

Carina Grindvold

LL.M. European Business Law

2014

“The legality of Exit Taxes within the EU- and the EEA: Where are we now?”

Supervisor: Mr Banggui Jin

Table of content

1. *Introduction*
2. *The EU, the EFTA and the EEA-Agreement*
 - 2.1 *The EU*
 - 2.2 *The EFTA*
 - 2.3 *The EEA-Agreement*
3. *The conflict between exit taxes and Internal Market principles*
4. *To what extent can exit taxes be charged on companies within the EU and the EEA?*
 - 4.1 *The legality of corporate exit taxes within the EU*
 - 4.1.1 *The legal framework for the application of exit taxes on companies within the EU*
 - 4.1.2 *The case law of the ECJ*
 - 4.1.3 *The EU's ability to adopt legislation in the area of exit taxes*
 - 4.2 *The legality of applying exit taxes on companies within the EEA*
 - 4.2.1 *The legal framework for charge of exit taxes on companies within the EEA*
 - 4.2.2 *The case law of the EFTA Court*
 - 4.3 *Can exit taxes on companies be charged to the same extent within the EU and the EEA?*
5. *Analyse of how states convey with EU- and/or EEA exit tax rules for companies*
 - 5.1 *Charge of exit taxes on companies within the United Kingdom*
 - 5.1.1. *Introduction*
 - 5.1.2. *National provisions*
 - 5.1.2.1. *Exit taxes charged on migrating companies*
 - 5.1.2.2. *Exit taxes charged on transferred assets and liabilities*
 - 5.1.3. *Relationship to EU-law*
 - 5.2 *Charge of exit taxes on companies in Norway*
 - 5.2.1. *Introduction*
 - 5.2.2. *National provisions*
 - 5.2.2.1. *Exit taxes charged on migrating companies*

5.2.2.2. Exit taxes charged on transferred assets and liabilities

5.2.3. Relationship to the EEA-Agreement

5.3 Comparison of the different exit taxation regimes applicable on companies in the UK and Norway

6. Conclusion

7. Bibliography

1 Introduction

The compatibility of national exit tax regimes, both by Member States of the European Union (EU) and states that are signatories to tax treaties, has been discussed for some time. In the international sphere is such a tax widely accepted, but within the borders of the Internal Market¹ is it still argued whether exit taxes infringe the internal market principles or not. It is commonly accepted since the *National Grid Indus case*² that exit taxes as such do not infringe the freedom of establishment, but the timing of when the tax is to be paid and on what conditions are still uncertain. However, the European Court of Justice (ECJ) and the Court of the European Free Trade Area (EFTA Court) have ruled in several cases recently concerning exit taxes, including the regimes of the Netherlands, Portugal, Norway, Spain, Denmark and Germany.³ Therefore I will investigate whether the circumstances around charge of exit taxes have become more definite. However, I will only cover exit taxes charged on companies, hereunder exit tax levied on assets and liabilities that are transferred out of a states tax jurisdiction.

The purpose of the thesis is to analyse and discuss to what extent exit taxes that are levied on companies are legal within the EU and the European Economic Area (EEA). I will assess the legal standpoint of the EU and under the EEA-Agreement, and consider their relation to other tax treaties. Further I will scrutinise the domestic exit tax regimes for charge of such taxes on companies of two Member States⁴ and compare them to examine how the Member States may levy such taxes, without violating EU-law and/or the EEA-Agreement. The states that will be assessed are the EU Member States United Kingdom and the EEA Member State Norway. The reason upon the decision of choosing these states is that both United Kingdom and Norway the last few years have been found to have corporate exit tax regimes that have infringed respectively EU-law and the EEA-agreement. I believe it is interesting to see how they have modified their exit tax rules. The aim of the thesis is to clarify the legal situation of corporate exit taxes within the EU and the EEA-area.

Increasing global mobility of taxpayers and individual assets has put taxation of taxpayers' migration from one tax jurisdiction to another on the agenda. In principle have the states fiscal sovereignty and

¹ The Internal Market, also known as the Single Market, is made up by the domestic markets of the 28 EU Member States and three of the EFTA Member States. The market seeks to guarantee the free movement of goods, capital, services and people, i.e. the four freedoms.

² "*National Grid Indus*" case C-371/10.

³ See NL: "*National Grid Indus*" case C-371/10, "*Commission v the Netherlands*" case C-301/11, "*Commission v Portugal*" case C-38/10, NO: "*Arcade Drilling AS v Staten v/Skatt vest*" case E-15/11, "*Commission v Spain*" case C-64/11, "*Commission v Denmark*" case C-261/11 and DE: "*DMC Beteiligungsgesellschaft mbH*" case C-164/12.

⁴ The term Member States will here be used about member states of the Internal Market; the 28 EU Member States and the three participating EFTA Member States: Norway, Iceland and Lichtenstein.

each state is able to determine the scope of their fiscal jurisdiction. Still, in order to avoid double taxation, prevent tax evasion and encouraging cross-border trade efficiency have many states entered into bilateral as well as multilateral agreements to allocate taxing powers. The two most important treaties regarding the principles of exit taxation is laid down in the OECD Model Convention^{5 6} (OECD MC) and the Treaty of the Functioning of the European Union⁷ (TFEU), which both effects the Member States ability to charge exit taxes on migrating taxpayers. Although neither of the treaties contains any provisions specifically addressing the tax consequences of emigrating persons (legal or individual).⁸ Tax aspects are certainly important in a situation where a taxpayer considers migrating to another state. In domestic situations are capital gains generally taxed by the home state of the owner when the value of the asset is realised, i.e. when the asset is sold or otherwise transferred from one party to another. In a cross-border situation on the other hand, may the home state (the emigration state) also impose a tax on unrealised capital gains over the migrating persons assets, which is a so-called exit tax.

Exit taxes, as can be understood from the term “exit”, generally refer to all types of taxes that are charged when a taxable person moves or an asset or liability is transferred out of the home state, or out of reach of the national tax jurisdiction of that state.⁹ The triggering factor for imposing the tax is the change of tax residence or transfer of asset or liability cross-border, i.e. the taxpayer’s, asset’s or liability’s exit of its tax jurisdiction of origin. There are two legal theories that concern a company’s ability to move and/or change tax residency: the incorporation theory and the real seat theory. The incorporation theory connects a company to the jurisdiction in which it has been incorporated, and its existence, internal affairs and dissolution of the company are determined by the state where the company is incorporated.¹⁰ Once a company is correctly incorporated, it is recognised everywhere and the company can transfer its seat of management to another state without losing its legal personality. As long as the company is incorporated in the state, the emigrating company remains subject to the law of that state.¹¹ The real seat theory on the other hand, determines which state has the power to regulate the company’s internal affairs by focusing on the substantial connection between a

⁵ The Organisation of Economic Cooperation and Development Model Tax Convention on Income and Capital (2010).

⁶ The OECD MC provides general principles and definitions accepted by the OECD states, and seeks to allocate taxation power in case of a tie in order to avoid double taxation.

⁷ Consolidated Version of the Treaty on the Functioning of the European Union as amended by the Treaty of Lisbon (2007).

⁸ The same goes for the UN Model Tax Treaty.

⁹ See Professor Frederik Zimmer, article “Exit Taxes in Norway” Word Tax Journal, October 2009 p. 115.

¹⁰ Christiana Hji Panayi, “Exit Taxation as an Obstacle to Corporate Emigration from the Spectre of EU Tax Law”, Cambridge Yearbook of European Legal Studies, Vol. 13, 2010-2011, p. 245-281 at p. 259-260.

¹¹ Ibid.

company and the legal system of which it depends upon for formation and the establishment of legal personality, i.e. where the company has its actual centre of administration.¹² A company has to incorporate in the state where it has its real seat of management, in order to be recognised as a company in that state.

A company's tax residence is determined by one of these two theories, or on a combination of the two. Whether a company transfers its tax residence or not, relies upon how the state of emigration and the state of immigration determines who is a tax resident, i.e. the connecting factor, and accordingly could both transfer of real seat or registered office constitute a transfer of tax residency. None of the theories are preferred over the other, and it is up to the states to decide the connecting factors in order to determine who is a tax resident of the state. As the theories are conflicting is there obviously a risk of double taxation, and in order to solve conflicts have many states become signatories to tax treaties.¹³ The EU has though refrained from taking a stand regarding which theory is more preferable.

The EU has taken measures to facilitate cross-border reorganisations, and it has created EU corporate vehicles (including the EEA); the Societa Europaea (SE) and the Societas Cooperative Europea (SCE). The SE and the SCE are the only legal entities that are allowed to transfer their seat from one Member State to another without being subject to the company law restriction that usually apply to the transfer of seat of a company.¹⁴ The tax issues in relation to cross-border migration remains the same though, and either a SE or a SCE company can become subject to exit taxation.

A company's assets and liabilities can be charged an exit tax if they are transferred out of their state of origin, i.e. home state. For instance, if an asset or liability is transferred from a resident company in state A, to a permanent establishment (PE) in state B, it is likely that state A will charge an exit tax. An exit tax may also be imposed if the transfer goes the other way around, or an asset is transferred from a PE in state A to a PE in state B. The reason for this is that a PE, which is established in another tax jurisdiction than the parent company, is liable to tax in the state where it is established.¹⁵

Exit tax is in essence a tax over unrealised capital gains, and the respectively tax assessment is normally done right before the taxpayer migrates to another tax jurisdiction (the immigration state), that is at the time when the taxpayer is still a resident of the emigration state, or just before the assets

¹² Ibid.

¹³ The OECD MD art 4 (3) puts up a tiebreaker rule in case of conflict, and in the case where a company is resident of two contracting states, shall the company's tax residency be decided upon the real seat theory.

¹⁴ Christiana Hji Panayi "*European Union Corporate Tax Law*" Cambridge tax law series, Cambridge University Press, 2013 p. 326.

¹⁵ Art. 7. OECD MC.

are transferred to the immigration state.¹⁶ Unrealised capital gains are typically the value increase of a company's hidden reserve. Hidden reserves are funds that are not declared on a company's balance sheet e.g. assets and liabilities of the company, in addition to the right to deduct losses on assets and liabilities. Such gains and losses on liabilities will mainly refer to foreign-currency gains and losses. The term assets include tangible, intangible and financial assets. The logic behind exit taxes is typically either a principle of fiscal territory whereby the state taxes unrealised capital gains that accrued within to neutralise tax avoidance schemes. Exit taxes may be labelled as the tax of last chance, as the states cannot enforce their taxing rights once the taxpayer has left its territory.¹⁷

Exit taxes are typically classified in two groups, "immediate exit taxes" and "trailing taxes". Immediate exit taxes are taxes that are imposed shortly before the emigration or transfer of assets, while trailing taxes are extended tax liabilities designed to tax future income and realised capital gains after the taxpayer transferred its residence to the immigration state.¹⁸ Usually will the extended tax liability expire after a limited period of time (normally 5 to 10 years) following the emigration, if the capital gains is not realised.¹⁹ What is important in regard of trailing taxes is that the tax liability is established when the taxpayer is still a resident of the emigration state. This form of taxation however is not common in the international sphere.²⁰

Exit taxes are characterised by the fact that they are materialised by the act of migration to another tax jurisdiction. Member States that charge exit taxes on migrating taxpayers or transferred assets or liabilities clearly violate the Internal Market principles, as the migrating taxpayer or transferred assets or liabilities become subject to a tax that is not levied on taxpayers or transferred assets or liabilities remaining within the Member States borders. Intra-group transfers of assets or liabilities for example, are normally not subject to tax when happening within the same tax jurisdiction.

Yet, charge of exit tax is to some extent accepted, which I will discuss in this thesis. Initially will I give a short presentation of the EU, EFTA and the EEA-Agreement, and then present the coherent conflict between exit taxes and the internal market principles. Following, I will analyse and discuss the approach to corporate exit taxes within the EU and the EEA. Further on I will discuss and compare the

¹⁶ Fernando de Man & Tiiu Albon, "Contradicting Views of Exit Taxation under OECD MC and TFEU: Are Exit Taxes Still Allowed in Europe?", *INTERTAX*, Volume 39, Issue 12, 2011 Kluwer Law International BV, The Netherlands, p. 613-626 at p. 613-614.

¹⁷ Klaus von Brocke & Stefan Müller, "Exit Taxes: The Commission versus Denmark Case Analysed against the Background of the Fundamental Conflict in the EU: Territorial Taxes and an Internal Market without Barriers" published in *ec Tax review* 2013-6 p. 299-304, p. 299.

¹⁸ Above mentioned Fernando de Man & Tiiu Albon.

¹⁹ *Ibid.*

²⁰ *Ibid.*

different exit tax practices in United Kingdom, France and Norway. In the end will I give some concluding remarks on the subject.

2 The EU, the EFTA and the EEA-Agreement

Before I continue I will give a short presentation of the EU, the EFTA and EEA-Agreement.

2.1 The EU

The EU is a regional organisation of 28 Member States²¹ primarily situated in Europe. The organisation can trace its roots back to 1950²², and have since then developed to become a Union of which the majority of the European countries are members, in addition to have expanded its competence areas significantly. The institutional framework now consists of seven institutions: the European Parliament, the European Council, the Council, the Commission, the Court of Justice, the European Central Bank and the Court of Auditors. The Unions ultimate objective is full European integration²³ however; its precise scope is as yet not determined in detail.²⁴ All nationals of the Member States are now also citizens of the Union, and this grants them certain rights.²⁵ The aims and objectives of the Union are many, but overall is it an organisation wanting to encourage European integration by promoting peace, freedom, security and justice without internal frontiers to its citizens, and establish an internal market to encourage economic growth and price stability.²⁶ The Member States have ceded some of their sovereign rights to the EU institutions and have conferred on the Union powers to act independently.²⁷ This distinguishes the EU from other international organisations.

²¹ Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and the United Kingdom, see http://europa.eu/about-eu/countries/index_en.htm (10 April 2014)

²² The French Foreign Minister at the time, Robert Schuman, put forward in his declaration of 9 May 1950 that he and Jean Monnet wanted to bring Europe's coal and steel industries together to form a European Coal and Steel Community, see Professor Klaus-Dieter Borchardt "*The ABC of European Union law*" European Union, 2010, p. 11.

²³ Cf. Treaty of the European Union (TEU) art. 1.

²⁴ See Dr P S R F Mathijsen, "*A Guide to European Union Law*" tenth edition, Sweet & Maxwell, 2010, p 4.

²⁵ The EU has legal personality cf. TEU art. 47. The rights granted to its citizens are regulated in the Treaty of the Functioning of the European Union (TFEU) art. 20-25, and provides, among other rights, the right of citizens to move and reside in the territory of all the Member States cf. art. 20 (2) a) and art. 21 (1), the right to vote and stand as candidate in elections of the European Parliament and in municipal elections on the Member State of residence, under the same conditions as nationals of that State cf. art. 20 (2) b) and art. 22 (1), in addition to the right to diplomatic and consular protection from any other Member State in third countries where their own state is not represented cf. art. 20 (2) c) and art. 23.

²⁶ See the Treaty of the European Union (TEU) art. 1, 2 and 3.

²⁷ See Professor Klaus-Dieter Borchardt "*The ABC of European Union law*" p. 11.

The EU has power to adopt legislation that is directly binding upon the Member States and its citizens, and it has created an own legal system, i.e. the EU legal system is “supranational”²⁸. It follows from the term and the spirits of the Treaties²⁹ that the EU legal system is superior to the national legal systems of the Member States.³⁰ In other words, the Member States cannot adopt legislation contrary to Union law, and the implementation of Union law cannot vary from one state to another.

2.2 *The EFTA*

EFTA is an intergovernmental organisation set up to promote free trade and economic integration to the benefit its Member States.³¹ EFTA is governed by the EFTA Council and serviced by the EFTA Secretariat, in addition to the EFTA Surveillance Authority and the EFTA Court. The organisation was established in 1960³² with the purpose to govern free trade relations among its Member States, and establish an economic counterbalance to the then- European Economic Community (EEC), which is now the EU.³³ EFTA's relations to the EU have been of its core activities from the beginning, and what started as an agreement to link the EFTA Member States to the internal market, have now expanded to also cover additional areas.³⁴³⁵ Not all EFTA Member States are participants to the EEA-Agreement; Switzerland has chosen to not be a part of the EEA, but has instead negotiated several bilateral agreements, including a free trade agreement, with the EU.³⁶ Thus will I neither assess the legal stand on exit taxes within Switzerland nor in the relationship between Switzerland and the EU.

2.3 *The EEA-Agreement*

The EEA -Agreement, which entered into force in 1994, is a treaty that brings together the EU Member States and the EFTA Member States Iceland, Norway and Liechtenstein, in a single market, here referred to as the Internal Market. The agreement does not cover all EU policies in the Internal

²⁸ See Dr P S R F Mathijsen, “A Guide to European Union Law” p 8.

²⁹ TEU and the Treaty of the Functioning of the European Union (TFEU)

³⁰ “Costa v ENEL” case 6-64.

³¹ Iceland, Liechtenstein, Norway, Switzerland see <http://www.efta.int/about-efta/european-free-trade-association> (10 April 2014)

³² EFTA was established by the Stockholm Convention in 1960. The Convention has later been amended, and the latest revision entered into force on June 2002, the Vaduz Convention.

³³ See <http://www.efta.int/about-efta/european-free-trade-association> (10 April 2014)

³⁴ Among others, competition policies cf. the EEA Agreement art. 53-60, state aid cf. art. 61-64, social policy cf. art. 66-71, consumer protection cf. art. 72, environment cf. art. 73-75 and statistics cf. art. 76.

³⁵ Among others, research and technological development, information services, the environment, education, training and youth, social policy, consumer protection, small and medium-sized enterprises, tourism, the audio-visual sector and civil protection cf. the EEA Agreement art. 78.

³⁶ See <http://www.europa.admin.ch/themen/00500/index.html?lang=en> (10 April 2014)

Market.³⁷ The EEA Joint Committee is responsible for the management of the agreement.³⁸ All new EU Member States do also become members of the EEA.³⁹ The functioning of the Internal Market is based on a common set of rules that is binding for all Member States of EU and EEA, consequently is the concept of homogeneity important. This is to be achieved firstly by the timely incorporation of EU legislation⁴⁰ into the EEA-Agreement, meaning that as soon as an EEA-relevant EU legal act has been formally adopted in the EU side, the EEA Joint Committee shall take a decision concerning the appropriate amendment of the EEA- Agreement “with a view to permitting a simultaneous application” of legislation in the EU and the EEA/EFTA States.⁴¹ Whenever a relevant legal act is adopted or amended, a corresponding amendment should be made to the relevant annex of the EEA-Agreement⁴², and then, as the EEA/EFTA States have not transferred any legislative powers to the EEA Joint Committee, must the legal act be implemented in the EEA/EFTA State in accordance with its constitutional requirements.⁴³ This is a rather significant treaty, as the EEA/EFTA States have committed themselves to adopt not only current but also future legislation, which is in fact created through a legislative process where the EEA/EFTA States’ ability to contribute is very limited. Eivind Smith, a Norwegian professor in public law, have said that the agreement is a “constitutional catastrophe”⁴⁴ as the EEA/EFTA states in practices have transferred sovereign powers to the EU.

The participants of the EEA-Agreement are subject to many of the same legal acts, but there are also several differences as the scope of the EU is much bigger than the EEA-Agreement, thus is it relevant to compare the two regarding charge of corporate exit taxes.

3. The conflict between exit taxes and the Internal Market principles

Taxes are an essential mechanism for governments to raise revenues, and exit taxes have become an important part of many states international taxation regimes. Enhanced international integration as a

³⁷ The following policies are not covered: Common Agriculture and Fisheries Policies, Customs Union, Common Trade Policy, Common Foreign and Security Policy, Justice and Home Affairs and the Monetary Union (EMU).

³⁸ The EEA Joint Committee is regulated in Section 2 of the EEA Agreement, art. 92-94.

³⁹ Cf. the EEA Agreement art 128.

⁴⁰ EU legislation is adopted by ordinary or special legislative procedure cf. TFEU art. 289. The formal legislators of the Union are the European Parliament and the Council, but normally they only act upon proposal of the Commission. The EEA/EFTA States are not represented in any of these institutions, and they have little or no formal opportunity to influence the Council or the European Parliament. However, they have the ability to influence at the preparatory stage when secondary EU legislation is amended or a new act is adopted, cf. the EEA Agreement art 102 (1).

⁴¹ Ibid art. 102 (1).

⁴² Ibid art. 102 (2).

⁴³ Ibid art. 103.

⁴⁴ Eivind Smith said this in a public hearing regarding approval of the Schengen agreement at the Norwegian Storting (Parliament) 5 Mai 1997.

result of globalisation has increased corporate cross-border mobility, and consequently has it become relatively easy for companies to relocate in order to benefit from more favourable tax systems. This is especially true for companies operating within the Internal Market, as the fundamental objectives of the Internal Market is to combine the national markets of the Member States in order to create a market without borders, where goods and services can be offered and sold on the same conditions and where persons and capital can circulate freely.⁴⁵ Freedom of establishment⁴⁶ is also among the protected rights, and it requires that economic operators, whether person or a company, are able to carry on an economic activity in any other EEA State under the same conditions as national economic operators. In other words, the purpose of the Internal Market is that even though the activities mentioned are carried out in a cross-border situation, they are to be treated in the same way as comparable domestic situations. Cross-border activities are not supposed to be subject to additional costs or other obstacles just for the fact that they are not entirely domestic transactions.

Tax rules in general and exit taxes in particular represent barriers for the functioning of the Internal Market. The Internal Market is made up by 31⁴⁷ tax jurisdictions, thus become companies migrating or transferring assets or liabilities cross-border subject to the legislation of two or more tax jurisdictions. The risk of discrimination and double taxation increase correspondingly and can make migration appear less attractive as the companies face additional costs when they have to comply with different sets of rules. A tax that makes it less attractive for companies to move and that are only triggered by cross-border migration/transfer, may constitute a violation of the freedom of establishment⁴⁸ and/or free movement of capital⁴⁹.

Nevertheless, exit taxes are regarded as an important tax by many states. An exit tax is, as mentioned, basically a tax charged on capital gains of a company's hidden reserves and can often comprise a big amount of money, as a company's hidden reserves include assets and liabilities, in addition to the right to deduct losses on assets and liabilities. If a state loses its taxing right over income that it is legal entitled to, it could create an erosion of the national tax base. From the perspective of a migrating company or a company transferring an asset cross-border on the other hand, such a tax could create an obstacle. For example: a company wants to migrate to another tax jurisdiction, but in order to do so must it pay off an exit tax. The company lacks capital, and in order to pay off the tax is it forced to sell machinery or immaterial rights such as trademarks or patents, or get a bank loan. This could make it

⁴⁵ See TFEU art 26 and the EEA Agreement art. 1. Freedom of establishment is not mentioned her, surprisingly enough.

⁴⁶ See TFEU art 49-55 and EEA Agreement art. 31-34.

⁴⁷ The 28 EU Member States and the three EFTA Member States.

⁴⁸ Art. 49 TFEU.

⁴⁹ Art. 63 TFEU.

less attractive for the company to migrate, and it may choose to maintain its business in the home state, even though the migration would have been more beneficial for its economic activities.

The main problem with exit taxes in regard to the principles of the Internal Market is that they are not triggered in similar domestic situations. Normally will the value increase of company's hidden reserves not be included in the company's tax base before the assets or liabilities are disposed of or otherwise realised.⁵⁰ In other words, the income of hidden reserves are not taxed the year they arise, but deferred until the capital gain is realised through for example a sale in the open market whereby the taxpayer get capital to pay the tax. Hidden reserves do not only arise when an asset increase in value, but also when the market value of an asset drops below its book value because of being subject to wear and tear or obsolescence, or when intangible assets are created.⁵¹ Intangible assets are usually not included in a company's balance sheet,⁵² but are reported in the income statement. In both situations, capital gains relating to a certain tax year are taxed in subsequent periods either by way of showing the full value of a specific asset in a subsequent period or by depreciation below its fair market value or by simply not showing the asset in the tax balance sheet.⁵³

It is clear that exit taxes may be considered necessary from the states point of view, but such taxes are nonetheless problematic in regard of the Internal Market, which seeks to increase trade and economic relations between the participating states by encouraging cross-border economic activities to increase competition and efficiency. The conflict is evident: on one hand you have the objectives of the Internal Market that prohibits discrimination and restrictive treatment of such cross-border transactions, contra the states who want to protect their national tax base.

4 To what extent can exit taxes be charged on companies within the EU and the EEA?

Here will I first analyse and discuss the legal framework for exit taxes charged on companies at EU law level, i.e. to what extent such taxes are legal within the EU. Further I will continue to analyse and discuss the legal framework for exit taxes applied on companies within the EEA, before I finish up

⁵⁰ Klaus von Brocke & Stefan Müller, "Exit Taxes: The Commission versus Denmark Case Analysed against the Background of the Fundamental Conflict in the EU: Territorial Taxes and an Internal Market without Barriers" published in ec Tax review 2013-6 p. 299-304, p. 299.

⁵¹ Ibid.

⁵² Intangible assets are in general not included in the balance sheet because several intangibles do not belong to the company, e.g. employees and relationships. It can be difficult set the market value of such assets as their value may be closely linked with related assets and the fact that there is no financial transaction creating the intangible asset, as they often are created outside the monetary system, see Mary Adams, November 19, 2010: <http://www.i-capitaladvisors.com/2010/11/19/why-are-intangibles-not-on-the-balance-sheet/>

⁵³ Above mentioned Klaus von Brocke & Stefan Müller, p. 299.

with comparing the two regimes and discuss the differences. Where it is relevant will I consider the position taken by the EU and the EEA in relation to tax treaties, respectively the OECD Model.

4.1 The legality of applying exit taxes on companies within the EU

4.1.1 The EU legal framework for the application of exit taxes on companies

As mentioned, direct taxation have remained a sole function of the Member States, and consequently have direct taxation not been referred to in any of the EU Treaties, neither current nor successive,⁵⁴ thus are tax consequences of migrating persons not specifically addressed either. Nevertheless, EU-law has still managed to heavily influence and control the Member States direct taxation regimes in general, and their ability to tax migrating persons in particular. The Member States are obliged to take any appropriate measure to ensure fulfilment of the obligations arising out of the Treaties or resulting from acts of the institutions of the Union, and refrain from any measure that could jeopardise the attainment of the Unions objectives.⁵⁵ In other words, the Member States have a duty to safeguard the objectives set out by the Union and take the necessary actions in order to make them effective. This is an important principle in regard of exit taxes, as direct taxation has remained with the Member States.

The ECJ is the EU institution that has had most impact on the Member States exit taxation regimes, as I shortly will come back to. However, in the recent years both the Commission and the Council have recognised the problematic effects of exit taxes, and taken actions in order to encourage harmonisation and cooperation between the Member States in the matter. The Commission was the first, and in 2006 it announced a series of initiatives seeking to promote better coordination of the Member States national direct tax systems. In it's Communication on exit taxes⁵⁶ the Commission expressed that the Member States would benefit from a coordinated approach in order to ensure that their national law was in accordance with EU-law, and to ensure better protection of the exit state's tax base. The Commission was also willing to assist the Member States to draw up guidelines, in order to remove discrimination and double taxation, in addition to prevent unintended non-taxation, abuse and tax base erosion. The Council Resolution⁵⁷ on coordination of exit taxes also invites the Member States to cooperate in order to avoid double taxation that could result from cross-border transfer of economic activities by following the same guiding principles regarding definition of "economic activities" and

⁵⁴ See Christiana Hji Panayi "European Union Corporate Tax Law" p. 3.

⁵⁵ Art. 4 (3) TFEU.

⁵⁶ COM/2006/0825: "Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – Exit taxation and the need for co-ordination of Member States' tax policies."

⁵⁷ Council Resolution on coordination exit taxation, 2911th ECONOMIC and FINANCIAL AFFAIRS, Brussels, 2 December 2008.

valuation of assets, e.g. the host State should allow a step-up in the tax base cost when the home State levied an exit tax. Nonetheless, neither communications nor resolutions are legally binding on the Member States i.e. soft law, and they only aim at providing guidance. More relevant nevertheless is the Commission's right to open infringement proceedings⁵⁸ against Member States who fail to fulfil their obligations under the Treaties. The Commission has been diligent, and it has during the latest years requested several member States to amend their legislation regarding exit taxes, and started infringement procedures against Member States that have refused to amend their legislation voluntarily.

4.1.1 The legal framework for the application of exit taxes on companies within the EU

Here will I analyse and discuss the ECJ's case law concerning exit taxes levied on companies. The ECJ's landmark decision regarding exit taxes applied on companies is the *National Grid Indus*⁵⁹ case from 2011. The judgement was based on two lines of case law: one line concerning migrating companies in general, starting with the *Daily Mail*⁶⁰ case from 1988, which later was followed by the *Cartesio* case⁶¹ in 2008, and the second line about exit taxes imposed on migrating individuals starting with the *Hughes de Lasteyrie du Saillant*⁶² from 2004, which later was followed by the *N* case⁶³ in 2006. As the above mentioned cases have been important for the ECJ decisions regarding exit taxes charged on corporations, it is natural to start with these, before I continue with the ECJ decisions concerning exit taxes charged on companies in particular. I will go through the cases in chronological order, before I present my conclusion.

4.1.2 The position taken by the ECJ so far

The *Daily Mail*⁶⁴ case concerned tax law, but it has been important in the context of migrating companies as well. The British company Daily Mail and General Trust PLC decided to transfer its central management and control functions to the Netherlands in order to benefit from lower tax rates. British company legislation permitted companies to transfer their real seat, whilst remaining status as a company of the United Kingdom (UK). The UK tax legislation however, relied on the real seat theory and when a company moved its real seat abroad would the company cease to be a UK tax residence. As a result of the transfer would Daily Mail exit the British tax jurisdiction, and it was therefore asked by the Treasury to sell parts of its assets before transferring its residence. Daily Mail refused to these

⁵⁸ Art. 258 and 260 (2) TFEU.

⁵⁹ Case C-371/10 "*National Grid Indus BV v. Inspecteur van de Belastingdienst Rijnmond/kantoor Rotterdam*" (2011)

⁶⁰ Case 81/87 "*Daily Mail and General Trust*" (1988)

⁶¹ Case C-2010/06 "*Cartesio*" (2008)

⁶² Case C-9/02 "*Hughes de Lasteyrie du Saillant*" (2004)

⁶³ Case C-470/04 "*N v. Inspecteur van de Belastingdienst Oost/kantoor Almelo*" (2006)

⁶⁴ Case 81/87 "*Daily Mail and General Trust*" (1988)

conditions and initiated proceedings before the court, arguing that the British legislation violated its freedom of establishment⁶⁵ because of the exit requirements.

In its judgement, the ECJ started by stating that freedom of establishment, as set out in the then art. 52 and 58 of the EEC Treaty, is a fundamental principle of the Community, and that it secures the right of establishment in another Member State.⁶⁶ Even though the provisions are directed mainly at ensuring that foreign national and companies are treated in the host Member State in the same way as nationals of that State, they also prohibit the Member State of origin from hindering its nationals or a company incorporated under its legislation, the establishment in another Member State.⁶⁷ If the Member State of origin could prohibit undertakings from leaving in order to establish themselves in another Member State, would the right become worthless. The ECJ found that the as the British provisions only required consent from the Treasury when a company was seeking to transfer its real seat out of the UK, while maintaining its legal personality and its status as a UK company, it did not impose any restrictions on a company's right to establish in another Member State.⁶⁸ Moreover, the ECJ pointed out "*unlike natural persons, companies are creatures of the law and, in the present state of Community law, creatures of national law.*"⁶⁹ And further that a company exists only by virtue of the varying national legislation, which determines their incorporation, and functioning.⁷⁰ Therefore, it is up to the Member State to regulate the connecting factor determining whether a company is incorporated in the Member State or not. The freedom of establishment do therefore not give a company, that is incorporated under the law of a Member State, the right to transfer its real seat to another Member State, while retaining its status as a company incorporated under the legislation of its Member State of origin.^{71 72} The ECJ found correspondingly that the British legislation at issue did not violate the freedom of establishment.

In this case, the ECJ recognise that companies are creatures of national law, i.e. companies exists only by virtue of national law. Furthermore, a company has no unconditional right to expatriate from its Member State of origin, while at the same time retain the status as a company of that state. A Member State can yet not hinder a company of another Member State to establish itself within its territory. Entry and exit requirements are accordingly treated differently.

⁶⁵ Article 52 and 58 of the EEC Treaty, but now article 49 and 54 TFEU.

⁶⁶ Case 81/87 "*Daily Mail and General Trust*" (1988) paragraph 17.

⁶⁷ *Ibid.*, paragraph 16.

⁶⁸ *Ibid.*, paragraph 18.

⁶⁹ *Ibid.*, paragraph 19.

⁷⁰ *Ibid.*

⁷¹ *Ibid.*, paragraph 24.

⁷² Freedom of establishment has a very basic wording in the Treaty, and it is set out in the articles 49 and 54 TFEU that companies must have been formed in accordance with the laws of the Member State and have the connecting factor required, in order to benefit from the freedom.

In the *Cartesio*⁷³ case wanted a Hungarian company, Cartesio, to transfer its real seat to Italy, while continuing to have Hungarian law as its personal law. This was not possible under Hungarian law, as it required that a company incorporated in Hungary had to have its real seat in Hungary, in order to have Hungarian law as its personal law. Cartesio claimed accordingly that Hungarian law was contrary to the freedom of establishment as set out in articles 43 and 48 EC.⁷⁴

The ECJ cited the *Daily Mail* case and repeated that companies are creatures of national law and exist only by virtue of the national legislation, which determines its incorporation and functioning.⁷⁵ Consequently have the Member States “power to define both the connecting factor required of a company if it is to be regarded as incorporated under the law of that Member State,” and to deny domestic companies the right to “retain that status if the company intends to reorganise itself in another Member State by moving its seat to the territory of the latter, thereby breaking the connecting factor require under the national law of the Member State of incorporation.”⁷⁶ In other words, the Member States have the power to determine a company’s existence under national law, and to set conditions in order to regulate whether a migrating company maintains to exist under national law. However, one must distinguish between whether a company transfers without reincorporation and change of governing law, or transfers with reincorporation and change of governing law. EU law could govern the second situation, as the company is converted into a form of company that is governed by the law of the Member State to which it has moved.⁷⁷ If the host State allows such transfers, then the home State cannot prevent companies, incorporated under its domestic law, from migrating by for example require winding-up or liquidation of the company.⁷⁸ The Hungarian law at issue prevented a company, incorporated under domestic law, to transfer its operational seat abroad and at the same time continue to be governed by Hungarian law. This was accordingly not a violation of the freedom of establishment.

The ECJ upheld its opinion from the *Daily Mail*⁷⁹ in the *Cartesio*⁸⁰ decision, and it is apparent that the ECJ is unwilling to interfere with national rules to regulating what is recognised as a company confer domestic law, and subsequently which companies may enjoy the right to freedom of establishment, i.e. a company have no right to emigrate while retaining legal registration in its home State, as long as this is prohibited under domestic law. However, both cases prove that one must differ between enter- and

⁷³ Case C-2010/06 “*Cartesio*” (2008)

⁷⁴ Now article 49 and 54 TFEU.

⁷⁵ Case C-2010/06 “*Cartesio*” (2008) paragraph 104.

⁷⁶ *Ibid.*, paragraph 110.

⁷⁷ *Ibid.*, paragraph 111.

⁷⁸ *Ibid.*, paragraph 112.

⁷⁹ Case 81/87 “*Daily Mail and General Trust*” 1988, ECR 5483.

⁸⁰ Case C-2010/06 “*Cartesio*” 2008, ECR I-9641.

exit requirements in the situation where a company transfers its central office to another Member State, as companies exist through national company law. In other words, as long as a company is recognised under the law of one Member State, can another Member State not refuse the company to establish itself within the territory of that Member State. After the *Cartesio*⁸¹ case was there a lot of theories as to what consequences the case would have for the charge of exit taxes.⁸²

The case *de Lasteyrie du Saillant*⁸³ is the first case before the ECJ regarding exit taxation. The case regarded an individual taxpayer transferring his tax resident from France to Belgium. At the time of the transfer the taxpayer, along with his family, held securities conferring entitlement to more than 25% of the profits of a company subject to corporation tax and established in France. The market value of the shares was higher than their acquisition price. The French legislation required the unrealised value increase of the shareholdings to be taxed, because of the transfer of tax residence. The payment of the tax could be deferred until the capital gain was actually realised, but only if the taxpayer provided a guarantee sufficient to ensure recovery of the tax. If the taxpayer still owned the shares after five years would the tax be ignored.

The ECJ consider whether the French tax, which was established solely on the ground of transfer of tax residence outside of France, is capable of restricting the exercise of freedom of establishment.⁸⁴ According to the ECJ, prohibited freedom of establishment the home State from hindering its own nationals the establishment in another Member State⁸⁵, even if the restriction is of limited scope or minor importance.⁸⁶ The French legislation did not prevent French taxpayers from exercising the right to freedom of establishment, but it had at least a dissuasive effect as taxpayers' wishing to transfer their tax residence was treated disadvantageous compared to taxpayers who maintained their residence in France. The tax was triggered only by the reason of such transfer, and if the taxpayer remained in France would taxation of value increases on income be taxed only when, and to the extent that they were actually realised. That different treatment was likely to discourage taxpayers from doing such transfers.⁸⁷

Even though it was possible to benefit from suspension of the payment on strict conditions, including conditions to provide guarantees, would those guarantees in themselves constitute a restrictive effect

⁸¹ Ibid.

⁸² For more about this debate see Christiana Hji Panayi, "Exit Taxation as an Obstacle to Corporate Emigration from the Spectre of EU Tax Law", Cambridge Yearbook of European Legal Studies, Vol. 13, 2010-2011, p. 245-281 at part IV.

⁸³ Case C-9/02 "*Hughes de Lasteyrie du Saillant*" (2004)

⁸⁴ Ibid., paragraph 39.

⁸⁵ Ibid., paragraph 42.

⁸⁶ Ibid., paragraph 43.

⁸⁷ Ibid., paragraph 45-46.

as they deprived the taxpayer from enjoying the assets given as a guarantee.⁸⁸ The French provision was found to be a restriction, and the ECJ then continued to consider whether the restriction could be justified: a restriction can be justified if it pursues a legitimate objective compatible with the Treaty and is justified by imperative reasons in the public interest. It is further necessary, in such a case, that its application is appropriate to ensuring the attainment of the objective thus pursued, and does not go beyond what is necessary to attain it.⁸⁹ The argument that the exit tax rule was justified on the basis of prevention of tax avoidance was rejected. Tax avoidance or evasion could not be inferred generally from the fact that the tax residence of a physical person had been transferred to another Member State.⁹⁰ The argument that the provision of guarantees ensured the coherence of the French system was also rejected, as the French provisions was aimed at preventing temporary transfers of tax residence exclusively for tax reasons. The provisions did not appear however to be aimed at ensuring generally that increases in value are to be taxed, in the case where a taxpayer transfers his tax residence outside France, in so far as the increases in value question are acquired during the latter's stay on French territory.⁹¹ The ECJ also rejected the argument that the restriction was justified because it concerned the allocation of tax powers between the home State and the host State.⁹² The restriction could not be justified and was therefore a restriction that breached the freedom of establishment.

The ECJ seemed in this case to be of the opinion that exit taxes in general can be compatible with EU law, as long as they are imposed under specific circumstances or are subject to proportionate implementing rules. The French legislation went beyond what was necessary as payment of the exit tax was not automatically deferred and the taxpayer had to provide security in order to defer the payment, i.e. deferral must be automatically available for the taxpayer, without having to provide security.

The *N*⁹³ case concerned the Dutch exit taxation rules. The Dutch provisions required that substantial shareholders, i.e. shareholders owning at least 5% of a company's capital, which transferred their place of residence outside the Netherlands became subject to an exit tax. A 10-year deferral of the payment of the tax was granted on provision of security. If the shares were not disposed within the 10-year period were the taxpayer acquitted from their liability and the security released.

Mr N transferred his residence from the Netherlands to the United Kingdom. At the time of the migration was he the sole shareholder of three Dutch limited liability companies, the management of

⁸⁸ Ibid., paragraph 47.

⁸⁹ Ibid., paragraph 49.

⁹⁰ Ibid., paragraph 51.

⁹¹ Ibid., paragraph 63-65.

⁹² Ibid., paragraph 68.

⁹³ "*N v. Inspecteur van de Belastingdiens Oost/kantoor Almelo*" (2006)

which had since that date been in the Netherlands Antilles. Mr N was charged an exit tax on unrealised capital gains. He obtained deferral of the tax as he provided security for the amount. Mr N argued that the Dutch provision restricted his freedom of movement. The ECJ however considered whether the Dutch rules restricted the freedom of establishment.⁹⁴ The Court cited the *de Lasteyrie du Saillant* case, and found that a taxpayer wishing to transfer his residence was treated disadvantageous in comparison with persons who maintained their residence in the Netherlands, because they had to pay tax on unrealised capital gains. Although it was possible to benefit from suspension of payment, that was not automatic and subject to conditions, such as provision of guarantees, would those guarantees in themselves constitute a restrictive effect, in that they deprived the taxpayer of the enjoyment of the assets given as a guarantee. The ECJ also made a point of the fact that decreases in value occurring after the transfer of residence were not taken into account in order to reduce the tax debt, in addition to that the tax declaration required at the time of the transferring residence was an additional formality likely to hamper persons freedom of establishment. The ECJ concluded that the Dutch rules were a restriction the freedom of establishment.⁹⁵

Next, the ECJ assessed whether the restriction could be justified because of legitimate objectives in public interest.⁹⁶ The Dutch legislation was designed to allocate the power to tax increases of value in company holdings between Member States, and to prevent double taxation. The ECJ pointed out that in the absence of harmonising EU legislation could the Member States draw inspiration from international practice, and in particular the OECD MC, in order to allocate their taxation power to eliminate double taxation. The ECJ found that the Dutch provisions were justified by legitimate objectives, and the provisions were appropriate for ensuring the attainment of the objectives.⁹⁷ Then, the ECJ examined whether the provisions were proportionate.⁹⁸ Demand of a tax declaration was accepted, but the obligation to provide guarantees went beyond what was necessary in order to ensure the functioning and effectiveness of such a tax system based on the principle of fiscal territoriality. There were methods less restrictive of the fundamental freedoms, e.g. the Mutual Assistance Directive for the Recovery of Taxes and the Mutual Assistance Directive for Exchange of Information. The ECJ also remarked that in order to be proportionate would the Dutch system have to take full account of reductions in value capable of arising after the transfer of residence, unless the host Member State had already done so.

⁹⁴ Ibid., paragraph 21-22: Freedom of movement and residence for citizens cf. art. 45 TFEU, is a general right, while freedom of establishment cf. Art. 49 TEU specifically addresses the issue at hand.

⁹⁵ Ibid., paragraph 35-39.

⁹⁶ Ibid., paragraph 40.

⁹⁷ Ibid., paragraph 41-47.

⁹⁸ Ibid., paragraph 48.

The ECJ upheld the view expressed in the *de Lasteyrie du Saillant* case, and held that charge of immediate exit taxes are likely to restrict the freedom of establishment. The Member States can impose an exit tax in the event of transfer of tax residence, but deferral must be automatically available. The ECJ also upheld that the obligation to provide guarantee was a restrictive and disproportionate measure, yet an obligation to provide a tax declaration at the time of the transfer was allowed. In regard of the examination of whether the restriction pursued a legitimate objective in the public interest, did the ECJ focus on allocation of taxing rights and found that, as the Dutch provisions were designed to allocate taxation between Member States, it pursued a legitimate objective. This was not accepted as a legitimate objective in the *de Lasteyrie du Saillant* case, as the purpose of the French legislation at dispute was just to prevent tax evasion. The Dutch legislation in the *N* case was on the other hand especially designed to pursue allocation of taxation powers between Member States, and as there was no harmonising EU law had the Member States retained the power to allocate their taxation powers, in order to eliminate double taxation. In the Advocate General's opinion was the different treatment of the French and Dutch legislation also supported.⁹⁹ After finding that the Dutch legislation could be justified continued the ECJ to assess whether the legislation was proportionate. The ECJ found that most aspects with the Dutch provisions could be considered proportionate, but the requirement of guarantees in order to obtain a tax deferral and the fact that the reductions in value after the cross-border transfer were not taken into account did not meet the proportionality test. In regard of the guarantees did the ECJ note that the Member States had less restrictive measures available, as the Mutual Assistance Directive for the Recovery of Taxes and the Mutual Assistance Directive for Exchange of Information, and this would be a much less restrictive of the fundamental freedoms.

In the *de Lasteyrie du Saillant* case and the *N* case was exit taxes accepted in order to safeguard the balanced allocation of taxation powers between Member States, but there are strict limitations regarding the proportionality of such rules. Both cases concerned exit taxes levied on natural persons, the freedom of establishment however, applies equally to legal persons. The arguments above can therefore be made also with respect to exit taxes on companies. This was also supported by the Commission in 2006, in its Communication "*Exit taxation and the need for co-ordination of Member States' tax policies*", where it expressed that "*the interpretation of the freedom of establishment given by the ECJ in de Lasteyrie du Saillant in respect of exit tax rules on individuals also had direct implications for Member States' exit tax rules on companies.*"¹⁰⁰ The Commission also announced that it intended to provide guidance on how the Member States should coordinate their tax policies in order to ensure the compatibility of such rules with EU law, while at the same time safeguarding the

⁹⁹ Advocate-General's opinion paragraph 100-101.

¹⁰⁰ COM/2006/0825: Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – Exit taxation and the need for co-ordination of Member States' tax policies, p. 5.

balanced allocation of taxation powers. The Member States on the other hand, have not yet taken any measures in this regard and no actual coordination has taken place since the Communication was published.¹⁰¹ In the absence of positive measures to coordinate the Member States exit taxation regimes, have negative integration by the ECJ's case law been important to ensure that EU law is not violated. The ECJ however, has refrained from making a distinction between companies and individuals in so far as the protective scope of EU law is concerned,¹⁰² and there still some uncertainty on this matter.

The *National Grid Indus*¹⁰³ case is the first case decided by the ECJ regarding exit taxation levied on companies. In this case a Dutch company, *National Grid Indus BV*, wanted to transfer its place of effective management to the UK. In order to leave Dutch tax jurisdiction was it charged an exit tax on unrealised capital gains on the assets that became subject to transfer. Since 1996 had the company had a claim of GBP 33 113 000 against National Grid Company plc., a company established in the UK. Following the rise in value of the pound sterling against the Dutch guilder, an unrealised exchange rate gain was generated on the claim. National Grid Indus transferred its place of effective management to the UK in 2000, and became as a result resident in the UK. Since National Grid Indus after the transfer no longer had a PE in the Netherlands was only the UK entitled to tax its profits and capital gains.¹⁰⁴ As the company ceased to derive taxable profits in the Netherlands, did the Dutch tax authorities decide that it had to be a final settlement of the unrealised capital gains at the time of the transfer and it had to be paid immediately. The company was taxed inter alia on the exchange rate gain on the claim mentioned above. National Grid Indus refused to accept the final settlement, and claimed that it violated its right to freedom of establishment. The case was brought before the Dutch court, and the ECJ was requested to do a preliminary ruling. The referring court asked essentially whether a company incorporated under the law of a Member State, which transfers its place of effective management to another Member State and is taxed by the former Member State because of the transfer, could rely on the freedom of establishment against that Member State. And secondly, if the first question was answered affirmative, whether it was contrary to the freedom of establishment that the final settlement tax was imposed without deferment and without the possibility of taking subsequent decreases in value into consideration, or if it could be justified by the necessity of allocating powers of taxation between the Member States.

¹⁰¹ Prof. Dr Otmar Thömmes and Dr Alexander Linn "Deferment of Exit Taxes after *National Grid Indus*: Is the Requirement to Provide a Bank Guarantee and the Charge of Interest Proportionate?" INTERTAX, Volume 40, Issue 8/9 2012 Kluwer Law International BV, The Netherlands, p. 485-493 at p. 487.

¹⁰² Christiana Hji Panayi "European Union Corporate Tax Law" p. 315.

¹⁰³ Case C-371/10 "*National Grid Indus BV v. Inspecteur van de Belastingdienst Rijnmond/kantoor Rotterdam*" (2011)

¹⁰⁴ Ibid., paragraph 13.

Initially in regard of the first question, stated the ECJ that a Member State has the power to define, inter alia, the connecting factor required of a company to be regarded as incorporated under its national law, and that the Member State therefore was free to decide whether a company could retain its legal personality under the law of that Member State, and subject it to restrictions on the transfer abroad of the company's place of effective management.¹⁰⁵ Yet, in this case would the transfer of National Grid Indus place of effective management not affect its status as a company incorporated under Dutch law, which applied the incorporation theory,¹⁰⁶ and the company could therefore rely on article 49 TFEU.¹⁰⁷ Conversely, the Court implied here that if a company does not retain its legal personality after transfer of office, as would be the case in a state of origin applying the real seat theory, would the company not be able to invoke article 49 TFEU under the same conditions. This approach creates subsequently a distortion, as situations that appear to be equal will be treated differently because Member States have the sole power to determine the connecting factor required to be recognised as a company under domestic law.

Then the Court continued to consider whether charge of tax on unrealised capital gains constituted a restriction to the freedom of establishment. Here the Court cited the *de Lasteyrie du Saillant* case and *N*, and found that a company transferring its place of effective management outside the Netherlands, was disadvantageously treated in regard of cash flow compared to similar companies retaining its place of effective management in the Netherlands.¹⁰⁸ In domestic situations was capital gains not taxed until the time of realisation, and consequently would the tax charged on unrealised capital gains in a cross-border situation constitute a restriction to the freedom of establishment.¹⁰⁹

Further considered the ECJ whether the restriction could be justified by overriding reasons in the public interest.¹¹⁰ The Netherlands claimed that to safeguard the balanced allocation of taxing powers between Member States could justify the restriction. The ECJ affirmed that this was a legitimate objective,¹¹¹ and that the Dutch legislation at issue was appropriate for ensuring this objective.¹¹² When considering whether the Dutch legislation was necessary or not did the ECJ make a distinction between the establishment of the amount of tax and the recovery of the tax. In regard of the definitive establishment of the tax found the ECJ that it was proportionate to do this at the time of the transfer and added that the Member States was not obliged to take into account value decreases or increases

¹⁰⁵ Ibid., paragraph 27. Here the Court is citing the first the “*Centros*” case, and then the “*Überseering*” case (case C-208/00).

¹⁰⁶ Ibid., paragraph 28.

¹⁰⁷ Ibid., paragraph 32-33.

¹⁰⁸ Ibid., paragraph 37.

¹⁰⁹ Ibid., paragraph 40-41.

¹¹⁰ Ibid., paragraph 42.

¹¹¹ Ibid., paragraph 45

¹¹² Ibid., paragraph 48.

that occur after the transfer, or possible exchange rate gains or losses.¹¹³ This is contrary to its decision in the *N* case where the Court held that a tax system must take full account of decreases in value that may arise after the transfer of residence, in order to be proportionate. Immediate recovery of the tax at the time of the transfer on the other hand, was not considered proportionate. At this point the Dutch legislation went beyond what was necessary, as it did not offer the possibility to defer the payment. Accordingly are immediate exit taxes prohibited conferring the freedom of establishment. The ECJ held that in order to be proportionate must the Netherlands grant an emigrating company the right to opt for deferment of the payment, if the company accepts and is capable of tracing the transferred assets and demonstrating that the company continues to own the assets after the migration.¹¹⁴ Then, the ECJ stated that as the risk of non-recovery of the tax increases over time, could it be proportionate for the Member States to ask for security for example a bank guarantee, in order to defer the payment. Furthermore found the ECJ that deferred payment could be rejected in a situation where tracing the assets would cause “*an excessive administrative burden.*”¹¹⁵ If the company finds that deferred payment will not cause such a burden, then the Member States cannot decide the contrary. The existing machinery for mutual assistance between authorities of the Member States provided the national tax authorities sufficiently measures to deal with the administrative burden in regard of deferred recovery¹¹⁶ and thus was it up to the company to decide whether it would defer the payment or not.

In addition, it was argued that the Dutch legislation at issue could be justified by the need to maintain the coherence of the national tax system.¹¹⁷ The ECJ found that this objective could not justify immediate recovery of the tax, as only the determination of the tax at the time of the transfer was necessary. The risk of tax avoidance was not accepted as a justifying reason either as it could not be set up a general presumption of tax evasion by the mere fact of transfer of a company’s place of management.¹¹⁸ Finally the ECJ concluded that article 49 TFEU prohibited the Member States to charge exit taxes that were due immediately at the time of the transfer.

The *National Grid Indus* judgment is somewhat both similar and different from the ECJ’s cases on exit taxes charged on individuals. As it had done in the *de Lasteyrie du Saillant* case and the *N* case, accepted the ECJ that exit taxes could be justified in order to safeguard the balanced allocation of taxation powers between the Member States, but they can only be levied on certain conditions, e.g. immediate exit taxes are likely to restrict the freedom of establishment. Companies should therefore be

¹¹³ Ibid., paragraph 64.

¹¹⁴ Ibid., paragraph 73.

¹¹⁵ Ibid., paragraph 77 et seq.

¹¹⁶ Ibid., paragraph 78.

¹¹⁷ Ibid., paragraph 79 et seq.

¹¹⁸ Ibid., paragraph 84.

able to choose between immediate- and deferred payment of the tax, as long as it will not be an excessive burden for the company. If the payment is deferred is the recovery supposed to happen at the time when the capital gain is realised, the Court however says nothing about more about the actual time the capital gain is to be considered realised.

If the company decide to defer the payment must it also carry the administrative burden in connection with tracing the transferred assets, and possibly pay interest in accordance with national law.¹¹⁹ The ECJ's mentioning of pay of interest charges was surprising, as it was not considered in the *de Lasteyrie du Saillant* case and the *N* case, or in the Advocate-Generals opinion to the *National Grid Indus* case. The ECJ was very brief on this point, and it is not clear whether the ECJ meant that a Member State can charge interest from the moment of the exit or only from the time the capital gains are realised.¹²⁰ The fact that the ECJ also opened for that Member States could ask for a guarantee was also rather surprising, as it in the *de Lasteyrie du Saillant* case and the *N* case ruled that it was disproportionate to ask for a bank guarantee, but it could be possible to ask for a tax declaration. The condition for being able to ask for charge of interest or a guarantee is that it also is possible in domestic situations. As exit taxes do not exist under national law, is it unclear what may be a comparable situation. Nevertheless, it could be difficult to understand the ECJs position that charge of interest and requirement of a bank guarantee can be allowed. Immediate taxation was found to be disproportionate because it put the company in a disadvantageous situation in regard of cash flow. Yet, if the Member States can require a bank guarantee at the time of the transfer and then later charge interest will the disadvantage on cash flow for the migrating company not be removed, even though the payment is deferred. It could be argued that the taxpayer has a benefit in terms of cash flow in the Member State to which it transfers its place of management, as a result of higher depreciation costs resulting from a step-up on immigration,¹²¹ but Reinout Kok has argued that this argument only is valid if 1) that member State actually grants a step-up and 2) the tax treatment in the host Member State should be irrelevant for the treatment in the Member State of origin. Still, even if a migrating company in theory is given the option between immediate and deferred payment of the exit tax, the reality may be that neither of the options are more attractive than the other.

Future decreases in value are also treated differently in the *National Grid Indus* case compared to the ECJ's decision in the *N* case. Contrary to the *N* case are the valuation of assets that are subject to tax at

¹¹⁹ Ibid., paragraph 73.

¹²⁰ Reinout Kok "Exit Taxes for Companies in the European Union after *National Grid Indus*" ec Tax Review 2012-4, 2012 Kluwer Law International BV, The Netherlands, p. 200-206, at p. 205.

¹²¹ Reinout Kok "Exit Taxes for Companies in the European Union after *National Grid Indus*" ec Tax Review 2012-4, 2012 Kluwer Law International BV, The Netherlands, å. 200-206, at p. 205. See S.c.W Douma in zijn not onder *National Grid Indus*, BNB 2012/40. He is of the view that calculating interest is, for that reason, nut unreasonable.

the time of the transfer, and the Member State of origin is not obliged to take into account decreases in value. This was not found to be disproportionate as the Member State of origin after the transfer had lost its connection with the assets of the company and therefore also the power of taxation on the value of such assets. Hence was it up to the other Member State to take into account any possible value decreases by granting step-up, but it was not an obligation. The ECJ decision in this regard appears to be contrary to the opinion of the Commission and the Council uttered in respectively the Communication on exit taxation¹²² and the resolution,¹²³ which the Member States should cooperate to avoid double taxation, by taking any possible value fluctuations into account. One may also raise the question whether the ECJ actually want migrating individual taxpayers to be stronger protected than migrating companies.

The next case on exit taxes was the *Commission v. Spain*¹²⁴ case on emigrating individuals. The Commission claimed that Spain failed to fulfil its obligations under the TEC regarding free movement of citizens and workers and freedom of establishment¹²⁵, and the EEA-Agreement¹²⁶ regarding free movement of workers and freedom of establishment. Initially the ECJ pointed out that free movement of citizens is a general right that is specified in article 45 and 49 TFEU, hence will it first consider the legislation opposed to article 45 and 49 TFEU and then article 21.¹²⁷ The Spanish legislation at issue required that any income that not previously had been charged income tax were to be levied tax in the last year in which the taxpayer who became a non-resident, was considered a Spanish tax resident. The fact that the Spanish legislation regarded taxation of income that had already been realised but not yet charged tax, makes the case different from the ECJs earlier cases about exit taxes.

The ECJ found that although the Spanish legislation did not prevent a taxpayer resident in Spain to exercise his rights secured by the freedom of movement of workers and the freedom of establishment, was it nonetheless a restriction as it made moving cross-border less attractive.¹²⁸ Taxpayers moving cross border were treated disadvantageous in terms of cash flow, compared to taxpayers that continued to be Spanish tax residents.¹²⁹ The Spanish provisions were therefore found to be liable to obstruct the exercise of the freedoms.¹³⁰ Further the ECJ continued to examine whether the Spanish legislation

¹²² COM/2006/0825: Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – Exit taxation and the need for co-ordination of Member States' tax policies.

¹²³ Council Resolution on coordination exit taxation, 2911th ECONOMIC and FINANCIAL AFFAIRS, Brussels, 2 December 2008.

¹²⁴ Case C-269/09 “*European Commission v. Kingdom of Spain*” 2012

¹²⁵ TEC articles 18, 39 and 43. Now articles 21, 45 and 49 TFEU.

¹²⁶ EEA-Agreement articles 28 and 31.

¹²⁷ *Ibid.*, paragraph 49.

¹²⁸ *Ibid.*, paragraph 56.

¹²⁹ *Ibid.*, paragraph 59.

¹³⁰ *Ibid.*, paragraph 61.

could be justified. The effective recovery of tax debts, the balanced allocation between the Member States of powers of taxation and the need to preserve the coherence of the tax system was discussed as justifying objectives, but neither of the objectives were accepted in order to justify the legislation. Immediate taxation was not necessary to attain any of the mentioned objectives.¹³¹ In relation to effective recovery of the tax cited the ECJ the *National Grid Indus* case, and repeated that the cooperation mechanisms existing at EU level were sufficient to enable the Member State of origin to recover the tax debt in another Member State.¹³² The ECJ implies here that it upholds the distinction between definitive establishment of the amount of the tax and time of recovery.

As regards the existence of a restriction of the free movement of citizens came the ECJ to the same conclusion based on the same reasons; that the Spanish legislation was a restriction also to the free movement of citizens.¹³³

The question of whether there was an infringement of the EEA-Agreement on the other hand, was dismissed. The ECJ found that the Spanish legislation constituted a restriction but it was justified, as Spain did not have any cooperation agreements with the three EFTA states on exchange of information.¹³⁴ Therefore it was both proportionate and necessary to charge an immediate exit tax to ensure the effectiveness of fiscal supervision and the prevention of tax avoidance.¹³⁵

In this judgement, the ECJ did follow its earlier case law on exit taxes imposed on individuals, and it did not mention neither guarantees nor charge of interest, as done in the *National Grid Indus* case.

The following case, *Commission v. Portugal*,¹³⁶ was the question whether the Portuguese exit tax regime infringed the freedom of establishment. Under the Portuguese legislation was a company that transferred its seat of effective management or assets or liabilities to another Member States, taxed on unrealised capital gains, contrary to a company that made similar transactions within Portugal. The ECJ found that the different fiscal treatment clearly caused an obstacle to the freedom of establishment, as companies making cross-border transactions were penalised financially compared with similar companies that maintains its activities in Portuguese territory.¹³⁷ However, the ECJ did not find that the Portuguese provision that provided taxation in a situation where the cessation of activity on Portuguese territory was contrary to the freedom of establishment, as there was no different

¹³¹ Ibid., paragraph 90.

¹³² Ibid., paragraph 68-69.

¹³³ Ibid., paragraph 93.

¹³⁴ Ibid., paragraph 96-98.

¹³⁵ Ibid., paragraph 99.

¹³⁶ Case C-38/10 “*European Commission v. Portugal*” (2012)

¹³⁷ Ibid., paragraph 28.

treatment between situations falling within the scope of article 49 and purely domestic situations.¹³⁸ Then the ECJ assessed whether the restriction could be justified by legitimate objectives and if it was proportionate. The ECJ cited the *National Grid Indus* case and repeated that article 49 TFEU precludes legislation of a Member State which prescribes the immediate recovery of tax on unrealised capital gains relating to assets of a company transferring its place of effective management to another Member State at the very time of the transfer.¹³⁹ Furthermore, the different fiscal treatment of companies transferring cross-border and companies that maintains their activity within the Member State could not be justified by the fact that they are objectively different situations. Moreover would it be less harmful to the freedom of establishment if the Member States gave the transferring company the choice between immediate and deferred payment of the tax, possibly together with interest in accordance with national law. The same conclusion had to be made for taxation of unrealised capital gains relating to assets of a PE situated in Portuguese territory that was transferred to another Member State as well.¹⁴⁰

This judgement is pretty straightforward and ECJ upheld its decision from the *National Grid Indus* case, also regarding the possibility to charge interest. It is clear that charge of exit taxes is a disadvantage for the company transferring activities cross border and constitutes a violation of article 49 TFEU. In addition, immediate taxation is prohibited in so far as the company is not given the choice to defer the payment.

In the case *Commission v. the Netherlands*¹⁴¹ was the Dutch exit tax regime again at issue, and the Commission argued that it was violating the freedom of establishment.^{142 143} Under the Dutch legislation was a taxpayer (company or individual) that transferred its place of management to another Member State, including a Member State of the EEA, charged an immediate tax on unrealised capital gains at the time of the transfer. The ECJ found, based on the proportionality test set out in the *National Grid Indus* case, that the Dutch legislation was a restriction to the freedom of establishment as long as the taxpayer who transferred activities to another Member State had a different fiscal treatment than taxpayers who maintained their business in the Netherlands.¹⁴⁴ Further was it not proportionate to require immediate payment of the tax, in order to safeguard the allocation of taxation powers between Member States.

¹³⁸ Ibid., paragraph 30.

¹³⁹ Ibid., paragraph 31 et seq.

¹⁴⁰ Ibid., paragraph 34.

¹⁴¹ Case C-301/11 “*Commission européenne contre Royaume des Pays-Bas*” 2013.

¹⁴² This case is a continuation of the infringement proceedings against the Netherlands that started with the “*National Grid Indus case*” in 2011.

¹⁴³ Case C-301/11 “*Commission européenne contre Royaume des Pays-Bas*” 2013, paragraph 23.

¹⁴⁴ Ibid., paragraph 14.

This decision was also rather forthright and respected the *National Grid Indus* case. The judgment did not come as a surprise, as the Netherlands following the *National Grid Indus* case had recognised the need to amend its exit tax legislation. Still, it had failed to amend its legislation in timely manner and consequently did the ECJ find that it had failed to fulfil its obligations under the Treaties. The ECJ pointed out in the judgement that although the Netherlands had acknowledged the violation, was it not relevant to the result of the infringement proceedings, as the important factor was the content of the law at the time of the infringement proceeding.

The *Commission v. Spain*¹⁴⁵ case concerned the Spanish exit taxation regime. Under the Spanish law was a taxpayer that transferred his residence from Spain to another Member State, or stopped the activities of a PE in Spain or transferred assets from this PE in Spain to another Member State charged an exit tax on unrealised capital gains. Similar transactions made within Spain had no immediate tax consequences. The ECJ had to assess whether the provisions infringed the freedom of establishment confer article 39 TFEU. The ECJ found that taxpayers that became non-residents or transferred activities to another Member State was treated disadvantageous compared to taxpayers that made the same transactions within Spanish territory, because of the different fiscal treatment.¹⁴⁶ Although the Spanish law did not prohibit migration or transfers abroad, was it still likely that such transferred would be considered less attractive and thus prevent cross border activities. The different treatment could not be justified by the fact that the situation was objectively different.¹⁴⁷ However, the ECJ found that the Spanish provision that charged a tax in a situation where a PE ceased it's activities in Spain was not treated differently from a purely domestic situation, and therefore did not constitute a restriction to the freedom of establishment.¹⁴⁸ Then the ECJ continued to examine whether the legislation could be justified.¹⁴⁹ The ECJ restated that it was within the right of the fiscal competence of the Member States to tax unrealised capital gains that had accrued within its territory when a company migrates and/or transfer assets. Immediate taxation was, however, not proportionate, as there are less restrictive measures available e.g. the mutual assistance directives. The ECJ concluded that the Spanish legislation, which levied immediate tax on companies transferring their residence or assets to another Member State, was contrary to the freedom of establishment.¹⁵⁰

This judgment is in line with *National Grid Indus* and later judgments on exit taxes charged on companies.

¹⁴⁵ Case C-64/11 “*Commission européenne contre Royaume d’Espagne*” 2013

¹⁴⁶ *Ibid.*, paragraph 22 et seq.

¹⁴⁷ *Ibid.*, paragraph 29.

¹⁴⁸ *Ibid.*, paragraph 30. Citation of the “*Commission v. Portugal*” case.

¹⁴⁹ *Ibid.*, paragraph 31 et seq.

¹⁵⁰ *Ibid.*, paragraph 40.

In the *Commission v. Denmark*¹⁵¹ case was the Danish exit taxation regime at issue. Under Danish legislation was an exit tax charged on the unrealised capital gains of assets that were transferred to another Member State of the EU or a third country, that were part of the EEA-Agreement. The Commission argued that this was contrary to the freedom of establishment conferred by article 49 TFEU and article 31 of the EEA-Agreement. The ECJ examined first the legislation opposed to article 49 TFEU, then to article 31 of the EEA-Agreement. Initially noted the ECJ that all restrictions to freedom of establishments are prohibited conferred by article 49 TFEU, and that it follows from this freedom that companies are to be ensured national treatment both by their home state and host state.¹⁵² National measures that make it less attractive to exercise this freedom are to be considered restrictions.¹⁵³ The ECJ found that the Danish legislation was a restriction to article 49 TFEU, as taxpayers transferring assets to another Member State became subject to a tax that was not triggered in similar domestic situations. The different treatment was likely to make cross-border transfers less attractive, and the different treatment could not be explained by the fact that the situations were objectively different.¹⁵⁴

Further the ECJ considered whether the Danish provisions could be justified and if it was proportionate.¹⁵⁵ Firstly the ECJ cited the *National Grid Indus* case and stated that immediate exit taxation on unrealised capital gains of assets in a company that transfers its seat of management to another Member State are disproportionate to safeguard the objective of ensuring coherence in the national tax system. Denmark had claimed that the ECJ in its decision in the *National Grid Indus* case¹⁵⁶ had presumed that the transferred assets actually were realised, and further that when the tax on unrealised capital gains was triggered by assets that were not supposed to be realised after the transfer, was it consequently proportionate according to the objective - of ensuring the allocation of taxation powers between Member States - to collect the tax at the time when the company transferred its assets to another Member State.¹⁵⁷ Such a narrow interpretation was clearly rejected by the ECJ. However, the ECJ stated that in a situation where a transferred asset possibly would not be sold when it arrived

¹⁵¹ Case C-261/11 “*Europa-Kommissionen mod Kongeriget Danmark*” 2013

¹⁵² *Ibid.*, paragraph 25 et seq.

¹⁵³ *Ibid.*, paragraph 27. Citation of the “*National Grid Indus*” case.

¹⁵⁴ *Ibid.*, paragraph 30-31. Citation of the “*Commission v. Portugal*” case.

¹⁵⁵ *Ibid.*, paragraph 32.

¹⁵⁶ Case C-371/10 “*National Grid Indus BV v. Inspecteur van de Belastingdienst Rijnmond/kantoor Rotterdam*” 2011, ECR I-0000, paragraphs 68 and 70. In short that deferred payment of the tax debt until the time of actual realisation of the capital gains will avoid the cash flow problems that come with immediate recovery. However, the asset situation of a company may appear so complex that an accurate cross-border tracing of the destiny of the assets until they are realised, can constitute an excessive burden for the company in question.

¹⁵⁷ Case C-261/11 “*Europa-Kommissionen mod Kongeriget Danmark*” 2013, paragraph 33 et seq.

to the host state, would that not in itself make the home state lose its power to collect the tax debt, which had been finally established at the time of the transfer.¹⁵⁸ The ECJ stated in paragraph 37 that:

“The Member States – which are entitled to tax capital gains that have accrued while the assets in question were located within their territory – are therefore entitled to provide an alternative criterion for the taxation than the actual disposal in order to ensure the taxation of assets, which are not intended to be realised, and that are less restrictive of the freedom of establishment than taxation at the time of the transfer.”¹⁵⁹

The ECJ clearly stated that the conclusion from the *National Grid Indus* case comprises all assets and that the Member States are entitled to provide an alternative criterion for recovery of the tax, other than at the time the asset is sold. This is nonetheless limited to assets that are not expected to be realised. Further, the ECJ stated that it was up to the Member States themselves to decide on the alternative criterion, because the tax debt nevertheless was finally established at the time of the transfer.¹⁶⁰ The ECJ concluded that the Danish legislation infringed article 49 TFEU.

Next the ECJ examines whether the Danish legislation violated article 31 of the EEA-Agreement. The ECJ remarked initially that article 31 of the EEA-Agreement is identical with article 49 TFEU, and that they must be interpreted identically. However, case law of the Union regarding restrictions on the right of free movement within the Union cannot be transmitted in its entirety to the freedoms, which are guaranteed by the EEA-Agreement, as the exercise of these freedoms form part of a different legal context.¹⁶¹ The ECJ found that the Danish provision was a restriction to the freedom of establishment conferred by article 31 of the EEA-Agreement. Then the ECJ continued to assess whether the restriction could be justified by the objective to ensure effective recovery of the tax, and if the provision was proportionate and necessary.¹⁶² First the ECJ remarked that the Danish provision covered transfer of assets from a PE for a company that was established on Danish territory, thus would such a company maintain to be subject to Danish tax jurisdiction. The transfer in itself would therefore have no effect on Denmark's possibility to collect the necessary information for the tax debt to be determined, and to recover the claim if the company not voluntarily paid the owed debt. In this situation was it thus not necessary to make use of a scheme concerning tax assistance, which the third country that was a part of the EEA-Agreement, had assigned to. The ECJ found consequently that the Danish provision violated article 31 of the EEA-Agreement.

¹⁵⁸ Ibid., paragraph 36.

¹⁵⁹ The authors own translation.

¹⁶⁰ Ibid., paragraph 38.

¹⁶¹ Ibid., paragraph 44.

¹⁶² Ibid., paragraph 46.

This case concerned both article 49 TFEU and article 31 of the EEA-Agreement, and the Danish legislation was found to be a restriction to both. The ECJ stated that to justify such a restriction was it already clear from previous case law that immediate exit taxes goes beyond what is necessary, in order to ensure the coherence of the national tax system. Yet, the ECJ did add a new important element regarding the proportionality of exit tax regimes. The ECJ expressed clearly that the conclusion from the *National Grid Indus* case applies to all assets also those that were not intended to be disposed.¹⁶³ The Member States are however entitled to provide an alternative criterion in order to collect the tax debt from such assets. This is though an exception as the rule is that deferral must be offered for all assets until the capital gain is realised. The ECJ did not give any examples of what could be an alternative criterion, but the criteria had to be less restrictive than immediate payment. Neither an obligation to provide securities nor the possibility to apply interest charges was mentioned in this case.

The ECJ's most recent case on exit taxes is the *DMC Beteiligungsgesellschaft mbH v. Finanzamt Hamburg-Mitte*¹⁶⁴, which was published in January this year. The case concerned a reorganisation under German law, and the core facts were that two Austrian corporate partners, in a German limited partnership, exchanged their partnership interests with a German company in return for shares in the latter. Germany did not have right to tax the capital gains on the shares received because of a double tax treaty with Austria. Yet, the German tax authorities issued a tax assessment to the German company in which they taxed the interests contributed by the two Austrian companies at their concern value, not at their book value, thus giving rise to taxation of the unrealised capital gains on the interests transferred to the German company. If the partners had been German residents would the assets have been transferred at book their value. The German law did however provide for an optional interest-free deferral of the payment over a five-year period, as long as security was provided. The German tax court of Hamburg asked for a preliminary ruling, and the questions that were asked were in short if it was compatible with the freedom of establishment to I) tax the unrealised capital gains on assets contributed to a capital company at their concern value and II) offer an interest-free five- year deferral of the tax debt, as long it was provided security for the payment.

Initially the ECJ examined what Treaty freedom the German provision should be linked. All the interested parties, also the referring court, agreed that the facts of the case had to be connected to the freedom of establishment. The Commission on the other hand was of the view that the German provision had to fall within the scope of the free movement of capital confer article 63 TFEU. The ECJ found, after assessing the purpose and application of the German provision, that the more relevant freedom was free movement of capital.¹⁶⁵

¹⁶³ Ibid., paragraph 37.

¹⁶⁴ Case C-164/12 “*DMC Beteiligungsgesellschaft mbH v. Finanzamt Hamburg-Mitte*” 2014.

¹⁶⁵ Ibid., paragraphs 28-38.

Then the ECJ continued to consider whether the German provision constituted a restriction to article 63 TFEU. The ECJ found, citing the *National Grid Indus* case, that the German legislation constituted a restriction that in principle was prohibited by article 63 TFEU, as investors that no longer were liable to tax in Germany was disadvantageously treated in the terms of cash flow, compared to investors that maintained to be German taxpayers.¹⁶⁶ Further, the different treatment could not be explained by the fact that they were objectively different. Next the ECJ assessed whether the restriction could be justified by overriding reasons in the public interest.¹⁶⁷ According to the German court was the purpose of the German provision to ensure the balanced allocation of taxation powers between Member States in accordance with the principle of territoriality. Germany sought to exercise its power to tax capital gains generated in its territory that, as a consequence of a bilateral agreement, could not be taxed by Germany at the time when the capital gains were actually realised.¹⁶⁸ The ECJ remarked that the preservation of the balanced allocation of taxation powers between Member States was a legitimate objective, and that in the absence of any unifying or harmonising measures of the EU, had the Member States retained the power to define how to allocate such powers.¹⁶⁹ Citing the cases *National Grid Indus* and *Commission v. Denmark*, did the ECJ find that the German provision could be justified, as for the fact that the conversion of an interest in a limited partnership into shares in a capital company had the effect of removing income from the Member State where the income was generated, as long as the amount of payable tax was established at the time of the conversion.¹⁷⁰ On the other hand, the objective of preserving the balanced allocation of taxation powers could only justify legislation such as the German provision if the home state actually was prevented from exercising its power to tax such income.¹⁷¹ In this case was the ECJ unsure whether Germany actually lost its power to tax the partnership interests at issue, and stated that it was for the national court to determine whether Germany would actually lose its taxing rights or not in this case.¹⁷² Hence concluded the ECJ that the restriction could be justified by the objective of preserving the balanced allocation of taxing rights between the Member States.

The second question concerned whether the German legislation at issue went beyond what was necessary to attain the objective of preserving the balanced allocation of the power to impose taxes between Member States, having regard, in particular to the deferral provided for under the German provision. Initially the ECJ notes that it is proportionate for the Member States to determine the tax on

¹⁶⁶ Ibid., paragraphs 40-43.

¹⁶⁷ Ibid., paragraphs 44.

¹⁶⁸ Ibid., paragraphs 45.

¹⁶⁹ Ibid., paragraphs 44-47.

¹⁷⁰ Ibid., paragraph 55.

¹⁷¹ Ibid., paragraph 56.

¹⁷² Ibid., paragraph 57-58.

unrealised capital gains at the time when the Member States taxation powers ceases to exist.¹⁷³ Yet, in regard to the collection of the tax found the ECJ, while citing the cases *National Grid Indus* and *Commission v. Portugal*, that the taxpayer should have the choice between immediate payment and deferred payment, possibly together with interest in accordance with national law.¹⁷⁴ The ECJ found that the German provision was proportionate in order to attain the objective, as it provided for the option to spread the payment of the tax debt over a period of five years and without having to pay interests, since the risk of non-recovery increases over time.¹⁷⁵ Additionally, the ECJ did also find that the risk of non-recovery could justify the requirement of a bank guarantee. The ECJ stated however that as such guarantees in themselves constitute a restrictive effect, can they not be imposed without prior assessment of the risk of non-recovery.¹⁷⁶ Consequently concluded the ECJ that the German legislation did not go beyond what was necessary, and thus was it compatible with article 63 TFEU.

Overall, the judgement is in line with the ECJ's previous cases on exit taxes charged on companies. Reorganisation was treated the same as migration, as the unrealised capital gains of the partnership assets, because of the exchange, were removed from German tax jurisdiction. The ECJ accepted that the assets market value was used to calculate the tax, and the deferral provided under German law was proportionate. Opposed to the ECJ previous case law on exit taxes was the freedom at issue in this case article 63 TFEU; free movement of capital. Then again, the ECJ's examination of the case at issue is similar to the examination done in preceding exit tax cases, where the relevant freedoms have been freedom of establishment or freedom of movement.

The main question within the case was whether the deferral method chosen was proportionate: a five-year interest-free deferral if security is provided, instead of a pending deferral that is to be paid at the time when the capital gain is realised. Initially, as found in the *National Grid Indus* case, can it be proportionate for a Member State to levy an exit tax when a taxpayer or asset ceases to be subject to the Member States tax jurisdiction, for the purpose of maintaining a balanced allocation of taxing powers. Still, the taxpayer must have the choice between immediate- and deferred taxation. The idea was that the administrative burden connected to tracing the assets and proving their existence, could ought weight the disadvantage of having to pay the tax at the time of the transfer, and that in such a case would immediate taxation be as proportionate as deferral. The problem arises when the assets in question typically not will be sold. This issue has been up for discussion earlier¹⁷⁷, but the ECJ have refrained from giving a clear answer. In this case however, the ECJ found that as the risk of non-

¹⁷³ Ibid., paragraph 60.

¹⁷⁴ Ibid., paragraph 61.

¹⁷⁵ Ibid., paragraph 62-64.

¹⁷⁶ Ibid., paragraph 65 et seq.

¹⁷⁷ Advocat-General Kokott's opinion to the "*National Grid Indus*" case and the "*Denmark v. Commission*" case.

recovery increases over time was it both proportionate and satisfactory to spread the payment of the tax over a period of five years. The ECJ does not say why exactly five years are a proportionate solution. Yet, if a deferral of five year is accepted, a deferral over a longer period should be accepted as well, as it would be less burdensome for the taxpayer.

The mechanism of a phased deferral seems to have been accepted because of the fact that some capital gains are realised over time, as they are depreciated. Normally when deferral is given is the tax to be paid at the time of disposal. Still, if the asset at hand is typically not disposed is the risk of non-recovery evident. Thus, it can be proportionate to provide a phased deferral, in order to attain the objective of a balanced allocation of taxation powers.

The German provision required providing of security, in order to be granted deferral. The ECJ referred to the risk of non-recovery also here, to justify this requirement. Yet, the ECJ stated clearly that as a matter of principle could guarantees not be required, without a prior assessment of the risk of non-recovery. The ECJ did give some implicit guidelines on how this assessment should be made; the risk of non-recovery must be assessed in the light if the unrealised capital gains and the form of asset. In this case was the assets, namely shares in a German capital company, held by two companies registered in Austria, considered to be such a situation that could justify the requirement to provide security. In this case was the number of assets limited to one type of assets, but it is not clear of this implies the need for security or not.

Post this judgment is there still outstanding questions regarding charge of exit taxes, mainly regarding charge of interest and subsequent value increases. The German law in this case provided an interest-free deferral, but to this was only mentioned by the ECJ. The issue regarding subsequent value drops on the other hand was not mentioned at all.

Conclusion

From preceding case law is it clear that exit taxes constitute an infringement of the freedom of establishment in article 49 TFEU, free movement of capital in article 63 TFEU and article 31 of the EEA-Agreement. It is also clear that an exit tax can be accepted in order to attain the objective of the balanced allocation of taxation powers between the Member States, in accordance to the principle of territoriality linked to the temporal component, as the Member States simply exercise its power to tax capital gains that has accrued within its territory.¹⁷⁸ The main issue concerning exit taxes is that the tax must not go beyond what is necessary to attain the pursued objective, i.e. the tax must be both

¹⁷⁸ See the cases “*National Grid Indus*” C-371/10 paragraph 45-47 and “*Commission v. Spain*” C-64/11 paragraph 31.

proportionate. When considering whether an exit tax is proportionate or not, it must be made a distinction between establishment of the tax debt and the recovery of the tax. It is proportionate to establish the tax debt at the time the taxpayer or asset exits the home states tax jurisdiction, and ignore changes in value of the assets after the exit.¹⁷⁹ However, to always require immediate recovery of the tax debt is disproportionate. In order to be proportionate must the national legislation offer a company the choice between immediate- and deferred recovery of the tax debt.¹⁸⁰ Immediate payment may create a disadvantage for the company in the terms of cash flow, but the company will avoid the administrative burden that is connected with deferred payment, hereunder tracing the assets.

The ECJ has also found that it is possible for the Member States to charge interest in accordance with national law and to ask for security for the payment in order to grant deferral. Yet, it is still uncertain under what conditions such requirements can be proportionate. In the *DMC Beteiligungsgesellschaft mbH v. Finanzamt Hamburg-Mitte* expressed the ECJ that as a matter of principle could guarantees not required without a prior assessment of the risk of non-recovery i.e. guarantees cannot be a fixed requirement but can be accepted after an individual assessment of the case at hand. In this case the EJC did also give some guidelines in regard of deferral e.g. that a phased interest-free deferral over five years if security is provided, could be proportionate. Nevertheless, under what conditions deferral can be granted is still not clear.

4.1.3. The EU's ability to adopt legislation in the area of exit taxes

EU- law and the ECJ have had a great impact on the Member States ability to impose exit taxes on companies, though have it not yet been produced any EU legislation directly addressing exit taxes applied on companies. It is likely to think that this is because the Union lacks legislative powers, but that is not the case. It is correct that there have never been an explicit legal base for harmonisation of neither direct tax in general nor exit tax charged on companies in particular, but the EU has still the power to interfere. The TFEU contains several flexi- clauses that can be used as legislative bases in order to adopt harmonising legislation to ensure the functioning of the Internal Market. The relevant articles here are article 115 to article 117 and article 352 TFEU. Article 115 and article 352 are yet the only articles that have been used as legal base for harmonisation of direct taxes and their use are strictly controlled by the ECJ.¹⁸¹ Neither of the articles has been used to harmonise exit taxation of companies though, and in this part will I discuss the reasons for this.

¹⁷⁹ See the cases “*National Grid Indus*” C-371/10 paragraph 86, *Commission v. the Netherlands* 301/11 paragraph 16, “*Commission v. Spain*” C-64/11 paragraph 31, *Commission v. Denmark* 261/11 paragraph 32.

¹⁸⁰ See the cases “*National Grid Indus*” C-371/10 paragraph 86, “*Commission v. the Netherlands*” 301/11 paragraph 16, “*Commission v. Portugal*” C-38/10 paragraph 32.

¹⁸¹ Christiana Hji Panayi ”*European Union Corporate Tax Law*” p. 3.

Article 115 states that *“the Council shall, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, issue directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the establishment of the internal market.”* This article gives the Council, on certain conditions, the right to issue legislation that directly affects formation of the internal market.

Article 352 (1) states that *“if action by the Union should prove necessary, within the framework of the policies defined in the Treaties, to attain one of the objectives set out in the Treaties, and the Treaties have not provided the necessary powers, the Council, acting unanimously on a proposal from the Commission and after obtaining the consent of the European Parliament, shall adopt the appropriate measures...”* National Parliaments must be informed about proposals based on this article.¹⁸² Article 352 is a flexibility clause, and is only to be used when actions from the Union are proved to be necessary in order to achieve its objectives.

Article 116 states that *“where the Commission finds that a difference between the provisions laid down by law, regulation or administrative action in Member States is distorting the conditions of competition in the internal market and the resultant distortion needs to be eliminated, it shall consult the Member States concerned.”* If the distortion is not eliminated the European Parliament and the Council can issue necessary directives in accordance with the ordinary legislative procedure. Article 116 addresses existing distortion affecting the conditions of competition in the internal market, and authorises the Union legislators to adopt necessary legislation to eliminate the market distortion. This legislative base does not require unanimity and the legislative process is based on the ordinary legislative procedure.

Article 117 (1) states *“where it is a reason to fear that the adoption or amendment of a provision laid down by law, regulation or administrative action may cause distortion within the meaning of Article 116, a Member State desiring to proceed therewith shall consult the Commission. After consulting the Member States, the Commission shall recommend to the States concerned such measures as may be appropriate to avoid the distortion in question.”* If the State in question does not comply with the recommendation addressed to it by the Commission, shall other Member States not be required to amend their own provisions in order to eliminate such distortion. Article 117 intends at preventing the Member States from introducing new market distortions. Article 117 does, contrary to article 116, not authorise the Union to adopt legislation in order to prevent new distortions but only permits the

¹⁸² Art 352 TFEU (2).

Commission to issue recommendations. Recommendations have now binding force.¹⁸³ Article 117 has the objective of a standstill clause, but the Member States are still obligated to cooperate in order to ensure the objectives of the Union, confer art 4 (3) TFEU, which is an important principle, especially in tax matters.

These legislative bases gives the EU institutions power to intervene in order to protect the functioning of the Internal Market. Still, none of the articles have been used yet in order to regulate the Member States national rules for charging exit tax on companies, although the ECJ have found that such regimes are likely to infringe Internal Market principles. A central issue here is the fiscal veto, which is the power of each of the Member States to reject to a harmonising measure in direct tax law.¹⁸⁴ The general rule confer the Treaties is that all Member States must agree unanimously to tax proposals, before they can be adopted.¹⁸⁵ The Member States safeguard their veto right carefully, and it has survived several Treaty amendments and attempts to move to qualified majority voting.¹⁸⁶ As an example, it was proposed to move from unanimity to qualified majority voting for proposals in a limited number of tax fields, essentially proposals necessary for the proper operation of the internal market, in the draft of the Constitutional Treaty.¹⁸⁷ All Member States did not ratify the Constitutional Treaty, and the Treaty of Lisbon was later drafted to replace it. The Commissions proposal was not in the new treaty. The Member States are evidently unwilling to give up parts of their sovereignty in direct taxation matters.

Only article 115 and article 352 (1) are dependent on unanimity. Article 116 on the other hand gives the European Parliament and the Council, on certain conditions, power to issue legislation based on ordinary legislative procedure in order to cope with distortions in competition because of national legislation. The article in itself appears to be a suitable legal base for the EU legislator to intervene in national exit taxation regimes that infringes EU competition law, but it has not happened yet. Article 116 is aggressive, as it gives the EU legislators power to issue legislation in order to eliminate distortion on competition based on regular legislative procedure, if the Member State in question do not remove the distortion itself. In addition are interventions from the EU institutions in matters that are supposed to be sovereign to the Member States extremely politically sensitive. This may be the reason for why article 115 and article 352 are the only ones that have been used for legislation in direct tax matters, as they are based on unanimity and that legislation based on these articles

¹⁸³ TFEU art. 288 in fine.

¹⁸⁴ Christiana Hji Panayi "European Union Corporate Tax Law" p. 4.

¹⁸⁵ Taxation and Qualified Majority Voting, The Intergovernmental Conference of 2003-2004 at http://ec.europa.eu/taxation_customs/taxation/gen_info/conference/index_en.htm (23.04.14)

¹⁸⁶ Christiana Hji Panayi "European Union Corporate Tax Law" p. 4.

¹⁸⁷ See amendments to the draft constitution proposed by the Commission, Article III-63 (corporate taxation) at http://ec.europa.eu/taxation_customs/resources/documents/amendments_iii_63_en.pdf (23.04.14)

consequently will have broader legitimacy in regard of both Member States and EU citizens. Yet, it does not explain why the EU legislators have refrained from using article 115 and article 352 to issue legislation in order to harmonise national exit taxation regimes.

4.2 The legality of applying exit taxes on companies within the EEA

4.2.1 The legal framework for charge of exit taxes on companies within the EEA

Exit taxes as such are not specifically addressed in the EEA-Agreement, but the EEA States exit taxation regimes have nonetheless been influenced by the agreement. The EEA States are bound to take any appropriate measure, whether general or particular, to ensure fulfilment of the obligations arising out of the agreement, and they shall abstain from any measure that could jeopardize the attainment of the objectives of the agreement.¹⁸⁸ In other words, the EEA States are obliged to safeguard the objectives set out by the agreement and to take any necessary actions in order to make them effective. The concept of homogeneity is of great importance, and the objective is that the parties are to have an as uniform interpretation as possible of the provisions of the agreement and those provisions of EU law which are substantially reproduced in the agreement.

As we have seen from the case law of the ECJ, a charge of exit taxes on companies likely to create restrictions to freedoms protected by the EU Treaties and the EEA-Agreement, in particular the freedom of establishment and the free movement of capital. The free movement of persons, services and capital, hereunder the freedom of establishment, are identically set out in the EU Treaties and the EEA-Agreement, and the provisions shall be interpreted in the same way.¹⁸⁹ In other words, a measure that is found to be a restriction to the EEA-Agreement must also be seen as a restriction under the EU Treaties. The case law of the EU concerning restrictions to the free movement within the Union can though not be implemented in its entirety to the freedoms guaranteed by the EEA-Agreement, as the EEA-Agreement covers a different legal context.¹⁹⁰ Nevertheless, the ECJ has had a big impact on the EEA States exit taxation regimes and the case law mentioned above are relevant also when determining the legality of charging exit taxes on companies within the EEA. Although it is necessary to keep in mind that the EU and the EEA are two different legal contexts.

An important difference in relation to the legality of exit taxes within the EU and the EEA is that the EEA States, which are not EU Member States, are not subject to the Mutual Assistance Directive for the Recovery of Taxes or the Mutual Assistance Directive for Exchange of Information. Both

¹⁸⁸ The EEA-Agreement article 3.

¹⁸⁹ Ibid. article 6.

¹⁹⁰ Case C-261/11 “*Europa-Kommissionen mod Kongeriget Danmark*” 2013, paragraph 44.

directives have been referred to by the ECJ in several cases about exit taxes, in connection to the necessity of a restrictive measure as part of the proportionality test used to determine whether a restriction can be justified or not. The effect of this will I come back to.

4.2.2. *The case law of the EFTA Court*

Firstly will I remark that the EFTA Court has jurisdiction of over cases regarding Iceland, Liechtenstein and Norway's compliance with the EEA-Agreement, and that the EFTA Court is bound to take regard to jurisprudence from the ECJ.

*Arcade Drilling AS v. Norway*¹⁹¹ is the only case the EFTA Court has had concerning exit taxes. The facts of the case were that Arcade Drilling AS (Arcade), a company incorporated and registered as a Norwegian limited liability company was deemed to have moved its head office i.e. real seat, and its tax residency to the UK in 2001. The Norwegian tax authorities claimed that Arcade, as a consequence of the relocation of the company's head office outside of Norway, was under an obligation to liquidate and pay off a liquidation tax.¹⁹² Arcade had however de facto not been liquidated and the obligation to liquidate according to Norwegian company legislation was disputed. Arcade filed for a legal annulment action and claimed that the decision at issue infringed EEA law. The case was brought before the Oslo municipal court, which requested an advisory opinion from the EFTA Court. As for the fact that Arcade not yet had been liquidated, was the questions referred formulated on the assumption that a liquidation obligation existed under Norwegian law.

The first question referred was whether it constituted a restriction pursuant to the articles 31 and 34 of the EEA-Agreement to impose liquidation tax on a company, if national company law entails an obligation to liquidate the company because the company has relocated its de facto head office from Norway to another EEA State. Initially the EFTA Court remarked that in the absence of clear and precise provisions on the obligation to liquidate, and of any decision by the competent authorities or courts putting the liquidation into effect, was Arcade still a company established under the legislation of an EEA State in accordance with article 34 and was thus able to rely on the freedom of establishment confer article 31.¹⁹³

Then the EFTA Court continued to consider breach of the articles 31 and 34. The EFTA Court stated first that freedom of establishment under article 31 entails a right for companies formed in accordance with the law of an EEA State having its registered office, central administration or principal place of

¹⁹¹ "*Arcade Drilling AS v Staten v/Skatt vest*" case E-15/11

¹⁹² *Ibid.*, paragraph 28-29.

¹⁹³ *Ibid.*, paragraph 45.

business within the EEA, to pursue their activities in another EEA State through a branch established there.¹⁹⁴ Then, article 31 is, despite of its wording, not only intended to secure the benefit of national treatment in a host State, but also prohibits the home State from hindering its own nationals or companies incorporated under its legislation, to establish in another EEA State.¹⁹⁵ Further does it follow from the prohibition of discrimination in article 31 that comparable situations must not be treated differently, and that different situations must not be treated in the same way unless such treatment is objectively justified.¹⁹⁶

The national legal basis used to impose the liquidation tax was the general anti-avoidance principles. The Norwegian State argued that the principles applied in the same manner to the taxation of all companies that was deemed to be in avoidance of taxation consequent to the winding up and liquidation of companies, while Arcade, on the other hand, argued that the principles applied only in cross-border situations. The EFTA Court held that it was up to the national court to determine the scope of the principles, but if it found that the principles only applied on cross-border situations would they constitute a restriction to the articles 31 and 34.¹⁹⁷ The EFTA Courts reasoned that if the principles only applied to companies transferring its place of management to another EEA State, then would this constitute a restriction because of the different treatment, and such difference in treatment could not be explained by an objective difference in situation.

The second question referred to the EFTA Court was what criteria would be decisive when determining whether the national regulation in question pursued an overriding public interest and whether it was suitable and necessary for the attainment of such an interest.¹⁹⁸ The EFTA Court stated first that a restriction of freedom of establishment only is permissible if it is justified by overriding reasons in public interest and that the restriction is appropriate to ensuring the attainment of the objective, in addition to that it does not go beyond what is necessary.¹⁹⁹ Furthermore, in the absence of any unifying or harmonising measures, had the EEA States kept the power to define, by treaty or unilaterally, the criteria for allocating their powers of taxation.²⁰⁰ Accordingly could the EEA States take appropriate measures with view to preserving the exercise of their tax jurisdiction when a company ceases to exist under that jurisdiction as a result of national company law, thus was preserving the allocation of taxation powers between the EEA State a legitimate objective.²⁰¹ The EFTA Court also noted that justification on these grounds could be accepted, in particular of the

¹⁹⁴ Ibid., paragraph 58.

¹⁹⁵ Ibid., paragraph 59.

¹⁹⁶ Ibid., paragraph 60.

¹⁹⁷ Ibid., paragraph 61-66.

¹⁹⁸ Ibid., paragraph 67.

¹⁹⁹ Ibid., paragraph 82-83.

²⁰⁰ Ibid., paragraph 84.

²⁰¹ Ibid., paragraph 85.

system in question was designed to prevent conduct capable of jeopardising the right of an EEA State to exercise its tax jurisdiction in relation to activities carried out in its territory.²⁰²

The Norwegian state had claimed that prevention of tax avoidance also could justify the legislation. To this the EFTA Court noted that it could be a justifying objective, but only if the legislation was especially designed for this matter.²⁰³ Furthermore stated the EFTA Court that the EEA State was entitled to tax a company's gains, and assess its tax position at the time when the taxpaying entity was dissolved and the gains were distributed to its owners, based on the principle of fiscal territoriality linked to a temporal component. In this case could the taxation be justified namely because of the taxpayer's existence as a separate legal entity for tax purposes within national territory during the period in which the gains arose and other tax positions become effective.²⁰⁴

The EFTA Court found therefore that if companies were permitted to relocate their head office to another EEA State, in violation to national company law, without having any consequences for taxation, would this undermine the balanced allocation of the power to impose taxes between the EEA States.²⁰⁵ The Norwegian legislation was thus found to enable the Norwegian State to exercise its tax jurisdiction in relation to activities carried out in its territory, and to prevent practices whereby companies sought to evade taxation obligations.²⁰⁶ Consequently held the EFTA Court that a national measure, such as the Norwegian legislation at issue, pursued legitimate objectives that were compatible with the EEA-Agreement and constituted overriding reasons in the public interest, and that it was appropriate for ensuring the attainment of those objectives.²⁰⁷

Then the EFTA Court assessed whether the Norwegian legislation went beyond what was necessary to attain the objectives of maintain the balanced allocation of taxation powers between the EEA States, and to prevent tax evasion. Under the Norwegian provision were both the establishment and the recovery of the tax at the time when the company was winding up or liquidated. The EFTA Court found that the definitive establishment of the tax amount at this time might be proportionate,²⁰⁸ but it was not proportionate to require immediate payment of the tax. The EFTA Court cited the *National Grid Indus* case, and held that national tax authorities has to distinguish between definite establishment of the tax debt, and the time of recovery.²⁰⁹ Immediate recovery of the tax could give rise to a significant disadvantage for the company in the terms of cash flow, and this problem might be

²⁰² Ibid., paragraph 86.

²⁰³ Ibid., paragraph 87.

²⁰⁴ Ibid., paragraph 90.

²⁰⁵ Ibid., paragraph 91.

²⁰⁶ Ibid., paragraph 92.

²⁰⁷ Ibid., paragraph 93.

²⁰⁸ Ibid., paragraph 97-98.

²⁰⁹ Ibid., paragraph 99.

avoided by deferring the payment of the tax until the capital gains were actually realised.²¹⁰ However, the national authorities were found to be entitled to require security for the payment, provided that there is a genuine and proven risk of non-recovery.²¹¹ Furthermore noted the EFTA Court that important factors were the nature and extent of the company's tax positions, and the sources for information available to the national authorities regarding these tax positions, inter alia, through cooperation with the other EEA States. If it was found that the assets would be easy to trace, could the migrating company be offered the choice between immediate- or deferred payment. The latter could however constitute an administrative burden for the company in connection with tracing the relocated assets.²¹² The EFTA Court also noted that account should be taken to the risk of non-recovery of the tax, which increases with the passage of time, by the EEA State in question by e.g. require provision of a bank guarantee.²¹³

The EFTA Court concluded that definitive establishment of the amount of the tax consequent to an obligation to wind up and liquidate a company could be justified by the objectives of maintain the balanced allocation of powers of taxation between the EEA States and preventing tax avoidance. A national measure that requires immediate recovery of tax on unrealised capital gains at the time of the tax assessment was precluded by article 31 of the EEA-Agreement.

This decision is not surprising, as the EFTA Court actively based its decision on the principles already set laid down by the ECJ, mainly in the *National Grid Indus* case. On the other hand, the EFTA Court did also provide some clarifications. First, that a company of a EEA State that uses the real seat system is protected by the freedom of establishment, even though it is deemed to be liquidated according to company law as long as the liquidation not formally has been put into effect.²¹⁴ Furthermore, in regard of the EEA States ability to ask for security when granting deferral, found the EFTA Court that it can be unnecessary to ask for security in relation to liquidation of a company, if the risk of non-recovery is covered by the personal liability of shareholders for outstanding tax debts of the company.²¹⁵

4.3. Can exit taxes be charged to the same extent within the EU and the EEA?

As mentioned above is it likely that exit taxes levied on companies are allowed to the same extent within the EU and the EEA, and the conclusion presented at p. 34 in relation to the discussion about

²¹⁰ Ibid., paragraph 100.

²¹¹ Ibid., paragraph 101.

²¹² Ibid., paragraph 102-103.

²¹³ Ibid., paragraph 105.

²¹⁴ Ibid., paragraph 45-46.

²¹⁵ Ibid., paragraph 105.

the ECJ's case law, could be applicable also in regard of exit taxes imposed on companies within the EEA. The fact that the EU and the EEA are two separate legal contexts has that effect that one cannot just accept that a restrictive measure under EU law also is restrictive confer the EEA-Agreement. When assessing the case law mentioned above is it apparent that the examination of whether an exit tax regime constitutes a restriction to a freedom protected by the EU Treaties and/or the EEA-Agreement, is the same. However the differences become evident under the assessment of whether an exit tax regime, which is found to be restrictive, can be justified and is proportionate. The question that must be asked is whether the two situations should be treated differently.

The *Commission v. Denmark*²¹⁶ case is suitable to demonstrate the difference between the contexts of the EU Treaties and the EEA Agreement. In this case considered the ECJ first whether the Danish legislation at issue violated the freedom of establishment confer article 49 TFEU, and then if it violated the freedom of establishment confer article 31 of the EEA-Agreement. The ECJ found that the Danish legislation violated both provisions. Under the assessment of whether the Danish legislation constituted a restriction to article 31 of the EEA-Agreement asked the ECJ whether such a restriction, in the legal context of the EEA-Agreement, could be justified by overriding reasons in the public interest to ensure effective recovery of the tax and further if the restriction would be appropriate to ensure the attainment of the objective in question and that it did not go beyond what was necessary to attain the objective.²¹⁷ It had been argued that immediate recovery of the tax could be justified in order to ensure effective recovery of the tax, because of the lack of sufficient legislation to ensure mutual exchange and recovery of the tax debt between Denmark and Iceland, Liechtenstein and Norway. The ECJ found essentially that if it were no need of assistance from the EEA State, which was not a EU Member, in order to recover the tax then would it be disproportionate to require immediate recovery of the tax debt. In the *Commission v. Denmark* case would the transferred assets continue to be subject to Danish tax jurisdiction after the transfer, and thus could the Danish legislation not be justified.

Neither the ECJ nor the EFTA Court has referred to situations where the assistance from an EEA State, which is not a EU Member State, has been needed. It is possible however, because of the absence of a legal framework for mutual assistance in the area of taxation, that immediate recovery could be accepted within the EEA between non-EU Member State or EU Member States and Iceland, Liechtenstein and Norway. The purpose to ensure effective tax recovery is a legitimate objective, and if the home state would need assistance from the host state in order to attain this objective, and such assistance was not available then could immediate recovery be considered both proportionate and necessary. Under the consideration of whether the restriction could be justified and if it is necessary would one of course have to look for alternative options that could be less burdensome for the

²¹⁶ The "*Commission v. Denmark*" case 261/11 paragraphs 41-48.

²¹⁷ *Ibid.*, paragraph 46.

taxpayer. The protection of the taxpayer is strong and as a general rule should the taxpayer have the option to choose between immediate and deferred recovery of the tax debt, and as long as a state can be entitled to ask for security or phased deferral, is it not likely that a restrictive measure would be prohibited in EU-context and not in EEA-context.

Conclusion

In general, there are no difference between the legality of exit taxes within the EU and the EEA. It is however important to see the EU and the EEA as two different legal contexts, and one must ask if it is reason to treat a restrictive measure differently within the two legal contexts.

5 Analyse of how states convey with EU- and/or EEA exit tax rules for companies

5.1 Charge of exit taxes on companies within the United Kingdom

5.1.1 Introduction

Exit taxes have been a part of the UK taxation regime for some time, at least since the Taxation of Chargeable Gains Act (TCGA) was adopted in 1992, and it applies to both individual and corporate taxpayers. The UK amended its exit tax provisions in 2013 with the Finance Act as a respond to the ECJ's judgement in the *National Grid Indus* case and on request from the Commission.²¹⁸ The objectives of the UK exit tax rules are based log on, among others, to prevent tax avoidance and counter act tax avoidance schemes, in addition to the principle of fiscal territoriality.

The basic principle in the UK is that capital gains tax only applies when the latent capital gain of an asset or liability is realised²¹⁹, i.e. subject to sale or in other ways disposed off. Yet there are exceptions, and a company that ceases to be tax resident in the UK, or transfers an asset or liability outside of the UK tax jurisdiction are deemed to have disposed and reacquired the asset or liability.²²⁰ In other words, the UK considers the removal of taxable income from the UK tax jurisdiction as a realisation of the company's assets, which consequently gives rise to a chargeable gain.

Further on, I will begin with giving an overview over the legal basis for charge of exit tax on migrating companies, and then continue with the legal basis for charge of exit tax on assets and

²¹⁸ The Commission requested the UK in February 2011 to amend two anti-abuse tax regimes, and in March 2012, in the form of a reasoned opinion, to change its exit tax provisions on companies in order to make them applicable with EU law.

²¹⁹ Taxation of Chargeable Gains Act (CGTA) 1992, § 1 cf. §§ 2, 8 and 15.

²²⁰ TCGA §§ 185 and 186.

liabilities that are transferred out of the UK's tax jurisdiction before I give some remarks to the relationship to EU-law.

5.1.2 National provisions

5.1.2.1 Charge of exit taxes on migrating companies

A company, which ceases to be resident in the UK for tax purposes, is charged a tax immediately before it becomes a non-resident under national law or a tax treaty.²²¹ It is possible that conflicts arise when considering who is a resident in the UK for tax purposes, as the national legislation is based upon the incorporation theory²²² and most treaties rely on the real seat theory. Such conflicts will in most cases be solved by a tiebreaker rule and as a consequence can a company, which is considered a UK resident under national law, become a non-resident for tax purposes.²²³ For example a company, which is incorporated in the UK, can under national law transfer its central management and control out of the UK and still be a taxpayer to the UK. A company that is incorporated outside the UK on the other hand, ceases to be a resident if it transfers its central management and control outside the UK. However, a company incorporated in the UK, which transfers its central management and control outside of the UK, can become a non-resident of the UK because of a tax treaty.

The exit of a company triggers immediate taxation of a company's unrealised gains, and the company is deemed to have disposed of all its assets at their market value immediately before the exit and to have reacquired them at that value at the time of the exit.²²⁴ Certain assets are though excluded from this charge, as long as the migrating company continues to trade within the UK through a PE. Assets that can be excluded are those that are used or held for the purpose of the trade or a PE in the UK.²²⁵ The reason for this is such assets actually remain within the scope of UK tax jurisdiction.²²⁶ Moreover is it possible to defer payment of tax on foreign assets of a foreign trade where a subsidiary company migrates but the principal company remains a resident of the UK.²²⁷

Furthermore is it possible to defer the payment of the exit charge if the migrating company enters into a payment plan with the HM's Revenue and Customs. The tax amount however, will be established at the time of the migration. For such deferral to be granted is it required that the migrating company a)

²²¹ TCGA section 185.

²²² Finance Act (FA) 1994 section 249.

²²³ The majority of tax treaties contain tiebreaker rules, but there are also those who dont e.g. the tax treaty between the USA and the UK.

²²⁴ TCGA section 185.

²²⁵ TCGA section 185 (4).

²²⁶ Corporation Tax Act (CTA) 2009 section 5 (2) and TCGA section 10B.

²²⁷ TCGA section 187.

ceases to be resident in the UK and b) becomes a resident in another EEA state and c) is liable to pay an exit charge in respect of the migration accounting period.²²⁸ In regard of condition b) is it required that the company carries on a business in that EEA state²²⁹, and c) that the company is not treated as resident in a territory outside the EEA for the purposes of any double taxation arrangements.²³⁰ In order to enter into such a payment plan must the company and the HM's Revenue Customs agree on how the payment shall be done, and hereunder can they choose a payment in accordance with the standard instalment method, the realisation method or a combination of the two methods.²³¹ The tax deferred will also be subject to interest, and security if it is considered necessary. As for securities is there an individual assessment of the risk of non-recovery in each case. In addition, if the taxpayer fails to make payments in accordance with the plan can the company be penalised.

The standard instalment method involves that the payment is to be done in six instalments of equal amounts over six years, starting with the first payment on the first day after the period of 9 months beginning immediately after the migration.²³² The realisation method²³³ on the other hand, involves that the payment of tax, on other assets than intangibles, is deferred until the asset or liability is wholly or partly disposed. Such deferral has an upper limit of 10 years. For fixed intangible assets and financial assets however, is the payment required in annual instalments over ten years or over the useful economic life of the asset or liability. The useful economic life of an asset or liability will be determined at the time of the exit. Moreover are both options are supplemented by a regular reporting requirement.

Companies that become non-residents of the UK and that maintain to carry on trade in the UK through a PE there, can also opt to defer the payment of exit charges, even if the company migrates to a third state.²³⁴

Before a company migrates is it required to notify the HM Revenue & Customs Board of the UK about its intentions to migrate and provide a statement of its tax liabilities, and make arrangements for securing the payment of the tax in due course, and obtain the Board's approval of the arrangements.²³⁵

²²⁸ Finance Act (FA) 2013 Schedule 3ZB, Part 1, section 1.

²²⁹ The basic test is whether the company carries on genuine economic business activities in the other state, or if it is just "a wholly artificial arrangement," see the "*Cadbury Schweppes plc & Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*" Case C-196/04 (2006).

²³⁰ FA Schedule 3ZB, Part 1, section 1.

²³¹ Ibid. Part 3, section 8.

²³² Ibid. Part 3, section 13.

²³³ Ibid. Part 3, section 14 and 15.

²³⁴ Ibid. Part 2 section 4.

²³⁵ Finance Act 1988 section 130-132.

5.1.2.2 Exit taxes charged on transferred assets and liabilities

As a starting point, under the UK law will the transfer of an asset or liability from a resident of the UK for tax purposes, to a recipient abroad, trigger charge of an “income charge” on the transferor. The tax is charged only where there has been a transfer of assets and, as a result of the transfer, income becomes payable to a person abroad, but the transferor is still able to enjoy the income of the person abroad, or receives, or is entitled to receive a capital sum, or another UK resident receives a benefit from the arrangements.²³⁶ The provisions apply to individual taxpayers, who are UK residents (natural or legal persons). The objective of the provisions is to prevent tax avoidance by individuals, and the rules seek to counteract tax-avoidance schemes by individuals who use companies, trusts or other entities, which are residents of other countries, to reduce UK tax liability.

Certain conditions must be met in order to make the tax applicable, and basically are there four conditions: 1) there must be a transfer of assets by an individual, 2) as a result of the transfer (alone or in conjunction with associated operations) income becomes payable to a person abroad, 3) the individual has power to enjoy that income in some way as a result of a transfer of assets alone or together with associated operations, or receive/be entitled to receive a capital sum in any way connected with any relevant transactions, and 4) the recipient of the benefit must be a resident in the UK in the year of the charge.²³⁷ When these requirements are fulfilled, will the individual (UK taxpayer) be taxed on income accruing from the transferred asset or liability, even though the capital gain actually is accruing outside of the UK.

Moreover, if an asset or liability is transferred abroad can a “Benefits Charge” be charged on a resident of the UK, other than the transferor, if that resident receives benefits from the transferred asset or liability.²³⁸ Basically are there three conditions that must be met; 1) there must be a relevant transfer, 2) an individual who is a UK resident receives a benefit, which is not otherwise chargeable to Income Tax, out of assets which are available for the purpose as a result of the transfer or one or more associated operations, and 3) the recipient of the benefit must be resident in the UK in the year of the charge.²³⁹ The difference between the benefits charge and the income charge discussed above is that the transferor and the beneficiary are different persons, yet both taxes intend to charge the beneficiary. The benefits charge typically applies to beneficiaries of non-resident trusts who receive benefits or capital payments from trustees.

²³⁶ Income Tax Act (ITA) 2007 Chapter 2 Transfer of Assets Abroad, section 721,727 and 231.

²³⁷ Ibid., 732.

²³⁸ ITA section 731.

²³⁹ Ibid., section 732.

Special rules apply if the transferor is a resident, but not domiciled in the UK. In such cases will the transferor only be taxed in respect of UK source income and foreign income if it is remitted²⁴⁰ to the UK.²⁴¹

Nevertheless, there are exemptions from the above mentioned tax-avoidance regimes, but here I will only discuss the exemption relevant for transfers of assets and liabilities to another EEA state. An individual residing in the UK who transfers assets or liabilities to another EEA state is automatically exempted from this charge if two conditions are fulfilled, a) the transfer is within the EEA and b) that it is a genuine transaction. If a transaction is “genuine” or not depends on whether it has been made in accordance with the arm’s length principle, and with regard to any arrangements under which it is affected and any other relevant circumstances.²⁴² In EU terms is the test basically whether the transaction only is a purely artificial arrangement or not. The exemption is intended to cover genuine commercial business activities that take place abroad. However, transactions that do not involve business activities but still are regarded as genuine transactions will also be covered by the exemption. Consequently will only non-genuine transactions be liable to tax.

5.1.3 Relationship to EU-law

The basic rule under domestic legislation is that a migrating company is charged an exit tax on hidden reserves. However, there are exemptions, and under the current legalisation can a company, which migrates to another EEA state, opt between immediate and deferred payment of the tax. Yet, the tax debt is established at the time of the transfer, but this is in accordance with EU-law. When a company choose to defer the payment must the payment be done in accord with the standard instalment method, the realisation method or a mix between the two. If the realisation method is chosen, then must the payment be done either when the latent capital gain is realised or when the asset’s useful economic life has ended, although there is an upper limit of 10 years. It can be questioned whether this 10-year time limit is proportionate. The starting point confer case law from the ECJ, is that the taxpayer shall have the possibility to opt for deferral of the payment until the time when the capital gain is realised, i.e. the asset or liability is disposed. Yet, in the case “*DMC Beteiligungsgesellschaft mbH v. Finanzamt Hamburg-Mitte*”²⁴³ accepted the ECJ that a 5-year deferral could be proportionate because of an assets nature; some capital gains are realised over time as they are depreciated. The assets at issue in the case were interest payments, i.e. intangible assets. The realisation method under the UK

²⁴⁰ In general, is a remittance for this purpose a transfer of money; the import of goods purchased abroad is not a remittance until the goods are sold, see “*remittance basis*” in Oxford Dictionary of Law, edited by Jonathan Law and Elizabeth A. Martin, 7th edition, Oxford University Press.

²⁴¹ ITA section 735.

²⁴² Finance Act 2013 Schedule 10, part 2, section 742A (6).

²⁴³ case C-164/12 “*DMC Beteiligungsgesellschaft mbH v. Finanzamt Hamburg-Mitte*”

legislation does however not apply to intangible assets, thus is it possible that the provision is disproportionate. The rule is still that it shall be possible to defer the payment of an exit tax until the capital gains are realised, as long as the company finds that deferral will not create an excessive administrative burden. Under the UK legislation as it is now, can the payment of a tax debt on an asset, which may exist in more than 10 years, not be deferred until realisation but only 10 years.

The UK legislation provides further that payment of tax on intangible- and financial assets can be deferred and paid in instalments over ten years. This however, must be proportionate, as the ECJ accepted a 5-year deferral of such assets in the “*DMC Beteiligungsgesellschaft mbH v. Finanzamt Hamburg-Mitte*” case.²⁴⁴

Under the UK law becomes transferred assets or liabilities subject to an exit charge if the transferor or a third person, who are residents of the UK for tax purposes, receives benefits from the transferred asset or liability. Nevertheless, there is an exemption from these rules if the asset or liability is transferred to another EEA state, then will the transferor or other beneficiaries not be taxed on the income. However, if the transaction is not genuine, then will the transferor or other beneficiaries still be liable for taxation. The purpose of these provisions is to prevent tax avoidance, and they are particularly designed to counteract tax avoidance schemes. It is clear that rules, which charge tax on cross-border transactions just because they are made cross-border, are restrictive to treaty freedoms, but the objective to prevent tax avoidance can still be legitimate. Additionally, as the restrictive provisions are especially designed to prevent tax avoidance and they only apply on non-genuine transactions, can they be justified. Overall, the UK provisions regarding taxation on transfers of assets and liabilities are in accordance with EU law.

5.2 Charge of exit taxes on companies in Norway

5.2.1 Introduction

²⁴⁴ Ibid.

Exit taxes are a rather new tax mechanism in Norway, although some provisions were presented as a part of a tax reform in 1991.²⁴⁵ In recent years have exit taxes been introduced in three waves: as from 1 January 2007 for capital gains on shares owned by individuals, as from 1 January 2008 on SEs and as from 1 January 2009 on joint-stock companies in general and their shareholders, as well as on assets and liabilities.²⁴⁶ The Norwegian exit tax rules are mainly based on the objective to counteract tax avoidance schemes, but also the principle of fiscal territoriality.

Under Norwegian tax law is the general rule that capital gains and losses are neither deemed gained nor deducted until the asset or liability is realised.²⁴⁷ Still there are exceptions, and unrealised capital gains are taxed when the taxpayer, individual or company, ceases to be liable to tax in Norway or the asset or liability is transferred out of the Norwegian tax jurisdiction. In other words, the removal of taxable income from the Norwegian tax jurisdiction is seen as a realisation of the capital gain of the asset or liability.

Further on, I will begin with giving an overview over the legal basis for charge of exit tax on migrating companies, and then continue with the legal basis for charge of exit tax on assets and liabilities that are transferred out of the Norwegian tax jurisdiction before I give some remarks to the relationship to the EEA-Agreement.

5.2.2 National provisions

5.2.2.1 Exit taxes charged on migrating companies

Exit tax on companies are triggered the day before the company ceases to be resident in Norway for tax purposes according to Norwegian tax law²⁴⁸ or a tax treaty.²⁴⁹ There is no big difference between resident for tax purposes according to Norwegian tax law or a tax treaty, as they both are based on the real seat theory. However, it could be a difference in fact as the domestic Norwegian law relies more heavily on the place where the board of the company makes its decisions than treaties do.²⁵⁰

Consequently it can happen that a company established in another state, but which has its effective management in Norway, are regarded as a taxpayer in Norway and thus becomes subject to an exit tax if it transfers its effective management to another state.

²⁴⁵ See Professor Frederik Zimmer, article "*Exit Taxes in Norway*" Word Tax Journal, October 2009 p. 115.

²⁴⁶ Ibid.

²⁴⁷ Skatteloven (the General Taxes Act, GTA) §§ 5-1, 5-30 and 6-2.

²⁴⁸ GTA § 2-2.

²⁴⁹ GTA § 10-71 (1).

²⁵⁰ Professor Frederik Zimmer, article "*Exit Taxes in Norway*" Word Tax Journal, October 2009 p. 131.

The exit of a company triggers immediate taxation of unrealised capital gains on the company's assets and liabilities, but also the right to deduct losses, i.e. the exit is in itself regarded as a realisation of a company's hidden reserves. The capital gain or loss corresponds to the difference between the asset or liability's market value and its tax value at the time of the transfer.

However, the general exit tax duty only apply when the company, which becomes a non-resident, establish itself in a state outside of the EEA, or migrates to a low tax country within the EEA and the company is not actually established in that host Member State or carries on genuine economic activities there.²⁵¹ Which countries are considered low tax countries follows by law²⁵², and in general are all countries with a tax level below two thirds of the tax level that is applicable to similar companies in Norway, considered as low tax countries. From 2014 is the Norwegian company tax 27%, and none of the EEA States are considered as low tax countries.²⁵³

Nevertheless, a company can migrate to another EEA state without triggering immediate exit taxation. Such tax-free migration is conditioned upon that the company continues to be subject to tax in Norway through a PE, and that the company's assets and liabilities are kept effectively connected to the PE following the transfer. In this regard are the exit taxation rules for assets and liabilities important because if the assets and liabilities, which are assigned to the Norwegian PE, are transferred out of the Norwegian tax jurisdiction, will these rules be applicable to those assets and liabilities.

5.2.2.2 Exit taxes charged on transferred assets and liabilities

Taxation of assets and liabilities, which are transferred out of the Norwegian tax jurisdiction, applies equally to assets and liabilities whether held by individuals, companies or other legal persons. In principle do the rules apply to all assets, whether tangible, financial or intangible, including real estate although in practice will the exit tax provisions not apply to such assets. However, tangible assets are only included if a depreciation allowance is granted, and movable tangible assets are only included when they, by the time of the exit, are connected to the business of the shareholder that rules on business income would apply i.e. private movable assets does not fall within the scope of this legislation.²⁵⁴ Ordinary debt claims outside the business of the creditor are also excluded, along with

²⁵¹ GTA § 10-71 (2) cf. § 10-64 litra b (the requirement of genuine economic activities)

²⁵² GTA § 10-63 and FSSD § 10-63.

²⁵³ European microstates as for example Andorra, Monaco and Montenegro are listed as low tax countries, but neither of them are part of the EEA.

²⁵⁴ Professor Frederik Zimmer, article "Exit Taxes in Norway" Word Tax Journal, October 2009 p. 139.

financial assets owned by individuals.²⁵⁵ Financial assets held by individuals are however regulated by another rule. The statute rule distinguish the relevant assets into five categories: I) fixed tangible business assets, II) financial assets, III) liabilities, IV) inventories and V) intangible assets.²⁵⁶

The exit tax is imposed when the asset or liability is transferred out of the Norwegian tax jurisdiction, as if the asset or liability was sold on the day before such transfer took place. The triggering factor is not based on a geographical concept, but rather the legal concept of the Norwegian tax jurisdiction. Such transfer is deemed to have taken place when Norway no longer has sufficient legal basis, according to domestic law or tax treaties, to tax the asset or liability. The taxable capital gain corresponds to the difference between the asset/liability's market value²⁵⁷ and the tax base at the time of the transfer. Correspondingly can calculated loss be tax deductible.

The statute divide the tax-triggering event into three broad groups of cases: I) when a taxpayer becomes a non-resident of the Norwegian tax jurisdiction, hereunder is it distinguished between a) transfer of the assets/liabilities themselves and b) the taxpayer ceases to be a tax resident of Norway, II) when a non-resident taxpayer with PE in Norway transfers assets or liabilities abroad and III) if the Norwegian control of a CFC-company²⁵⁸ comes to an end, and the assets/liabilities thus no longer are under the Norwegian tax jurisdiction.

If the taxpayer is a Norwegian resident or a resident of another EEA state can the payment of tax charged on fixed tangible business assets, financial assets or liabilities be deferred. Conversely if there is a genuine risk of non-recovery, can it be required security for the deferred tax and incurred interest. Exit taxes imposed on intangible assets and inventories cannot be deferred and must be paid immediately upon the transfer. The legislator's reason for the exemption of intangible assets and inventories in regard of the possibility for deferral is split; intangible assets are often kept by the taxpayer and may never be sold and the value of such assets will therefore often vanish, whilst inventories on the contrary normally are sold within a short period of time and that the latent capital gains are usually low.

When the payment is deferred the exit tax liability will terminate when the asset or liability in question is sold or in other ways realised. If an asset or liability is brought back to the Norwegian tax jurisdiction will this not have that consequence that the tax is waived. If the asset or liability is sold at

²⁵⁵ Ibid.

²⁵⁶ GTA § 9-14.

²⁵⁷ If the transfer is between related parties e.g. intragroup parties or other parties with shared interests, shall the actual market price be used cf. the arm's length principle, see Article 9 OECD MC.

²⁵⁸ Short for controlled foreign corporation, i.e. companies that are residing in low-tax countries, but are controlled by, in this case, Norwegian residents.

a later time, will the input value of the asset or liability be set to the market value at the time of the re-entry. This is different from the general rule that the original cost price shall be set as the input value, and is reasoned by the objective to prevent international double taxation.

5.2.3 Relationship to the EEA-Agreement

After the “*National Grid Indus*” case was it made several amendments to the Norwegian exit tax provisions in order to ensure accordance with the EEA-Agreement, and the general exit tax duty on companies now mainly only apply if a company migrates to a state outside of the EEA. Assets and liabilities that are transferred abroad do also become subject to taxation, but if they are transferred to another state within the EEA, can the payment of the tax on most assets and liabilities be deferred. However, the payment of tax on intangible assets and inventories cannot be deferred, i.e. intangible assets and inventories are subject to immediate taxation at the time of the transfer. Thus can it still be questioned whether the Norwegian exit tax regime is fully compatible with the EEA-Agreement.

It is clear from EU/EEA-law that it is inconsistent to require immediate recovery of an exit tax, and the taxpayer must be able to opt between immediate and deferred payment of the tax.²⁵⁹ Immediate taxation of intangible assets and inventories with no possibility of deferral is therefore most likely an infringement of the EEA-Agreement. Per today however, there is no indication for that the Norwegian legislation will be amended.

5.3 Comparison of the different exit taxation regimes applicable on companies in the UK and Norway

Both the UK and Norway apply exit charges on companies that become non-residents for tax purposes, and on assets and liabilities that are transferred out of their respective tax jurisdictions. How their exit tax provisions are designed are on the other hand quite different. In the UK is there a more evident separation of exit taxes charged on migrating companies, and exit taxes charged on transferred assets and liabilities, and two individual set of rules are applied. A company that migrates from the UK and becomes a tax resident of another state within the EEA can choose between immediate payment of the tax debt, or opt for deferral. Assets or liabilities that are transferred to another EEA state can on the other hand be transferred tax-free as long as the transaction is genuine.

In Norway is it exactly the same rules that applicably in regard of transfer of assets or liabilities abroad, whether it only is a transfer of an asset or liability, or if the transfer happens as part of a company’s migration. The provisions particularly addressing migrating companies only regulate

²⁵⁹ See the cases “*National Grid Indus*” C-371/10 paragraph 86, “*Commission v. the Netherlands*” 301/11 paragraph 16, “*Commission v. Portugal*” C-38/10 paragraph 32.

when the exit tax on a company's unrealised capital gains is triggered (the migration) and provides exemptions from the general tax duty, e.g. that a Norwegian company can migrate to another EEA state without triggering the tax, as long as the transfer is genuine. In regard of assets and liabilities that will be subject to transfer, is it the general rules for transfer of assets and liabilities abroad that are applicable. It is those rules that specify how the exit charge applies to each asset or liability, and regulates deferral. Norway does not, as the UK, treat the migration of a company and transfer of assets and liabilities as two separate situations, but see them as two connected events.

As for the material substance are the two exit tax regimes more alike, at least in regard of the basics; exit taxes are applied to both migrating companies and transferred assets, deferral can be granted, security can be asked for in order to grant deferral and interest can be charged. Both systems have also taken regard to their obligations as member states of the EEA. However, the mechanisms for granting deferral differ from each other; the UK provides a seemingly complex system for grant of deferral, and a company can choose between the standard instalment method, where the tax is paid over a six-year period, or the realisation method, where the payment is deferred until the latent capital gain is realised or 10 year after the transfer, or a mix between the two. The realisation method however, does not apply to intangible assets, i.e. such assets must be paid in accordance with the standard instalment method. Under Norwegian law can companies, which migrate and become tax residents of another EEA country, simply defer the payment of the tax until the unrealised capital gains are realised. There is no upper time limit that deems realisation of the latent capital gain. The payment of tax on intangibles and inventories can though not be deferred; this is nonetheless similar to the UK provisions.

It is interesting that both UK and Norway have chosen limited deferral or not provide deferral in relation to intangible assets. Norway has reasoned its rule to not grant deferral to such assets because their nature; they will most likely not be disposed and their value will often vanish over time. It was therefore regarded that immediate taxation was necessary in order to ensure efficient recovery of the tax and prevent tax avoidance. To prevent tax avoidance was also an important objective behind the UK provisions. Nevertheless, the ECJ has mentioned the fact that some assets distinguish from others, because of their nature, but the taxpayer should still be able to opt for deferral. In the *Commission v. Denmark*²⁶⁰ case stated the ECJ nevertheless that the Member States are entitled to provide an alternative criterion for recovery of the tax, other than at the time the asset is sold. This was however limited to assets that were not expected to be realised. The Norwegian rule, which requires immediate payment of an exit tax charged on intangible assets, is most likely infringing Norway's obligations

²⁶⁰ The "*Commission v. Denmark*" case 261/11

under the EEA-Agreement, as there is no possibility of deferral. The UK provisions on the other hand, is probably in accordance with EU-law, as it provides the possibility to pay the tax debt of intangible assets in annual instalments over 10 years or in annual instalments over the useful life of the asset.

Differently from Norway, does the UK have a separate legal framework for the situation where an individual taxpayer of the UK (individual or legal person) transfers assets or liabilities abroad to another person. The transferor, or other beneficiary, becomes liable to tax in the UK if he receives income from the transferred asset or liability. However, assets or liabilities that are transferred to another EEA state are exempted from such tax as long as the transaction is genuine. This taxation regime is interesting as it is created only in order to counteract tax-avoidance schemes.

Overall do the UK and Norway have similar exit tax regimes, but there are individual differences when one looks more closely on how the provisions apply in the specific situation.

6 Concluding Remarks

The ECJ have ruled in several cases regarding exit taxes charged on companies the last years, and the legal framework around charge of exit taxes have become clearer; the main conditions under which the states can apply exit charges in situations where they lose their right to tax unrealised capital gains because of a cross-border migration or transfer within the EEA, has been set out. However, there are still issues that need to be figured. In one of the newest cases²⁶¹ by the ECJ has it been implied that the nature of specific assets can make it proportionate have another criteria than the actual realisation of the asset, to decide when the exit tax is to be finally recovered. Moreover, it is still undefined under what circumstances requirements as charge of interest and the obligation to provide security is proportionate.

The conflict between legitimate national interests of protecting the state's tax base and prevent tax avoidance, contra the functioning of the internal market principles is obvious, and the discussion above shows that national exit taxation regimes raise numerous issues both in a domestic- and EU/EEA-context. Nevertheless, the EEA consist of 31 different tax systems, and it is necessary that the states cooperate and harmonise their taxation regimes in order to ensure the functioning of the internal market. How such cooperation and harmonisation should be done, in order to protect both the state's sovereignty and ensure efficiency is not clear. The EU institutions have tried to set out "guiding principles" at EU-level, but the states have not been eager amend their national legislation in order to harmonise their taxation regimes. Additionally is it also an issue that the three EFTA-states, which

²⁶¹ Ibid.

participate in the EEA, are not subject to all of the same acts as the EU Member States. Nevertheless, exit taxes form an integral part of many states taxation regimes, and I do not think that they will be abolished in the nearest future.

Bibliography

Articles/Books/Reports

- Borchardt, Klaus-Dieter (2010): "*The ABC of European Union law*". European Union
- de Man, Fernando & Tiiu Albon: "*Contradicting Views of Exit Taxation under OECD MC and TFEU: Are Exit Taxes Still Allowed in Europe?*" INTERTAX, Volume 39, Issue 12, 2011 Kluwer Law International BV, The Netherlands, p. 613-626
- Kok, Reinout: "*Exit Taxes for Companies in the European Union after National Grid Indus*" ec Tax Review 2012-4, 2012 Kluwer Law International BV, The Netherlands, p. 200-206
- Law, Jonathan and Elizabeth A. Martin, Oxford Dictionary of Law, 7th edition, Oxford University Press
- Mathijssen, P S R F (2010): "*A Guide to European Union Law*" tenth edition, Sweet & Maxwell
- Panayi, Christiana Hji: "*Exit Taxation as an Obstacle to Corporate Emigration from the Spectre of EU Tax Law*". Cambridge Yearbook of European Legal Studies, Vol. 13, 2010-2011, p. 245-281
- Panayi, Christiana Hji (2013): "*European Union Corporate Tax Law*" Cambridge tax law series, Cambridge University Press
- Thömmes, Otmar and Dr Alexander Linn "*Deferment of Exit Taxes after National Grid Indus: Is the Requirement to Provide a Bank Guarantee and the Charge of Interest Proportionate?*" INTERTAX, Volume 40, Issue 8/9 2012 Kluwer Law International BV, The Netherlands
- von Brocke, Klaus & Stefan Müller, "*Exit Taxes: The Commission versus Denmark Case Analysed against the Background of the Fundamental Conflict in the EU: Territorial Taxes and an Internal Market without Barriers*". ec Tax review 2013-6 p. 299-304
- Zimmer, Frederik: "*Exit Taxes in Norway*". Word Tax Journal, October 2009, p. 115-148.

Case Law

- "*Costa v ENEL*" case 6-64 (1964)
- "*Daily Mail and General Trust*" case 81/87 (1988)
- "*Hughes de Lasteyrie du Saillant*" Case C-9/02 (2004)
- "*Cadbury Schweppes plc & Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*" case C-196/04 (2006).
- "*N v. Inspecteur van de Belastingdiens Oost/kantoor Almelo*" case C-470/04 (2006)
- "*Cartesio*" case C-2010/06 (2008)
- "*National Grid Indus BV v. Inspecteur van de Belastingdienst Rijnmond/kantoor Rotterdam*" case C-371/10 (2011)
- "*Commission v the Netherlands*" case C-301/11 (2011)
- "*Commission v Portugal*" case C-38/10 (2012)

- "Arcade Drilling AS v Staten v/Skatt vest" case E-15/11 (2012)
- "Commission v. Spain" Case C-269/09 (2012)
- "Commission européenne contre Royaume des Pays-Bas" case C-301/11 (2013)
- "Commission v Spain" case C-64/11 (2013)
- "Commission v Denmark" case C-261/11 (2013)
- "DMC Beteiligungsgesellschaft mbH v. Finanzamt Hamburg-Mitte" case C-164/12 (2014)

Communications/Opinions/Resolutions/Requests

- COM/2006/0825: "Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – Exit taxation and the need for co-ordination of Member States' tax policies"
- Council Resolution on coordination exit taxation, 2911th ECONOMIC and FINANCIAL AFFAIRS, Brussels, 2 December 2008
- Opinion of Advocate-General Mischo's to the "de Lasteyrie du Saillant" case (2003)
- Opinion of Advocate-General Kokott's to the "National Grid Indus" case (2011)
- Opinion of Advocate-General Kokott's to the "Denmark v. Commission" case (2011)
- Request (taxation): The Commission requests UK to amend two anti-abuse regimes, 16.02.2011
- Request (taxation): The Commission requests UK to amend its corporate tax legislation providing for the exit taxes on companies, 22.03.012

Legislation

Norway

- Skatteloven (1999)

The United Kingdom

- Finance Act (1994)
- Finance Act (1988)
- Finance Act (2013)
- Taxation of Chargeable Gains Act (1992)
- Income Tax Act (2007)

Treaties

- the EEA Agreement

- Treaty on the Functioning of the EU as amended by the Treaty of Lisbon (2007)
- Treaty of the European Union as amended by the Treaty of Lisbon (2007)
- OECD Model Tax Convention on Income and Capital (2010)
- UN Model Tax Treaty
- the Stockholm Convention

Other Sources

- <http://www.efta.int/about-efta/european-free-trade-association> (10.04.2014)
- <http://www.europa.admin.ch/themen/00500/index.html?lang=en> (10.04.2014)
- http://europa.eu/about-eu/countries/index_en.htm (10.04.2014)
- See amendments to the draft constitution proposed by the Commission, Article III-63 (corporate taxation) at http://ec.europa.eu/taxation_customs/resources/documents/amendments_iii_63_en.pdf (23.04.14)
- Taxation and Qualified Majority Voting, The Intergovernmental Conference of 2003-2004 at http://ec.europa.eu/taxation_customs/taxation/gen_info/conference/index_en.htm (23.04.14)
- Mary Adams, November 19, 2010: <http://www.i-capitaladvisors.com/2010/11/19/why-are-intangibles-not-on-the-balance-sheet/>