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### CJ considers German add-back rules in respect of interest expenses for business tax purposes in line with the Interest and Royalties Directive (*Scheuten Solar*)

On 21 July 2011, the Court of Justice ('CJ') gave its judgement in the *Scheuten Solar* case (C-397/09) holding that the non-deductibility of half of the interest expenses in the calculation of the basis of assessment of the German business tax does not qualify as a forbidden levy of tax on interest payments under the Interest and Royalties Directive. (See: Top News)

### Preliminary question referred to the CJ on the compatibility of Luxembourg net wealth tax reduction with the freedom of establishment

On 13 July 2011, the Luxembourg Administrative Tribunal referred a question to the CJ for a preliminary ruling as regards the compatibility of paragraph 8a of Luxembourg's Net Wealth Tax Act with the freedom of establishment set out under Article 49 TFEU (case n 27380). (See: Top News)

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## Top News

### CJ considers German add-back rules in respect of interest expenses for business tax purposes in line with the Interest and Royalties Directive (*Scheuten Solar*)

On 21 July 2011, the Court of Justice ('CJ'), gave its judgment in the *Scheuten Solar* case (C-397/09), in which it followed the Opinion of Advocate General Sharpston of 12 May 2011 (EU Tax Alert edition no. 93, June 2011).

The case concerns the question of whether the partial non-deductibility of interest expenses for the purposes of the German business tax falls under the scope of Article 1(1) of Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States ('Interest and Royalties Directive'). That provision precludes Member States, in which interest and royalty payments arise, from imposing taxes on those payments, whether by deduction at source or by assessment, where those payments are made to a qualifying beneficiary under the Directive. Under German tax law, business tax (*Gewerbesteuer*) is levied by municipalities on business profits in addition to either personal income tax or corporate income tax. The taxable base of this business tax is determined by reference to the taxable profits calculated in accordance with the personal or corporate income tax rules with certain amounts added back to those profits and others deducted therefrom. These rules provide that half of the interest payments on loans must be added back to the taxable base.

Scheuten Solar Technology GmbH ('Scheuten') is a company established in Germany which manufactures solar panels. Solar Systems BV ('Solar Systems'), which is established in the Netherlands, became the sole shareholder of Scheuten in 2003. Solar Systems had granted Scheuten loans on which the latter paid interest during the fiscal year 2004. The tax authorities assessed Scheuten to business tax in 2004, not allowing 50% of the interest paid to Solar Systems to be deducted from the taxable base, making use of the add-back rule. Scheuten considered that the full amount of the interest should be

deductible and challenged the tax authorities' decision. Upon appeal, the Federal Finance Court referred questions for a preliminary ruling to the CJ.

The most important question in the case is whether an add-back rule which prevents the full deduction of interest expenses can qualify as a forbidden levy of tax on interest payments under the Interest and Royalties Directive.

The CJ examined whether the German legislation falls within the scope of Article 1(1) of the Interest and Royalties Directive. The Court's reasoning is as follows.

It first noted that the business tax is developed in such a way, that the business profit in a given year is first determined in accordance with domestic income tax laws. Thereafter, certain amounts are added or deducted. Additions only relate to amounts which were deducted for purposes of the aforementioned determination of the business profit in the first stage of the calculation. The domestic rules on the basis of assessment of the payer of the interest, such as the rules on the deductibility of certain expenses, are matters left at the discretion of the Member States.

Article 1(1) of the Interest and Royalties Directive, read in the light of recitals 2 to 4 in the recital to the Directive, aims to avoid legal double taxation of cross-border payments of interest by prohibiting the taxation of interest in the source *Member State to the detriment of the actual beneficial owner*, i.e. to the detriment of the creditor (receiving the interest) of the loan and not to the detriment of the debtor of the loan (paying the interest). According to the CJ, this view is supported by the wording of Article 1(10) of the Interest and Royalties Directive, which only refers to the beneficial owner of the interest (or royalties). Another argument is the wording of Article 2(a) of the Directive, which defines interest as 'income from debt claims of every kind'. Only the actual beneficial owner can receive interest which constitutes income from such claims. For the payer the interest that it pays himself is not income.

The CJ continued by stating that the German legislation does not concern taxation to the detriment of the beneficial owner/creditor of the loan. The German legislation only affects the determination of the basis of assessment of the business tax due by the debtor of the loan.

The foregoing leads to the judgment that in the absence of a provision governing the rules for calculating the basis of assessment of the payer of interest, the scope of Article 1(1) of the Interest and Royalties Directive cannot extend beyond the exemption it lays down. Therefore, according to the CJ, the provision does not preclude national tax legislation under which loan interest paid by a company established in one Member State to an associated company in another Member State is incorporated in the basis of assessment of the business tax payable by the former company.

#### *Preliminary comments*

It appears from the judgment that, in general, interest deduction limitations at debtor level, cannot be considered in breach of the Interest and Royalty Directive. This is due to the fact that the scope of the Interest and Royalty Directive is limited to taxation of the interest to be received by the creditor of the loan. If the payer of the interest (the debtor of the loan), is burdened with taxation, this is not covered by the scope of the Directive. Does this mean that all interest deduction limitations at debtor level are in line with EU Law?

No, it does not. It only means that the Interest and Royalty Directive does not prohibit the domestic measure. Such measure would still have to comply with primary EU Law, i.e. the Treaty freedoms. This involves that a measure which discriminates against cross-border interest payments and is attempted to be justified as an anti-abuse measure, would have to pass the test under the EU anti-abuse doctrine as developed in the case law (e.g. *Cadbury Schweppes, C-196/04*). If an anti-abuse measure is of a general nature without the possibility for the taxpayer to provide counter-evidence, such domestic measure might be in breach of EU law after all.

### **Preliminary question referred to the CJ on the compatibility of Luxembourg net wealth tax reduction with the freedom of establishment**

On 13 July 2011, the Luxembourg Administrative Tribunal referred a question to the CJ for a preliminary ruling as regards the compatibility of paragraph 8a of Luxembourg's

Net Wealth Tax Act with the freedom of establishment set out under Article 49 Treaty on the Functioning of the European Union (TFEU) (case n° 27380).

Under paragraph 8a of the Net Wealth Tax Act (NWT Act), a Luxembourg company may benefit from a reduction in net wealth tax if it allocates an amount equivalent to five times the net wealth tax reduction it seeks to obtain as a specific net wealth tax reserve (NWT Reserve). The NWT Reserve must be maintained for five years after its allocation. If it is distributed during that period, net wealth tax becomes payable.

In the case concerned, a Luxembourg S.à.r.l., or private limited liability company (LuxCo), allocated funds to a NWT Reserve for the years 2004, 2005 and 2006 in order to benefit from the reduction under paragraph 8a of the NWT Act, and was granted the benefit of the exemption for 2004 and 2005. In 2006, LuxCo migrated to another EU member State, Italy. The NWT Reserve was kept as a reserve in LuxCo's accounts after the migration. However, the Luxembourg tax authorities issued assessments on the basis that as LuxCo was no longer a Luxembourg resident subject to net wealth tax because it had migrated, it had lost the benefit of the NWT Reserve regime. Consequently, the Luxembourg tax authorities decided to tax the previously conditionally exempt net wealth tax. LuxCo appealed against these assessments. One of the arguments it used was that the taxation of its NWT Reserve owing to its migration was contrary to the principle of freedom of movement within the EU.

The Luxembourg Administrative Tribunal referred the following question to the CJ for a preliminary ruling:

'Should Article 49 TFEU be interpreted as prohibiting a rule such as the one stated in paragraph 8a of the NWT Act which makes the right for a reduction of the net wealth tax contingent upon the fact that the company remains subject to Luxembourg net wealth tax for the subsequent five years?'

## State Aid/WTO

### Dutch air passenger tax cleared

On 13 July 2011, the Commission decided to close its investigation into a complaint about a Dutch air passenger tax, which was repealed mid-2009. The scheme provided for two rates, depending on the final destination being inside or outside the EU. The Commission found the exclusions of other transportation and of air cargo traffic not to result in State aid as those operators were not in a situation comparable to that of air passenger transporters. Furthermore, the exclusion of transfer and transit passengers did not lead to State aid as it intended to create neutrality in respect of the route to be selected to the final destination. The Commission also considered whether the use of fixed tax rates, unrelated to the ticket price, conferred an advantage to classic airlines over low-cost airlines, which it found not to do so.

### Commission opens investigation into Spanish tax benefits for the purchase of ships

On 1 July 2011, the Commission opened a full, formal investigation into a Spanish tax scheme that would allow maritime transport companies to purchase ships at 20 to 30% below market price by buying them indirectly through a contractual and finance structure involving leasing companies and an economic interest grouping (EIG). In order for this scheme to work, certain tax measures that are part of the structure had to be approved beforehand by the tax authorities. After its initial investigation, the preliminary finding of the Commission was that this scheme led to State aid for the EIGs involved, together with their (non-private?) investors and the maritime companies that purchased the ships and possibly also the shipyards and other intermediaries.

### German air passenger tax exemption cleared

On 29 June 2011, the Commission authorized, under the EU State aid rules, a German plan to grant an exemption from air-transport tax to selected groups of passengers flying to and from certain German islands. In January 2011, Germany decided to introduce an air transport tax on all passengers departing from German airports. Residents of seven remote islands as well as civil servants working

there are exempt from that tax, as are medical flights to and from those islands. This exemption concerned islands that faced connectivity problems due to ferries being tide- and weather-dependent in the absence of a connection to the mainland by road or rail. Both the point of departure and of arrival on the mainland should be within 100 km of the North Sea coast or the Baltic coast or of one of the other islands, this in order to restrict the exemption to local traffic. The Commission's approval, received on 29 June 2011, was based on the exemption for aid of a social character granted to individuals, which is rather seldom used. In order to prevent any discriminatory treatment, Germany agreed to extend the tax exemption to flights between the domestic islands and other EEA destinations.

## Direct Taxation

### Commission presents multi-annual EU budget proposing new own resources

On 29 June 2011, the Commission presented its proposal for the multi-annual budget of the EU for the period 2014-2020. In this budget, the Commission proposes the following changes to the system of the EU's own resources:

- Simplify Member States' contribution by ending the complex VAT-based own resource from 2014 to render the system of contributions simpler and more transparent
- Introduce two new own resources: a tax on the financial transactions (FTT) and a modernized VAT in order to facilitate budgetary consolidation in the Member States by reducing their contributions to the EU budget, to bring a new impetus to the development of the Internal Market in the areas of VAT and financial sector taxation
- Reform the correction mechanisms by replacing all existing corrections by a simple and transparent system of lump sums related to the prosperity of the Member States

The Commission explained the reasons for choosing EU taxation of the financial sector and EU VAT as new own resources in the following terms:

- EU taxation of the financial transaction ('FTT'): It would give extra room for manoeuvre to national governments and contribute to general budgetary consolidation efforts. Such taxation exists at national level in some Member States, but action at EU level could prove more effective and efficient, and it could play a role in reducing the existing fragmentation of the Internal Market. The Commission will make this proposal after the summer.
- Modernized VAT: It would create a genuine link between national and EU VAT and foster additional harmonization of national VAT systems. It would provide significant and stable receipts to the EU with limited administrative and compliance costs for national administrations and business. It forms part of a broader recent Commission initiative launched in December 2010 with the issuance of the Green Paper on the future of VAT aimed at reducing the extent of tax-induced distortions in the internal market. Broadening the tax base, reducing the scope for fraud, improving the administration of the tax and reducing compliance costs administrative cooperation in the context of a broad reform of VAT could deliver important results and generate new revenue streams for the Member States and the EU.

The decision on new own resources falls under the Council's competence, which adopts a Decision by unanimous vote, after consulting the European Parliament. In order to enter into force, this Decision must be ratified by all Member States, in accordance with their constitutional requirements.

### Council discusses Polish presidency's work programme and negotiation of Savings Tax Agreements with third countries

At the meeting of the Economic and Financial Affairs Council (ECOFIN) of 12 July 2011, the Polish presidency presented to the Council its work programme on economic and financial matters for its term of office, which runs from July 2011 to December 2011. The Council held an exchange of views on the matter. As regards taxation, the work programme sets out the following objective:

- progress in the areas of savings taxation and anti-fraud agreements with third countries,
- taxation of the financial sector,
- the common consolidated corporate tax base,
- revision of the Energy Taxation Directive
- simplification of VAT rules,
- updating administrative cooperation in the field of excise duties, which will receive priority once a proposal has been received from the Commission.

At the same meeting, the Commission presented a recommendation to the ECOFIN Council for a Council decision authorising it to negotiate changes to agreements signed in 2004 with Switzerland, Liechtenstein, Monaco, Andorra and San Marino on the taxation of savings income. The agreements provide for measures equivalent to those laid down in the Council Directive on taxation of savings income in the form of interest payments.

With respect to electricity tax, the Council adopted a decision authorising Germany to apply, in accordance with Article 19 of Directive 2003/96/EC, a reduced rate of electricity tax to electricity directly supplied to vessels at berth in a port.

As regards other economic and financial affairs, the Council, *inter alia*, concluded the European Semester, which is being implemented this year for the first time as part of a broader reform of the EU's economic governance. The European Semester involves simultaneous monitoring of the Member States' economic, employment and budgetary policies, in accordance with common rules, during a six-month period every year. Accordingly, the Council adopted:

- a recommendation on the implementation of the broad guidelines for the economic policies of the Member States whose currency is the euro;
- for each Member State, a recommendation on its 2011 national reform programme and including an opinion on the 2011 update of its stability or convergence programme.

As regards the Single Market Act (see EU Tax Alert edition 80, June 2010), the Council adopted conclusions on priorities for re-launching the EU's single market. In the conclusions, the Council reiterated that it will examine the

Commission's initiatives on the review of the Energy Tax Directive and a common consolidated corporate tax base for businesses (CCCTB), including with regard to their impact on the functioning of the Single Market

### CJ decides on the tax residence of spouse of EU official (*Gistö*)

On 28 July 2011, the CJ gave its judgement in the *Gistö* case (C-270/10) regarding the interpretation of the first paragraph of Article 14 of the Protocol on the Privileges and Immunities of the European Communities ('Protocol') dealing with the residence for tax purposes of EU officials and their spouses.

Mrs Gistö, a Finnish national, settled in Luxembourg with her family in 2003, when her husband started working as a translator at the European Parliament. Mr and Mrs Gistö have resided in Luxembourg since then. In 2007, Mrs Gistö had no separate gainful occupation in Luxembourg. In Finland, she owns various securities and several investment properties, which she leases. To determine whether, for the 2007 tax year, she still had general income tax liability in Finland, Mrs Gistö applied for a ruling to the Central Tax Commission in Finland. The ruling found that she was still domiciled for tax purposes in Finland pursuant to Article 14 of the Protocol, and that, therefore, she was generally liable to income tax there. Mrs Gistö appealed against that decision to the Supreme Administrative Court of Finland, which, in turn, referred a question for a preliminary ruling to the CJ.

The first paragraph of Article 14 of the Protocol provides that: 'In the application of income tax, wealth tax and death duties and in the application of conventions on the avoidance of double taxation concluded between Member States of the Communities, officials and other servants of the Communities who, solely by reason of the performance of their duties in the service of the Communities, establish their residence in the territory of a Member State other than their country of domicile for tax purposes at the time of entering the service of the Communities, shall be considered, both in the country of their actual residence and in the country of domicile for tax purposes, as having maintained their domicile in the latter country provided that it is a member of the Communities. This provision shall also apply to a spouse, to the extent that the latter

is not separately engaged in a gainful occupation, and to children dependent on and in the care of the persons referred to in this Article.'

Finnish national law provides that a Finnish national is to be regarded as resident in Finland even if he or she does not reside there continuously for more than six months, which status is maintained for three years from the end of the year during which he or she left the country.

Accordingly, under Finnish law Mrs Gistö would have ceased to be a tax resident in Finland by 2007 and thus, she would have only had limited tax liability on income sourced in Finland. However, due to Article 14 of the Protocol, her status as a resident in Finland was maintained even after the expiry of the three-year period set out under Finnish law. The CJ considered that the determination of the spouse's domicile for tax purposes could not depend on the wishes of the person concerned. Therefore, it confirmed that the provision under the Protocol prevails over domestic law to the effect that the former State of domicile is where the spouse of an EU official remains resident for tax purposes as long as he or she is not separately engaged in gainful occupation in the other Member State. That interpretation does not contradict the principle of equal treatment, as from the tax point of view, EU officials and their spouses, insofar as the spouse is not separately engaged in gainful occupation in the Member State in which the official performs his duties, cannot be regarded as being in the same situation as a migrant worker who becomes established in a Member State other than his State of origin.

### Advocate General considers Belgian legislation relating to registration duty payable on the purchase of a principal residence compatible with the EU free movement provisions (*Commission v Belgium*)

On 21 July 2011, Advocate General Sharpston issued her Opinion in the *Commission v Belgium* case (C-250/08).

This case deals with the Flemish region's legislation regarding the payment of registration duty on the purchase of a principal residence in the Flemish Region. Under this legislation, registration duty paid on the purchase of such principal residence in the Flemish Region can be offset against registration duty payable on the acquisition of a

subsequent principal residence within the same Region provided that the sale of the previous principal residence takes place within the two years preceding the subsequent acquisition or within two years after this acquisition (five years if it concerns a plot of land destined for building a principal residence). In contrast, registration duty paid on the purchase of a principal residence situated in another Member State or an EFTA State is not taken into account at the purchase of a subsequent principal residence in the Flemish Region. Given this different treatment, the Commission brought an action against Belgium based on an alleged breach of the freedom of movement (Article 18 TFEU), the freedom of establishment (Article 49 TFEU) and the free movement of capital (Article 63 TFEU).

Firstly, the Advocate General addressed the Commission's arguments under Article 18 TFEU. Because the infringement proceedings are based on legislation relating to the purchase of a private residence, they primarily concern the right of EU citizens to move and reside freely in the territory of the Member States. Under Article 18 TFEU, a citizen of the European Union who exercises the right to move and reside, must be granted the same treatment in all Member States as nationals of those Member States who find themselves in the same situation.

The Advocate General first examined whether or not both categories were comparable and were indeed in the same situation regarding the registration duty. She concluded that it cannot be assumed that this is the case.

If the comparison is made on a wide basis, i.e. between Belgian nationals who reside in the Flemish Region and all EU citizens who might wish to purchase a home in that region, a subdivision needs to be made:

- (i) First-time home buyers: these are all treated in the same manner, i.e. they are not eligible for offset on the first purchase whether or not they have been previously resident in the Flemish region (but both benefit from another advantage, i.e. reduction as regards the basis of assessment of the registration duty).
- (ii) Individuals who subsequently sell their property and buy another property in the Flemish Region: as opposed to Flemish residents, citizens moving from another Member State to the Flemish Region do not benefit from the offset. According to the Advocate

General, this is merely the consequence of fiscal territoriality. On the one hand, no registration duty can be levied by the Flemish Region on property purchased abroad and therefore, no offset is available. On the other hand, the Flemish Region is not obliged to offer persons purchasing a property in the Flemish Region a benefit that is equivalent to the offset they would have received had their next purchase been in the Flemish Region.

- (iii) Individuals that subsequently sell their property and move to another Region in Belgium or to another Member State: neither of them benefits from the offset and they are thus treated alike.

The Commission, however, contended that a narrow comparison must be made between individuals moving to the Flemish Region from another Member State and individuals moving within the Flemish Region. However, according to Advocate General Sharpston, it cannot be assumed that both categories are in the same situation. In order to be considered to be in the same situation, the individual in question must meet the conditions of the disputed measure. One of these conditions is that registration duty or an equivalent tax is paid upon acquisition of the preceding residence. This condition cannot be assumed to be met if an individual moves from another Member State to the Flemish Region. He might not have paid the same or an equivalent duty in that other Member State, since property transfer taxes are not harmonized within the EU, i.e. they differ as to their base, rate, available exemptions and relief mechanism from Member State to Member State. Furthermore, according to the Advocate General, the question of mutual recognition of such taxes is a matter within the domain of the Member States.

The Advocate General then examined whether there was a discrimination against returning residents of the Flemish Region. The question was whether residents of the Flemish Region that have moved to another Member State and return to the Flemish Region after a certain period are treated less favourably in Belgium than if they had not exercised the right of freedom of movement. The Advocate General concluded that any disadvantage which may occur in this situation will follow from the fact that the individual has not purchased a replacement property

within two years, as prescribed by the disputed measure, and not from the exercise of the right of freedom of movement.

Given the above, Advocate General Sharpston found the Flemish Region's legislation not in violation with the freedom of movement.

Secondly, she examined whether or not the Flemish Region's legislation violates the freedom of establishment and/or the free movement of capital.

Although admitting the difference in treatment between persons whose preceding principal residence was situated in the Flemish Region and persons whose preceding principal residence was situated in another Member State, Belgium holds that this difference is not discriminating since the two categories are not in a comparable situation with regard to the registration duty previously paid. Moreover, according to the Belgian government, the need to maintain the cohesion of the tax system justified the fact that only a duty already levied within one jurisdiction can be offset against a duty subsequently levied in that same jurisdiction. Finally, Belgium submitted that the disputed measure was justified by overriding reasons in the public interest.

Advocate General Sharpston agreed with Belgium that no direct or indirect discrimination exists. It is clear that the disputed measure does not discriminate directly on the grounds of nationality. Furthermore, the Advocate General is of the opinion that the disputed measure is not intrinsically liable to affect nationals of other Member States more than Belgian nationals and, thus, does not constitute an indirect discrimination. Indeed, there is a difference in treatment between those buying their first principal residence in the Flemish Region and those buying a subsequent principal residence there. It seems plausible, however, that the less favourable treatment for first-time buyers is more likely to affect residents of the Flemish Region than residents moving from other Member States or EFTA States. After all, people tend to buy their first home in a country or region where they are already resident. Once Flemish registration duty has been paid a first time, all those buying a principal residence in the Flemish Region are given the same treatment.

If the CJ should not agree and decided that the disputed measure does constitute a forbidden restriction of the freedom of establishment and/or the free movement of capital, the Advocate General holds that the justifications contended by the Belgian government cannot be accepted. The restriction could not be justified by the need to maintain the cohesion of the tax system. For that, a direct link needs to exist between the tax advantage concerned and the offsetting of this tax advantage by a particular tax levy. The mere fact that the disputed measure makes the amount which can be offset against the registration duty payable on the subsequent purchase dependent on the amount paid or payable on the preceding purchase does not suffice to create such direct link. This is, in fact, confirmed by the disputed measure itself insofar as no offset is possible once a certain period has elapsed between the sale of the preceding principal residence and the purchase of the subsequent property. Furthermore, the Belgian government has not established that there are indeed overriding reasons in the public interest that could justify the disputed measure.

Regarding the temporal limitation, Advocate General Sharpston sees no reason for limiting the temporal effect of the CJ's judgment as no new interpretation of EU law is involved and the Belgian government has provided no indication of what the financial consequences of the judgment might be.

### **Eurostat publishes statistical information regarding taxation in the Member States**

On 1 July 2011, the Eurostat published the 2011 edition of the Taxation Trends in the European Union. This publication provides information regarding the overall tax-to-GDP (Gross Domestic Product) ratio in the 27 countries of the EU during 2009. In this year, the ratio decreased from 39.3% (in 2008), to 38.4% mainly due to a drop in the GDP rather than to tax cuts.

During the same year, the overall tax ratio in the euro area fell to 39.1%, a decrease of 0.6% in respect of the ratio of 2008. However, this ratio remains high if compared to countries such as the USA and Japan.

It is important to point out that the tax burden varies significantly between the Member States with some ratios in 2009 being less than 30% (Latvia, for example, has a ratio of 26.6%), while others are higher than 45% (Denmark has a 48.1% ratio).

Moreover, between 2000 and 2009, some EU countries suffered falls in their tax-to-GDP ratio (Slovakia, Sweden, Greece and Finland) while others experienced an increase (Malta, Cyprus and Estonia).

In the EU, the largest source of tax revenue is labour taxes (almost half of total receipts), followed by consumption taxes (one third) and taxes on capital (less than one fifth).

One area where the onset of the economic and financial crisis has clearly had an impact was consumption taxation. Most importantly, the average standard VAT rate increased from 19.4% in 2008 to 20.7% in 2011, with about half of the Member States increasing the rate during that period. The VAT rates in the different Member States range from 15.0% (Cyprus and Luxembourg) to 25% (Denmark, Hungary and Sweden).

The average top personal income tax rate fell 7.6 %; however, this decrease is explained mainly by the 20 percentage point drop in Hungary. Also in the case of this tax there are important differences in the tax rates of the different Member States with a range that goes from 10% (Bulgaria) up to 56.4% (Sweden).

A similar phenomenon occurred with the corporate income tax in the Member States whose average tax rate decreased 8.7 points. In this case, the tax rates in the EU range between 10% (Bulgaria and Cyprus) and 35% (Malta).

In order to measure the average tax burden on work income, on consumption and on capital, Eurostat used an average implicit tax rates.

Regarding the tax burden on work income, there was a decrease from 33.8% of the potential tax base in 2008 to 32.9% in 2009. The range among the Member States is between 20.2% in Malta to 41% in Hungary.

In respect of the tax rate on consumption, the general increasing trend which took place between 2001 and 2008 changed, resulting in reduction of 0.5 points for a rate of 20.9% in 2009. The lowest implicit tax rate on consumption was in Spain (12.3%), and the highest was in Denmark (31.5%).

Finally, in respect of the average implicit tax rate on capital, it decreased from 25.2% in 2008 to 24.7% in 2009. Latvia was the country with the lowest tax rate (10.3%) and, once again, Denmark had the highest rate (43.8%).

## Results of consultation on cross-border dividends published

On 18 July 2011, the Commission published the results of the consultation 'Taxation problems that arise when dividends are distributed across borders to portfolio and individual investors and possible solutions', which ran from 28 January 2011 to 30 April 2011 (EU Tax Alert edition no. 89, February 2011). In sum, 33 citizens, 58 organizations and 1 public authority submitted answers to the questions included in the consultation.

## VAT

### Services in respect of betting rendered by principal to commission agent are VAT exempt (*Tiercé France-Belge*)

On 14 July 2011, the CJ gave its judgment in the *Tiercé Franco-Belge SA* case (C-464/10). The activities of Tiercé Franco-Belge SA ('TFB') consisted of the taking of bets. In the course of its business, TFB used a network of local agents called 'buralistes' who were responsible for collecting betters' stakes, registering the bets, issuing betting slips or tickets for betters and paying out winnings. Under a commission contract, TFB was the owner of the business that the 'buralistes' were responsible for managing. The 'buralistes' were paid by means of commission consisting of a percentage of the stakes placed on registered bets after deducting the amount of payments made.

Taking the view that the buralistes worked in the name of TFB and that the commission was subject to VAT, the Belgian tax authorities sent TFB a VAT assessment

increased with fines and interest. TFB was of the opinion, however, that the buralistes had to be considered as commission agents acting in the context of a supply of services exempt from VAT. Eventually the case ended up before the *État Belge*, which court decided to refer preliminary questions to the CJ.

Based on the premise that the buralistes indeed act in their own name, which is for the referring Court to decide, the CJ indicates that a legal relationship is brought about between the *betters* and the buralistes on the one hand, and between the buralistes and TFB on the other hand. Under such circumstances the buralistes, acting as commission agents, are regarded to have received and rendered those services on the basis of article 6(4) of the EU VAT Directive. According to the CJ, if the supply of services in which the commission agents take part are VAT exempt, that exemption also applies to the legal relationship between the principal and the commission agents. When the services rendered by the buralistes to the *betters* are VAT exempt, the services rendered by TFB to the buralistes are therefore also VAT exempt.

### Advocate General concludes that the supply of self-employed persons qualifies as the supply of staff (*ADV Allround Vermittlungs*)

On 28 June 2011, Advocate General Mazák gave his Opinion in the *ADV Allround Vermittlungs AG* case (C-218/10). The business of *ADV Allround Vermittlungs AG* ('ADV') consisted of the supply of self-employed lorry drivers to haulage contractors in Germany and Italy. For the work carried out the drivers invoiced ADV, which in its turn invoiced the haulage contractors with a mark up of between 8% and 20%.

In an audit report, the tax office Hamburg-Bergedorf expressed the view that the services rendered by ADV did not qualify as the supply of staff. According to the tax office, the provision for the supply of staff only covered those situations in which a company made its own workers available. As a result, the tax office indicated that the services were taxable in Germany and that, therefore, ADV had to charge 16% German VAT to its Italian customers. In compliance with the view of the tax office, ADV started

charging German VAT to its Italian customers. Moreover, ADV drew up amended invoices with respect to the invoices it had issued to the Italian customers in the past.

When the Italian customers applied for a refund of the German VAT at the Federal Central Tax Office, this tax office indicated that the services rendered qualified as the supply of staff and that, therefore, the services were not taxable in Germany. In this regard, the tax office claimed that the German VAT indicated on the invoices issued to the Italian customers had been charged incorrectly as a consequence of which, the refund requests of the Italian customers were denied. Subsequently, the Italian customers refused to keep paying ADV the German VAT on the invoices. As a result, ADV had to bear the 16% non-refundable VAT. With its margin being between 8% and 20% ADV eventually had to cease its activities. In the following proceedings, the Finance Court of Hamburg decided to refer preliminary questions to the CJ.

In its first question, the referring Court wished to know whether the provision for the supply of staff as indicated in Article 9(2)(e) of the Sixth EU VAT Directive also covered the situation in which self-employed persons are supplied. In this regard, the Advocate General considered that a literal interpretation does not appear to be conclusive as to whether or not the supply of staff covers the supply of self-employed persons. However, taking into account the purpose of Article 9(2)(e) of the Sixth EU VAT Directive, the Advocate General concluded that there was no objective reason why a distinction should be made between supplies of self-employed persons and the supply of a company's own workers for establishing the place of supply.

Furthermore, the referring Court inquired whether Member States are obliged on the basis of the EU VAT Directive to make sure in national procedural law that the taxability and liability to tax of one and the same service are assessed in the same way in relation to the trader providing the service and the trader receiving it, even where the two traders fall within the jurisdiction of different tax authorities. The Advocate General indicated in this regard that the Member States have to ensure effective judicial protection against the decisions of administrative authorities, but that there is

no obligation to coordinate administrative proceedings so that in every case, a uniform position as regards provisions of EU VAT law is adopted by the authorities concerned.

### Advocate General concludes that debt collection does not have to constitute a service for VAT purposes (*GFKL Financial Services*)

On 14 July 2011, Advocate General Jääskinen rendered his Opinion in the *GFKL Financial Services* case (C-93/10).

*GFKL Financial Services* AG ('GFKL') purchased mortgages on immovable property and debts arising from terminated and matured loan agreements ('the portfolio') from a bank for a purchase price that was much lower than the face value. After the purchase, the portfolio was held for and at the risk of GFKL. A dispute between GFKL and the German tax authorities arose whether GFKL rendered a service for VAT purposes to the bank by taking over the portfolio. Eventually the Federal Finance Court decided to refer preliminary questions to the CJ.

The Advocate General indicated that the bank receives an advantage going beyond the payment of a price that reflects the current value of the debts, which indicates that GFKL is rendering a service to the bank. However, in order to be able to take into account a service for VAT purposes, the service needs to be rendered for consideration. GFKL and the bank did not agree to a commission. Moreover, the difference between the purchase price and face value of the portfolio cannot be said to constitute consideration, because it reflects the actual amount of risk that is being assigned since the debts in question are defaulted debts, according to the Advocate General. Therefore, in the opinion of the Advocate General, GFKL is not receiving any consideration for rendered services. If the CJ should disagree and decide that the price difference does constitute a consideration, the Advocate General has indicated that this consideration is not directly linked to the rendered service. As a result, no service for VAT purposes should be taken into account.

In the event the CJ should disagree and rule that a service for VAT purposes has to be taken into account, the Advocate General indicated that such a service would qualify as debt collection and, therefore, would not be VAT

exempt. VAT would, in that case, have to be calculated on the difference of what GFKL collects from the debtors in the portfolio and the purchase price of the portfolio.

## Customs Duties, Excises and other Indirect Taxes

### CJ rules on the CN classification of malt beer base (*Paderborner Brauerei Haus Cramer*)

On 16 June 2011, the CJ gave its judgment in the *Paderborner Brauerei* case (C-196/10). The case concerns the classification in the Combined Nomenclature (CN) of malt beer base. Paderborner Brauerei is a brewery. In 2002, it purchased a total of 99,847.33 litres, and on 6 and 23 June 2003, a total of 74,745.41 litres, of a 'malt beer base' from Alko International BV in the Netherlands, which it used to produce a mixed drink marketed under the designation 'Salitos Ice'.

According to the information provided by the Finance Court of Düsseldorf, the 'malt beer base' is produced from brewed beer with an alcoholic strength by volume of approximately 14%, which is clarified and then subjected to ultrafiltration, by which the concentration of ingredients such as bitter substances and proteins is reduced. The 'malt beer base' also has an alcoholic strength by volume of 14%. It is a colourless, clear liquid which smells of alcohol and has a slightly bitter taste.

The Principal Customs Office, taking the view that the 'malt beer base' ought to be classified under heading 2208 of the CN, claimed excise duty on the corresponding alcohol from Paderborner Brauerei under point 1 of Paragraph 130(2) of the Law on the monopoly in spirits. Consequently, by decision of 1 August 2003, it imposed on Paderborner Brauerei spirits tax totalling EUR 182,141.49 in respect of the 'malt beer base' purchased by it in 2002 and, by three decisions of 14 July 2003, spirits tax totalling EUR 136,350.74 in respect of the 'malt beer base' purchased on 6 and 23 June 2003.

By decision of 19 June 2009, the Principal Customs Office rejected Paderborner Brauerei's objection to those decisions. Thereupon, Paderborner Brauerei brought proceedings before the Finance Court of Düsseldorf.

In the action in the main proceedings, Paderborner Brauerei contended, in particular, that the 'malt beer base' should not be classified under heading 2208 of the CN. That product, it argued, was not obtained by distillation or the addition of a variety of flavourings or sugar. Rather, it is a product obtained by fermentation, which has been classified in other Member States under heading 2203 of the CN. The product is made from malt and is used, as an intermediate product, for the production of a light beer-based mixed drink. Heading 2203 of the CN, it submits, does not require that the product concerned be a beverage which is intended for direct consumption. Principal Customs Office Bielefeld contested the action and maintained its position that the 'malt beer base' must be classified under heading 2208 of the CN.

In those circumstances, the Finance Court of Düsseldorf decided to stay the proceedings and to refer the following question to the CJ for a preliminary ruling:

'Is the CN, in the version of Commission Regulation (EC) No 2031/2001 of 6 August 2001 amending Annex I to Regulation (EEC) No 2658/87 (OJ 2001 L 279, p. 1) and in the version of Commission Regulation (EC) No 1832/2002 of 1 August 2002 (OJ 2002 L 290, p. 1), to be interpreted as meaning that a product described as a "malt beer base" with an alcoholic strength by volume of approximately 14%, obtained from brewed beer which has been clarified and then subjected to ultrafiltration, by which the concentration of ingredients such as bitter substances and proteins has been reduced, is to be classified under heading 2208?'

The CJ considered that the 'malt beer base' is not obtained purely and simply by fermentation but is thereafter subjected to ultrafiltration. As a result of this additional treatment, the product in question, which is produced from brewed beer, loses the objective properties and characteristics particular to beer. It does not look like beer and it also does not have the bitter taste specific to beer. The objective properties and characteristics of the liquid do not correspond to those of beer coming under heading 2203 of the CN but do, by contrast, correspond to those of ethyl alcohol under heading 2208 or are, in any event, akin to those properties and characteristics.

The CJ ruled that the CN must be interpreted as meaning that a liquid described as a 'malt beer base', such as that in issue in the main proceedings, with an alcoholic strength by volume of 14% and obtained from brewed beer which has been clarified and then subjected to ultrafiltration, by which the concentration of ingredients such as bitter substances and proteins has been reduced, must be classified under CN heading 2208.

### Fight against fakes: Increased customs actions boost protection of intellectual property rights

In 2010, EU Customs seized more than 103 million products suspected of violating intellectual property rights (IPR) at the EU's external borders. According to the Commission's annual report on EU Customs enforcement of IPR published on 14 July 2011, the number of shipments stopped by customs had almost doubled compared to last year, rising from 43,500 in 2009 to almost 80,000 in 2010. The report also gives statistics on the type, origin and transport method of IPR infringing products stopped at the EU's external borders. For the first time, the report also indicates the value of the goods detained which is estimated at over EUR 1 billion. The top categories of articles stopped by customs were cigarettes (34%), office supplies (9%) other tobacco products (8%), labels, tags and emblems (8%), clothing (7%) and toys (7%). Of all detained articles, 14.5% were household products such as shampoos, soaps, medicines or household appliances (hair dryers, shavers, computer parts) which could potentially have health and safety implications for consumers. One of the major trends this year is the growing number of detentions of postal packages.

Regarding the countries of provenance, China continued to be the main source of IPR infringing products, totalling 85% of all IPR infringing articles. Other countries such as Turkey, Thailand, Hong Kong or India accounted for the majority in certain product categories (foodstuffs, beverages other than alcoholic beverages, memory cards and medicines respectively). 90% of all detained products were either destroyed or a court case was initiated to determine the infringement.

## WTO Panel Report on export restrictions of raw material in China

The EU, along with the US and Mexico, had launched WTO dispute settlement proceedings against various export restrictions on raw materials' export from China. The WTO dispute settlement Panel issued its report on 5 July.

The Panel supported the EU's claims against China. Its key findings are:

1. China's export duties imposed on certain raw materials are inconsistent with China's obligations under its WTO Accession Protocol, under which China committed to discipline its export duties. The Panel finds that China cannot revert to the general exceptions of the GATT Agreement to justify these duties. This limitation of China's right to regulate its exports does not mean that China's sovereignty over its natural resources is not respected.
2. The export quotas as imposed by China violate the provision that prohibits quantitative trade restrictions (Article XI of the General Agreement on Tariffs and Trade of 1994). In the Panel's view, China did not demonstrate that these export quotas are justified; they were neither based on the alleged need to prevent a critical shortage of an essential product, nor on the alleged aims of environmental protection and conservation of exhaustible resources (Articles XX (b) and (g) GATT 1994).
3. While the Panel takes due account of legitimate environmental considerations raised by China, it clearly states that these cannot be used as a pretext for restricting exports. Measures that increase the costs of certain raw materials for foreign consumers and decrease to domestic consumers are difficult to reconcile with the goal of protecting the environment or conserving these raw materials.
4. The Panel also upheld the EU's claim that the conditions imposed by China for the allocation of export quotas also violate its obligations under the WTO Accession Protocol. For example, China's authorities have the right to refuse the grant of export quotas to enterprises which, in the Chinese authorities' view, do not possess 'business management capacity'. As there is no

definition of this criterion in Chinese legislation, the panels supports the EU's claim that this allows China to administer its export quota allocation system in a manner that is non-uniform and unreasonable and hence inconsistent with WTO law (Article X:3 (a) GATT 1994).

5. Finally, the Panel finds that China imposed a minimum export price requirement on exporters of certain raw materials which also violates the 'general elimination of quantitative restrictions' contained in Article XI:1 GATT 1994.

## Launch of Phase 2 of the EU-China Smart and Secure Trade Lanes Pilot Project

On 24 June 2011, the EU-China Joint Understanding on Smart and Secure Trade Lanes (SSTL), Phase 2 was signed at the headquarters of the World Customs Organization (WCO). In the EU, the project is coordinated by the Commission and implemented on the ground by the customs administrations of participating Member States. With this signature, Belgium, France, Germany and Italy join the founding members China, Netherlands and UK as project participants. Senior representatives from these administrations, along with representatives for the Commission and China Customs signed the joint understanding at a ceremony in the margins of the WCO Council Session. The SSTL Pilot Project was developed to test the customs to customs pillar of the WCO's SAFE Framework of Standards. The objective of SSTL is to strengthen end-to-end supply chain security based on multi-layered risk management. Controls performed at export are based on joint risk rules, allowing Customs to better target dangerous traffic at the beginning of the supply chain. Thus, safe consignments can be identified and trade facilitation benefits can be provided to legitimate trade. SSTL is also highly valuable for the future development of the SAFE Framework and Globally Networked Customs (GNC).

During phase 1, participating customs administrations developed mutual understanding, trust and engaged in cooperation. Common operating procedures, minimum control standards and risk criteria were successfully developed. The SAFE Framework of Standards was tested in a realistic, operational environment, which involved the shipment of over 5000 containers.

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