdf; Joanna Niedojadło, Agnieszka Olesińska, "Tax Avoidance Revisited: Exploring the Boundaries of Anti-Avoidance Rules in the EU BEPS Context", National Report Poland, EATLP Conference 2016, pp. 6-7, http://www.eatlp.org/uploads/public/Poland%20(16%20November%202015).pdf.

53. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 3 ("As tax planning structures are ever more elaborate and national legislators are frequently left with insufficient time for reaction, specific anti-abuse measures often turn out to be inadequate for successfully catching up with novel aggressive tax planning structures. Such structures can be harmful to national tax revenues and to the functioning of the internal market. Therefore, it is appropriate to recommend the adoption by Member States of a common general anti-abuse rule, which should also avoid the complexity of many different ones. In this context, it is necessary to take account of the limits imposed by Union law with regard to anti-abuse rules").

54. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 3 ("So as to preserve the autonomous operation of existing Union acts in the area concerned, this Recommendation does not apply within the scope of Council Directive 2009/133/EC, of Council Directive 2011/96/EU and of Council Directive 2003/49/EC. A revision of those Directives with a view to implement the principles underlying this Recommendation is currently considered by the Commission").

55. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 4 ("For the purposes of point 4.2 an arrangement means any transaction, scheme, action, operation, agreement, grant, understanding, promise, undertaking or event. An arrangement may comprise more than one step or part").

Cadbury Schweppes judgment.[56] The Commission Recommendation also adds criteria that will help in determining artificiality:

> [...] an arrangement or a series of arrangements is artificial where it lacks commercial substance. In determining whether the arrangement or series of arrangements is artificial, national authorities are invited to consider whether they involve one or more of the following situations:
>
> (a) the legal characterization of the individual steps which an arrangement consists of is inconsistent with the legal substance of the arrangement as a whole;[57]
>
> (b) the arrangement or series of arrangements is carried out in a manner which would not ordinarily be employed in what is expected to be a reasonable business conduct;[58]
>
> (c) the arrangement or series of arrangements includes elements which have the effect of offsetting or cancelling each other;[59]
>
> (d) transactions concluded are circular in nature;[60]
>
> (e) the arrangement or series of arrangements results in a significant tax benefit but this is not reflected in the business risks undertaken by the taxpayer or its cash flows;[61]
>
> (f) the expected pre-tax profit is insignificant in comparison to the amount of the expected tax benefit.[62]

56. *Cadbury Schweppes* (C-196/04), *supra* n. 15, paras. 54 & 55.
57. UK: ECJ, 25 Feb. 1999, Case C-349/96, *Card Protection Plan Ltd v. Commissioners of Customs and Excise*, (1999) ECR I-973, para. 17, ECJ Case Law IBFD; SE: ECJ, 8 Mar. 2001, Case C-240/99, *Försäkringsaktiebolaget Skandia*, (2001) ECR I-1951, paras. 37, 41, ECJ Case Law IBFD; DK: ECJ, 20 Nov. 2003, Case C-8/01, *Taksatorringen*, (2003) ECR I-13741, paras. 39-41; NL: Opinion of Advocate General Poiares Maduro, 12 Jan. 2005, Case C-472/03, *Staatssecretaris van Financiën v. Arthur Andersen & Co. Accountants c.s.*, para. 16, ECJ Case Law IBFD; NL: ECJ, 3 Mar. 2005, Case C-472/03, *Staatssecretaris van Financiën v. Arthur Andersen & Co. Accountants c.s.*, (2005) ECR I-1719, paras. 34-36, ECJ Case Law IBFD.
58. Regarding VAT cases, the ECJ has been very tolerant when interpreting the transactions or series of transactions carried out by the companies and when interpreting what is expected to be a reasonable business conduct, even if the latter expression has not been used. *See* IT: ECJ, 22 May 2008, Case C-162/07, *Amplifin SpA v. Ministero dell'Economia e delle Finanze, Agenzia delle Entrate*, (2008) ECR I-4019, para. 28, ECJ Case Law IBFD; *RBS Deutschland Holdings* (C-277/09), paras. 47-54.
59. This is the case of hybrids. *See* OECD, *Action 2 Deliverable*, *supra* n. 17, chs. 2-4.
60. *See* DE: ECJ, 14 Dec. 2000, Case C-110/99, *Emsland-Stärke GmbH v. Hauptzollamt Hamburg-Jonas*, (2000) ECR I-11569, ECJ Case Law IBFD.
61. *See* D.N. Shaviro & D.A. Weisbach, *The Fifth Circuit Gets it Wrong in* Compaq v. Commissioner, University of Chicago, John M. Olin Law & Economics Working Paper 142 (2d Series). This could cover the carry forward of losses in the case of mergers, reverse mergers and leverage-buy-out arrangements.
62. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 4-5.

The design of the GAAR in the Commission Recommendation aims to follow the case law of the European Court of Justice on abuse, by making reference to the several tests that are included in the analysis.

And in general, probably with the exception of the *Ocean Finance* (*Paul Newey*) case, "artificiality" and a "reasonable business conduct" (*see* criterion (b)) have been interpreted by the European Court of Justice in a more tolerant manner than what is suggested in the BEPS Action Plan and Action 6. Examples of this tolerant interpretation of artificiality and reasonable business conduct (normal commercial operations) include the *Weald Leasing Ltd* and *RBS Deutschland Holdings GmbH* cases.[63]

The other criteria in 4.4. of the Recommendation do not correspond to facts assessed in existing European Court of Justice case law and are related to current concerns regarding derivatives (criterion (c)) and transactions leading to the elimination of risks (criterion (e)), although facts as those assessed in the *Foggia* case could be covered under criterion (e) or (f), and thin capitalization cases (*Thin Cap GLO*) and the *SGI* case[64] could be covered under criterion (e).

As case law using the criterion of normal commercial operations to assess abuse already illustrates, artificiality in the proposed GAAR is to be interpreted in light of the criteria enumerated in 4.4. from (a) through (f). The above-mentioned criteria will contribute to reaching a conclusion as to whether an artificial scheme was adopted.

The GAAR in the ATAD proposal is not identical to and is much more concise than the one in the aforementioned Recommendation. The original version of the Proposal refers to "non-genuine arrangements" or "a series thereof" (article 7(1), of the ATAD Proposal). Arrangements "shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality" (article 7(2) of the ATAD Proposal).

In turn, the Recommendation relies on the concept of "artificiality" and an arrangement or a series of arrangements is artificial where it "lacks commercial substance".

63. *RBS Deutschland Holdings* (C-277/09), para. 23.
64. BE: ECJ, 21 Jan. 2010, Case C-311/08, *Société de Gestion Industrielle (SGI)*, [2010] ECR I-487, paras. 71-72, ECJ Case Law IBFD; UK: ECJ, 13 Mar. 2007, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v. Commissioners of Inland Revenue*, (2007) ECR I-2107, para. 82, ECJ Case Law IBFD.

"Non-genuine arrangements" can be interpreted as equivalent to "artificiality" and the absence of "valid commercial reasons" equivalent to a "lack of commercial substance", but since all mentioned expressions are vague, they will lead to indeterminacy, at least in hard cases.

The relationship between the GAAR in the Directive and the GAAR in the Recommendation, as well as the relationship between national GAARs approved in light of the Recommendation and the GAAR in the Directive are examples of legal pluralism that will raise interpretation difficulties.

9.11. BEPS Action 6: Anti-abuse rules and their compatibility with EU law

Action 6 focuses on treaty abuse, recommending new anti-abuse rules and the strengthening of existing ones. It develops "model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances".[65] It further distinguishes between cases where limitations in a tax treaty are circumvented and cases where domestic tax provisions are circumvented using treaty benefits.

In order to tackle the complex phenomenon of treaty abuse, different but complementary anti-abuse measures must be included in both tax treaties and in domestic law. First, it is recommended that tax treaties include in their title and preamble a clear statement that the contracting states intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements. Second, it is recommended that tax treaties include a specific limitation-on-benefits rule. Third, in order to address other forms of treaty abuse (including treaty shopping that would not be covered by the limitation-on-benefits rule), it is recommended to add to tax treaties a more general anti-abuse rule based on the principal purpose of a transaction or arrangement (the principal-purpose test). Furthermore, Action 6 includes additional recommendations for new specific treaty anti-abuse rules (targeted rules), which are supplemented by the principal-purpose test.[66]

65. OECD, *Action 6 Deliverable*, *supra* n. 14, at 10 et seq.
66. OECD, *Action 6 Deliverable*, *supra* n. 14, at 10, at 13.

As tax treaties concluded by EU Member States must comply with EU law,[67] it remains to be seen whether and to what extent the proposals in Action 6 can be adopted by EU Member States.

The first recommendation raises no issues of compatibility with EU law, because, as analysed above, tax advantages in domestic or EU law cannot be obtained by using abusive transactions. Regarding limitation-on-benefits provisions, the European Court of Justice declared them to be compatible with EU law in the *ACT GLO* case.[68] Even though the arguments used by the Court are far from satisfactory,[69] it can be taken as settled case law that limitation-on-benefits rules are not incompatible with EU law.

Action 6 further recommends a general anti-abuse rule to address other forms of treaty abuse. More specifically, it is recommended that tax treaties include a more general anti-abuse rule based on the principal purpose of transactions or arrangements (i.e. the principal-purpose test).[70] The proposed rule reads as follows:

> Notwithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit,

67. Art. 307 TFEU. *See also* K. Vogel, D. Gutmann & A.P. Dourado, *Tax Treaties between Member States and Third States: "Reciprocity" in Bilateral Tax Treaties and Non-discrimination in EC Law*, EC Tax Rev. 2 (2006) at 83-94; A.P. Dourado, *National Report Portugal*, in *The EU and Third Countries* (M. Lang & P. Pistone eds., Linde 2007), at 523-526.
68. UK: ECJ, 12 Dec. 2006, Case C-374/04, *Test Claimants in Class IV of the ACT Group Litigation*, (2006) ECR I-11673, ECJ Case Law IBFD; NL: ECJ, 5 July 2005, Case C-376/03, *D. v. Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, (2005) ECR I-5821, ECJ Case Law IBFD.
69. Vogel, Gutmann & Dourado, *supra* n. 67, at 92 et seq. *See D.* (C-376/03), para. 61 ("The fact that those reciprocal rights and obligations apply only to persons resident in one of the two Contracting Member States is an inherent consequence of bilateral double taxation conventions"). Confirming this case law, *see Test Claimants in Class IV of the ACT Group Litigation* (C-374/04), para. 88. Moreover, the decision was in contradiction to previous case law involving the analysis of the compatibility between bilateral treaties concluded by at least one Member State and another state. *See* IT: ECJ, 15 Jan. 2002, Case C-55/00, *Elide Gottardo v. Istituto nazionale della previdenza sociale (INPS)*, (2002) ECR I-413, ECJ Case Law IBFD; NL: ECJ, 12 Apr. 1994, Case C-1/93, *Halliburton Services BV v. Staatssecretaris van Financiën*, (1994) ECR I-1337, ECJ Case Law IBFD; UK: ECJ, 5 Nov. 2002, Cases C-466/98 and 467/98, *Commission of the European Communities v. United Kingdom of Great Britain and Northern Ireland (Open Skies)*, (2002) ECR I-09427, ECJ Case Law IBFD.
70. OECD, *Action 6 Deliverable*, *supra* n. 14, at 11.

unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.[71]

The proposed principal-purpose test includes the two *Halifax* elements of the abuse principle in EU law, namely (i) whether the tax benefit granted is in accordance with the object and purpose of the relevant provisions in the tax treaty and (ii) whether obtaining the tax benefit was one of the principal purposes of any arrangement or transaction.

Commentary 10 on the principal-purpose test also is in line with point 4.5. of the Commission Recommendation on aggressive tax planning, clarifying that the purpose is to be determined by an objective analysis.[72] Moreover, the expression "one of the principal purposes" in the principal-purpose test at least formally corresponds to "the main purpose or one of the main purposes" in *Cadbury Schweppes*[73] and to "one of the principal purposes" as used in the Merger Directive.[74] But "one of the principal purposes" is broader than the "sole purpose" (as results from some case law of the European Court of Justice)[75] or even "the essential purpose" as results from *Halifax*, and is proposed in the Commission Recommendation on aggressive tax planning.[76]

Besides the above-mentioned qualification of the "purpose", the proposed principal-purpose test includes several relevant differences from the EU principle of abuse and from the proposed GAAR in the Commission Recommendation on aggressive tax planning. Under the principal-purpose test, if obtaining the tax benefit was one of the principal purposes of the arrangement or transaction, there is a presumption that the tax benefit is

71. OECD, *Action 6 Deliverable*, *supra* n. 14, at 12.
72. OECD, *Action 6 Deliverable*, *supra* n. 14, at 69 ("To determine whether or not one of the principal purposes of any person concerned with an arrangement or a transaction is to obtain benefits under the Convention, it is important to undertake an objective analysis of the aims and objects of all persons involved in putting that arrangement or transaction in place of being a party to it. What are the purposes of an arrangement or transaction is a question of fact which can only be answered by considering all circumstances surrounding the arrangement or event on a case by case basis").
73. *Cadbury Schweppes* (C-196/04), *supra* n.15, para. 62.
74. *Leur-Bloem* (C-28/95), para. 47; *Foggia* (C-126/10), paras. 34-35.
75. *Ocean Finance* (*Paul Newey*) (C-653/11), para. 46. *See also Amplifin* (C-162/07), para. 28; SK: ECJ, 27 Oct. 2011, Case C-504/10, *Tanoarch s.r.o. v. Tax Directorate of the Slovak Republic*, para. 51, ECJ Case Law IBFD; NL: ECJ, 12 July 2012, Case C-326/11, *J.J. Komen en Zonen Beheer Heerhugowaard BV v. Staatssecretaris van Financiën*, (2012) ECR I-00000, para. 35, ECJ Case Law IBFD.
76. European Commission Recommendation on aggressive tax planning, *supra* n. 12, at 4, point 4.2.

not in accordance with the object and purpose of the tax treaty provision.[77] Such a presumption exists neither in the EU principle of abuse nor in the GAAR proposed in the Commission Recommendation on aggressive tax planning; in light of settled case law of the European Court of Justice, it would most likely be contrary to the fundamental freedoms (it would be disproportionate). There is no reference to "artificiality" or "normal commercial operations" in the principal-purpose test. One example refers to "valid commercial reasons"[78] without defining it. The Commentary on the principal-purpose test makes reference to "bona fide exchanges of goods and services, and movements of capital and persons as opposed to arrangements whose principal objective is to secure a more favourable tax treatment".[79] It is at the very least dubious that a bona fide analysis is adequate to determine tax avoidance or abuse.

Due to its vagueness, a GAAR needs to be progressively articulated so that legal uncertainty is reduced. In contrast, the use of broad principles (such as the bona fide principle) will not contribute to reducing the above-mentioned vagueness and legal uncertainty. In the examples of abuse put forward in the Commentary on the principal-purpose test, either a third state comes into play (so that a tax benefit is obtained)[80] or the taxpayer moves his or her residence shortly before entering into a transaction.[81] If a Member State applied a principal-purpose test to the latter situation, there would be a restriction of a fundamental freedom.

Taking into account the above-mentioned differences between the principal-purpose test and the EU principle of abuse, if the principal-purpose test designed were to be included in tax treaties by EU Member States, some issues of incompatibility with EU law could arise.

However, it is foreseen in BEPS Action 6 that EU Member States may have to adapt the recommendations in Action 6 so that they are compatible with EU law: "[...] some countries may have [...] EU Law restrictions that prevent them from adopting the exact wording of the model provisions that are

77. OECD, *Action 6 Deliverable*, *supra* n. 14, at 66-67.
78. OECD, *Action 6 Deliverable*, *supra* n. 14, at 68-69 (Commentary on the PPT rule, para. 8).
79. OECD, *Action 6 Deliverable*, *supra* n. 14, at 68.
80. OECD, *Action 6 Deliverable*, *supra* n. 14, Ibid. at 67, (Commentary on the PPT rule, para. comm. 5), pp. at 68-69, (Commentary on the PPT rule, para. commentary 8); pp. at 71-72, (Commentary on the PPT rule, para. commentary 14).
81. OECD, *Action 6 Deliverable*, *supra* n. 14, at 70 (Commentary on the PPT rule, para. 12).

recommended in this report".[82] The principal-purpose test provision in tax treaties is complementary to the GAAR under domestic laws proposed in the Commission Recommendation on aggressive tax planning, as they have different scopes. Whereas the principal-purpose test aims to combat abuse of tax treaties, the GAAR under domestic laws aims to combat abuse of domestic law through the use of a tax treaty or an EU fundamental freedom.

On 9 December 2014, the Economic and Financial Affairs Council (ECOFIN) approved an amendment that adds a GAAR to the EU Parent-Subsidiary Directive.[83] The approved GAAR requires Member States to refrain from granting the benefits of the Directive if (i) one of the main purposes of an arrangement is to obtain a tax advantage that would defeat the object or purpose of the Directive and (ii) such arrangement is not "genuine". This recently approved GAAR combines elements of the above-mentioned principal-purpose test under BEPS Action 6 (whether the tax benefit granted is in accordance with the object and purpose of the relevant provisions in the tax treaty; whether obtaining the tax benefit was one of the principal purposes of any arrangement or transaction) and the artificiality test as required by the European Court of Justice and proposed in the Commission Recommendation on aggressive tax planning.

Thus, the GAAR amending the Parent-Subsidiary Directive can now be used as a standard for principal-purpose test provisions introduced by EU Member States in their tax treaties, and this standard requires an analysis of the genuine character of the arrangement.

9.12. Conclusion

Legal pluralism in tax law is currently occurring through the use of international standards, as they result from the OECD/G20 calls for action under the BEPS project. This is true in respect of the tax transparency movement towards automatic and multilateral exchange of information, as well as in respect of the BEPS project.

Both the OECD and the European Union aim to be at the forefront of the process. Even though the EU decision-making process in respect of direct taxes creates true difficulties for a swift and holistic approach, some

82. OECD, *Action 6 Deliverable*, *supra* n. 14, at 9; *see also* at 11.
83. Council Proposal for a Council Directive amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, 16435/14, FISC 221, ECOFIN 1157 (5 Dec. 2014).

amendments to the Mutual Assistance Directive, the Savings Directive, the Parent-Subsidiary Directive and the ATAD have been quickly achieved.

It has also been expected that EU Member States would act by introducing unilateral measures, as was being recommended by the European Commission, until the recent approval of the ATAD. However, unilateral measures will create legal uncertainty due to their vagueness and therefore regional harmonization will reduce the risk of jeopardizing the international tax system.

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