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To my precious daughter,
Maria Zacharia Palexa

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FOREWORD BY MALCOLM GAMMIE QC

For more than fifty years the European Project, currently incarnated as the European Union, has struggled with the issues of corporate taxation.[1] At an early stage the European Commission recognised that, in an ideal world, Member States should address these issues. So long as two or more States are engaged in a project to create a single market, national taxation of corporate profits is likely to present an obstacle to that project. The production of a single market system for taxing corporate profits raises a number of significant difficulties, however. The corporate tax is in effect a compromise: a surrogate, or an essential backstop, for the national system of taxing personal income. As a result, the corporate tax is likely to be tailored to the policies and priorities of national taxes on income. Nowhere is this more apparent than in the choices that States make for taxing company dividends. Dividend taxation systems link the corporate and personal tax systems and are the mechanism through which States integrate the two. They can be designed to reduce the distortion in financing via debt and equity by matching the deductibility of interest in computing profits with a credit for the corporate tax paid on profits, or by conferring a partial or complete dividend deduction or exemption.

At the same time, the jurisdictional limits of national taxation demand as a practical matter that States draw a line between what is national or domestic and what is international or cross-border. The international corporate tax system is founded on concepts of residence, of arm's length transfer pricing and of crediting foreign tax or exempting foreign income. At the same time cross-border taxation of dividends works on a classical basis, under which the residence country taxes profit distributions without regard to the source country's taxation of the profits. The economic and juridical taxation that results, and the distortion that these taxes produce in comparison to debt finance, are likely to be significant barriers to cross-border investment and the single market. None of these are

[1] I include dividend taxation as part of corporate taxation.

ordinarily found as features of a true single market, where 'residence' in a particular place in the market is irrelevant and where sub-national taxing jurisdictions more likely operate on a territorial basis, with formulary apportionment as necessary, and do not assert any right to tax dividends.

The publication by the European Commission in 1975 of a Draft Directive for the harmonisation of dividend taxation on an 'imputation' model attracted the attention of those in the United Kingdom with an interest in these matters. The UK had adopted a partial imputation system in 1973, abandoning its 1965 classical system and reverting more closely to its pre-1965 model. In the context of the UK's recent entry to the European Economic Community, it seemed as though the UK had made the correct choice and had charted a course compatible with the future development of an EEC corporate tax system.

As with other Commission initiatives, the 1975 Draft Directive came to naught and was finally withdrawn in April 1990. Indeed, the core problem from the outset with any Commission initiative was the failure of governments to truly engage in whatever debate then ensued. It would be many years before this changed. The pressures of the developing single market on corporate and dividend tax systems were not, however, going to abate and work by the Institute for Fiscal Studies drew attention to the importance of addressing the distortions created for cross-border investment by dividend withholding taxes.[2] It was against that backdrop and the preparations for the 'completion' of the single market from 1993 that the Member States adopted the French package of measures in Dublin on 11 June 1990. In 1990 the Commission also appointed the Ruding Committee to consider the fundamental issues that corporate tax systems raised for the single market. This represented the high-water mark at the time and, for some, offered renewed optimism for future progress; an optimism that was soon dashed by Member States' reaction to the Ruding Committee Report in 1992. It would take until the early 2000s before the Commission, led by Commissioner Mario Monti, would pursue with any real vigour the possibility of radical corporate tax measures.

The real development that was emerging in the mid-1990s, however, was the jurisprudence of the European Court of Justice. In 2012 it is easy to forget how irrelevant Community law was to daily corporate tax practice until well into the 1990s. From early beginnings in the 1986 *Avoir Fiscal*

[2] M. P. Devereux and Marie Pearson, *Corporate Tax Harmonisation and Economic Efficiency*, IFS Report Series No. 35, October 1989.

case,[3] concerning dividend imputation, references from national courts gathered pace throughout the 1990s and into the new millennium. This enabled the Court, with the benefit of the judicial activism of judges such as Michel Wathelet of Belgium and David Edwards of the UK, to assert the priority of the treaty freedoms over national tax systems that discriminated as a matter of course between the national and domestic and the international and cross-border. The extension of a restriction-based analysis to the tax sphere guaranteed the need for governments to take note of the impact of these developments on their tax systems and to reassess fundamentally their approach to and their engagement with the debate on corporate tax systems within the single market.

It is against this backdrop that Christiana HJI Panayi has reviewed the efforts of more than fifty years to achieve some rational progress in the corporate tax field and considers the limited corporate tax measures that have been adopted or are under discussion. A significant part of her book, however, is taken up with an analysis of the current case law and its implications for corporate taxation. The basic parameters set by the case law within which Member States can legislate in the corporate tax field are now relatively clear. There nevertheless remains substantial scope for analysis by commentators such as the current author to elucidate and cast light on the significant number of cases that now exist. Without political agreement on the role and direction for corporate taxes within Europe, Member States are left to strike the right balance between those matters within their competence and those that lie within the sphere and competence of the European Union. There is an ongoing need for expert criticism and commentary on their efforts. Progress in the corporate tax sphere may no longer be 'glacial',[4] but it may yet be some years before the current author can limit her task in a future edition to describing and analysing a single European corporate tax system.

One Essex Court & Institute for Fiscal Studies *Malcolm Gammie QC*

[3] Case 270/83, *Commission of the European Communities* v. *French Republic*, EC Court of Justice, 28 January 1986.

[4] John Isaac (Deputy Chairman, Inland Revenue), Corporate Tax Harmonisation, in *Beyond 1992: A European Tax System*, Proceedings of the Fourth IFS Residential Conference, Oxford 1989, eds. Malcolm Gammie and Bill Robinson, IFS Commentary No. 13.

FOREWORD BY PROFESSOR MICHAEL LANG

Tax law is still within the competence of the Member States. However, European Union law has become quite important. The Court of Justice of the European Union has become an important player. Before 1986 probably only a few experts had foreseen which limits the Court of Justice would put on the legislation of the Member States. In the meantime the Court has rendered hundreds of decisions. Today it is fair to say that the Court has developed common rules that serve as a framework for Member States. Judges who are interpreting their domestic law in the various Member States have no choice other than to take European Union law into account when rendering their decisions.

Since the Court of Justice of the European Union can only act as a 'negative legislator', the European Commission has tried to propose 'positive legislation'. In the meantime the European legislator has introduced some directives in the area of direct taxation that are part of European secondary law. Those directives do not have a broad scope yet and the Commission has started to propose new initiatives. In the area of corporate tax law the proposal for a CCCTB has become very important.

Christiana HJI Panayi has made the effort to not only collect all the rules and decisions that are relevant in the area of corporate taxation, but has also tried to bring all of the rules into a system and to describe that system in an understandable way. This task has been very successful and Christiana has written an extremely interesting book. She discusses European primary law as well as European secondary law. What is fascinating is the fact that it is much easier to see the full picture having read the whole book. At the same time she points to the open issues that cannot be solved by the Court of Justice of the European Union alone, but which need the action of the European legislator.

Therefore, I hope that not only will students and practitioners study the book, but that policy-makers all over Europe will make use of her research and will draw the conclusion that greater harmonisation is needed in the area of corporate tax law.

Professor at the Institute for Austrian and International Tax Law, WU, Vienna

Michael Lang

PREFACE

I decided to write this book after many years of teaching international tax law and EU tax law at Queen Mary, University of London and many years of research in this field. I assumed it would be easy to write a book that combines the two topics in examining the corporate angle to the tax developments in the European Union. I also assumed it would be easy to write this book while on maternity leave, after having my first child. Both of these assumptions proved wrong.

There was an enormous amount of material to be covered and the case law of the Court of Justice, especially the more recent one, was very challenging. The interplay with the OECD Model and general international tax law was always a source of potential conflict, generating interesting developments. The changes were fast-paced and often unpredictable. Trying to discern the past, present and future of EU corporate tax law was certainly not an easy task.

In writing the various chapters, I often found myself rereading old cases and gaining a different perspective from the one I had initially. I also developed a better understanding of endogenous changes in the case law in various areas. Some of the judgments were, however, completely perplexing – an indication of what I thought was the uneasiness of the Court of Justice in dealing with certain issues. Nevertheless, my admiration for the Court of Justice and its work in this area grew. The fact that today we have a developing body of principles that form what could be considered as the corporate tax law of the European Union is mostly attributable to the Court of Justice, as well as the Commission and national courts that trigger the European judicial process. The book depicts these themes and discusses the existing principles of EU corporate tax law.

This book would not have been written had it not been for my family. I would like to thank my husband Zak Palexas for his continuous inspiration, support and encouragement. I would also like to thank my parents for their help and the endless hours of babysitting they had to endure in order for me to be able to complete the book on time. Most of all I would

like to thank my daughter Maria for her patience in becoming so heavily involved in the tax world at such a young age. The number of times she shook her head in disbelief, deleted paragraphs from the draft and tore up papers laying around is perhaps an indication that the current state of the law is in need of some improvement. It is hoped that future editions of this book will reflect that.