CONFEDERATION FISCALE EUROPEENNE

Opinion Statement of the CFE ECJ Taskforce on the judgment in the case of

Cartesio Oktató és Szolgáltató BT (Case C-210/06)

Judgment of 16 December 2008

Paper submitted by the
Confédération Fiscale Européenne
to the European Institutions
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This is an Opinion Statement on the ECJ judgment of Cortesia Oktató és Szolgáltató BT (Case C-210/06), prepared by the ECJ Taskforce[1] *of the Confédération Fiscale Européenne (CFE). The CFE is the leading European association of 32 national tax advisory organisations representing over 180,000 tax advisers.*

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1. On the 16th December 2008 the Grand Chamber of the ECJ delivered the long-awaited judgment in the Cartesio case. The case is not a tax case, but nevertheless the judgment had been long anticipated for what it might imply about the compatibility of exit taxes – particularly corporate exit taxes – with Community law[2]. In the final analysis, the Cartesio judgment says little about the compatibility of exit taxes, though some additional comments by the Court suggest that such charges on companies moving from one Member State to another may not be compatible with Community law.[3]

2. Cartesio was a limited partnership established in accordance with Hungarian law. It wished to transfer its seat to Italy, while remaining as partnership established in accordance with Hungarian law. Its application to register the transfer of its seat in the Hungarian commercial register was rejected, and the Commercial Court in Hungary referred several questions to the ECJ.

3. On the issue of substance, the ECJ concluded that, in the absence of a uniform Community law definition of those companies which enjoyed the right of establishment, it was a matter of national law to define which companies might rely upon the freedom

[1] Members of the taskforce who took part in discussion of this case were: Stella Raventos Calvo, Isabelle Richelle, Philip Baker, Daniel Gutmann, Michael Lang, Franck Le Mentec, Axel Cordewener, Volker Heydt, Albert Raedler and Friedrich Rödler. The views expressed in this statement do not necessarily represent the views of individual members of the taskforce or of organisations with which any of the members are associated.

[2] So far as exit taxes on individuals are concerned, the ECJ has already delivered judgments in De Lasteyrie (Case C-9/02, judgment of the 11th March 2004) and N (Case C-470/04, Decision of the 7th September 2006).

[3] It does not appear that the Hungarian partnership intended to move to Italy to gain any specific tax advantage. So far as members of the Taskforce are concerned, the case was brought as a test case to ascertain the current status of the Daily Mail case.

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of establishment in Article 43 (taken together with Article 48)[4]. Member States retain the power to define the connecting factors required before a company can be incorporated under the law of each state, and whether those connecting factors could be changed while the company maintained its status under the law of that state. Thus, the freedom of establishment did not prevent Hungary from insisting that a company governed by its law retained its seat in that territory[5]. In reaching this conclusion, the Grand Chamber differed from the conclusion proposed by the Advocate General.

4. The implicit relevance of the case for corporate exit taxes arose from any indication that would be given in the judgement as to the status of the Daily Mail case[6]. In that case, a company resident in the United Kingdom had sought to move its place of central management and control to the Netherlands in order that it could dispose of certain assets without a UK tax charge on its gains. At that time, under United Kingdom law, a company could not move its central management and control out of the United Kingdom without Treasury Consent; it would have been a criminal offence for the directors of a company resident in the United Kingdom to move central management and control without such consent. At the time, the ECJ concluded that there was no right under Community law for a company to move its central management and control to another Member State; the UK requirement of Treasury consent did not, therefore, conflict with Community law.

5. Strictly speaking, the Daily Mail case was not an exit tax case either. At that time, as explained, there was a prohibition – backed up by a criminal sanction – on a UK company becoming non-resident for tax purposes. Even so, in the last few years there have been some suggestions that the Daily Mail case might justify a different conclusion with regard to corporate exit taxes than for individuals. Had the ECJ in Cartesio expressed doubts over the correctness of the Daily Mail decision, then this possible justification of corporate exit taxes would have been removed.

[4] See paragraph 109 of the judgment.
[5] See paragraph 110 of the judgment.
[6] Case 81/87; judgment of the 27th September 1988.

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6. As it is, the ECJ in Cartesio appears to have understood the Daily Mail case for what it correctly was: a case concerning a prohibition on a company moving its central management and control to another Member State without consent.

7. It is worth noting that the UK rules with regard to movement of corporate residence have been changed since the time of the Daily Mail case. A UK company is now permitted to move its central management and control to another country, but this move triggers several possible exit charges[7]. The prohibition on a UK-resident company moving its central management and control to another jurisdiction (and the consequential criminal liability) has been abolished.[8]

8. The judgment in Cartesio follows Daily Mail in holding that the country under whose law a company is incorporated may prohibit the company from moving its seat or its place of central management and control to another country, while still remaining a local company under the law of that state. This has no direct impact on the position where, under the corporate law of a country, it is permitted to move the seat or the place of central management and control to another country, but there is simply a tax charge that is triggered by the exit.

9. In effect, the ECJ is drawing a parallel between the incorporation of companies and the nationality of individuals. An individual must have the nationality of a Member State to enjoy freedoms such as the freedom of establishment: it is clearly for the national law of each Member State to determine which individuals enjoy its nationality. Similarly, a company incorporated in a Member State enjoys the fundamental freedoms: it is for the domestic law of each Member State to define what conditions have to be satisfied for a company to be incorporated in that state, and whether a company, once incorporated, may shift any of those conditions to another Member State and yet still remain incorporated under the law of the first state.

[7] The primary charge is under s.185 of the Taxation of Chargeable Gains Act 1992, and involves a deemed disposal of all capital assets at their market value at the time of exit.
[8] The prohibition was in s. 765(1)(a) of the Income and Corporation Taxes Act 1988, which was repealed by s. 105 of the Finance Act 1988.

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10. The analogy with individuals raises some interesting questions on the Cartesio judgment. Suppose that a Member State provided in its domestic law that an individual who moved to another Member State would lose the nationality of his state of origin: the potential loss of nationality might well deter an individual from exercising his freedom of movement as a worker or as a citizen. Would such a rule for individuals be compatible with Community law?[9] For a company the potential loss of its incorporation – in effect, the death of the company – would equally deter that company from exercising its fundamental freedoms.

11. This analogy between individuals and companies explains why the European Commission has stated that "the interpretation of the freedom of establishment given by the ECJ in de Lasteyrie in respect of exit tax rules on individuals also has direct implications for Member States' exit tax rules on companies (...) It follows from de Lasteyrie that taxpayers who exercise their right to freedom of establishment by moving to another Member State may not be subject to an earlier or higher tax charge than taxpayers who remain in one and the same Member State" [10]. Some doubts may certainly remain whether the parallel between companies and individuals can still be made after the Cartesio judgment.

12. There are some ancillary comments in the ECJ's judgment that suggest that an exit tax would be an infringement of the freedom of establishment and would need to be justified. Though the ECJ was not called upon to do so, it discussed the situation where a company governed by the law of one Member State wished to move to another Member State and continue its existence under the law of the second state *and the law of the state of arrival contained provisions allowing it to continue its existence*[11]. In that situation, the ECJ indicated that the state of departure could not prevent the company from continuing under the law of another Member State by requiring the winding up or liquidation of the company. The ECJ commented that such

[9] Ignoring for a moment any prohibition under international law on a State making an individual stateless. The hypothetical might be phrased in terms of a State of departure requiring a former resident to give up its citizenship when he became entitled to apply for the citizenship of his State of arrival.
[10] COM (2006) 825 final, Exit taxation and the need for co-ordination of Member States' tax policies, p.
[11] This is discussed at paragraphs 111 and 112. Strictly speaking these comments are *obiter dicta* since they go beyond the question posed to the ECJ: there has been a noticeable trend in recent months for the ECJ to go beyond the question referred and add certain obiter comments.

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a situation would not fall within the domain of domestic law only, and that it would be an infringement of Community law to prevent such a company establishing itself in a state that was a willing recipient. This suggests that it would be an infringement of Community law for a Member State to impose a tax charge which might deter a company moving to another state where that move was lawful under both the law of the state of departure and the law of the state of arrival.

13. Overall, the decision in Cartesio provides no support for those who consider that corporate exit taxes are compatible with Community law. Rather, it gives some indication that the court will follow its jurisprudence with regard to individuals, and will find such corporate exit taxes to be incompatible with Community law.

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