

Newsalert

EU Direct Tax Group

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The EUDTG is one of PwC's Thought Leadership Initiatives and embedded in the International Tax Services Network. The EUDTG is a pan-European network of EU tax law experts and provides assistance to organizations, companies and private persons to help them to fully benefit from their rights under EU law.

JUDGMENT IN CASE C-470/04 (N.): DUTCH EXIT TAX DISPROPORTIONAL

On 22 January 1997 Mr. N. transferred his residence from the Netherlands to the UK. At the time he left the Netherlands, N. held 100% of the shares in three Dutch BV's (limited liability companies). The management of these BV's has since that same date been in the Netherlands Antilles. Due to his emigration, N. was pursuant to Dutch income tax law deemed to have disposed of his shares; consequently Dutch income tax was levied with regard to the difference between the market value and the acquisition price of the respective shareholdings. At his request, N. obtained a deferment of payment of income tax for a period of ten years, which deferment was made subject to the provision of a security. N. objected against both the fact that the Netherlands levied taxes upon emigration with regard to his substantial shareholdings and the obligation to provide security in order to obtain deferment of payment of taxes. He considered both measures in breach of EU law.

The *Gerechtshof te Arnhem* decided to stay proceedings and requested the European Court of Justice for a ruling.

On 7 September 2006 the ECJ ruled in favour of N. Article 43 EC applies to the situation of a Community national who, since the transfer of his residence, has been living in one Member State and holding all the shares of companies established in another.

With regard to the permissibility of taxing increases in value of shares on the transfer of a taxpayer's residence outside that Member State, the ECJ contemplated the following. The Dutch tax system, containing this taxation and the rules regarding the obtainment of a deferment of payment of income tax, is likely to restrict the exercise of the taxpayer's rights of establishment. A taxpayer wishing to transfer his residence outside Netherlands territory was subjected at the time of the facts to disadvantageous treatment in comparison with a person who maintained his residence in the Netherlands. After all, the latter person's value increases of shareholdings would only be taxed when and to the extent that they were actually realised. This difference in treatment was likely to discourage the person concerned from transferring his residence outside the Netherlands. More specifically the emigrant is confronted with the following three disadvantages: (1) he cannot obtain an automatic and unconditional suspension of payment of taxes; (2) the tax declaration required at the time of transferring residence outside the Netherlands; (3) decreases in value occurring after the transfer of residence were not taken into account in order to reduce the tax debt at the time of the facts in the main proceedings. To summarize: the Dutch tax system is likely to hinder the exercise of the freedom of establishment.

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However, the legislation at issue pursues an objective in the public interest and is appropriate for ensuring the attainment of that objective, being the allocation between Member States of the power to tax increases of value in substantial shareholdings on the basis of the territoriality principle. Still the measures at issue cannot stand the *rule of reason* test, since they go beyond what is necessary to attain the objective pursued. Firstly, the obligation to provide guarantees, necessary for the obtainment of a deferment of the tax normally due, is disproportionate, given the Council Directives on mutual assistance. Secondly, in order to be proportionate to the objective pursued, a system for recovering tax on the income from securities would have to take full account of reductions in the value capable of arising after the transfer of residence by the taxpayer concerned, unless such reductions have already been taken into account in the host Member State.

For more detailed information, please do not hesitate to contact your local PwC contact person or a member of the EUDTG.

Frank Engelen

+31 (0)10 407 5302

frank.engelen@nl.pwc.com

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