NATIONAL GRID INDUS BV - C-371/10 – JUDGMENT

ROBERT WATERSON

NGI BV made an unrealised currency exchange profit of NLG 22m prior to the transfer of its effective place of management to the UK. Under Dutch law, this profit was deemed to be realised at the time of the transfer and NGI was assessed to tax. The taxpayer argued that this ‘exit tax’ was contrary to the freedom of establishment and contravened EU law.

The Court, agreeing with the taxpayer, ruled that there was a disparity between the tax treatment of companies wishing to move their place of management within the Netherlands (where no exit taxes apply) and those moving to another member state (where they do). The Court opined that the imposition of exit taxes per se may be justified to ensure the balanced allocation of taxing rights but that such rules had to be proportionate for them to be compatible with EU law. The Dutch rules were not. The Court ruled that the national legislation should have given the taxpayer an option either to settle tax liabilities at the time of transfer or defer until such time as the gains became realised.

Infringement proceedings have been commenced by the EU Commission against member states who currently charge exit tax (such as Ireland, Denmark, Spain and Portugal). These countries will now have to review their legislation to ensure compatibility with EU law or amend accordingly.

CFC REFORM

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Responses to the reformed CFC rules, published this week in the draft Finance Bill, have been generally positive. As expected, the old CFC regime will be repealed and replaced with a wholly new system which is likely to come into force after Royal Assent next year.

The new rules will introduce a new ‘Gateway test’ which is designed to take the majority of companies out of the CFC regime altogether. In addition, new ‘safe harbours’ will introduce exclusions for certain categories of profits alongside reformulated entity level exemptions and a low rate Finance Company Exemption (the Treasury is aiming for an effective 5.75% tax rate for intra-group financing by 2014). The Treasury’s stated aim is to improve the CFC regime to better reflect the way that businesses operate in a global economy. Should you wish to make submissions on the draft rules, the consultation period is open until 10 February 2012.
A Spanish bank received interest income in Belgium which was exempt from tax at source under Belgian law. The bank claimed the right to deduct the amount of tax that was due in Belgium, but not actually paid by virtue of the exemption, from its corporation tax liability in Spain. This foreign tax credit was denied by the Spanish tax authorities.

The Spanish Supreme Court referred the question of the compatibility of the tax regime with the free movement of capital, since the national rules had the effect of neutralising the benefit of the tax advantage granted by the Belgian tax authorities for Spanish-established companies investing in Belgium.

The ECJ found that national rules which prohibited the deduction of tax due, but not paid, in other Member States did not contravene EU law. This was subject to the condition that the Spanish provisions did not treat interest obtained domestically more favourably than interest obtained in other Member States. It was for the national court to establish whether this was the case.

It is surprising that the national court felt the need to obtain the ECJ’s guidance in such an obvious “windfall” case, where the taxpayer sought credit for tax never paid. The outcome was less surprising.

A study group, led by Graham Aaronson QC, has recommended that a narrowly focused general anti-avoidance rule (GAAR) be introduced to the UK’s tax system.

In a report, published on 21 November, the study group rejected the introduction of a broad spectrum GAAR for the reason that it would make the UK’s tax system unattractive to business and also that it risked undermining the ability of business and individuals to conduct sensible and responsible tax planning.

The report instead concluded with the recommendation that a moderate GAAR be introduced which is directed at highly abusive artificial arrangements. The report cites a number of benefits in favour of a specifically targeted GAAR including the deterrence of artificial schemes and simplification of tax rules.

It is intended that any GAAR would apply to corporation tax, income tax, capital gains tax, petroleum revenue tax and national insurance contributions.

The study report appended an illustrative draft GAAR and a guidance note.

The Government has stated that it will discuss the recommendations from the GAAR study group with business and tax practitioners prior to responding fully in Budget 2012.

The Chancellor of the Exchequer’s Autumn statement and associated documents contained no surprises in relation to EU law claims. The Chancellor repeated the planned reduction in the Corporation Tax rate to 25% in April 2012. He also announced the publication of the draft CFC rules (see above) and reaffirmed that legislation to prevent the use of Manufactured Overseas Dividends to offset income tax liabilities will be effective from the date of the Written Ministerial Statement of 15 September 2011.

In relation to indirect tax: low value consignment relief (goods from the Channel Islands to the UK mainland) will be abolished from 1 April 2012 and a new exemption for services shared between VAT exempt bodies (including charities and universities) is to be introduced.