PORUŠUJE ČESKÁ REPUBLIKA SVOBODU VOLNÉHO POHYBU KAPITÁLU?

DOES THE CZECH REPUBLIC VIOLATE A FREEDOM OF FREE MOVEMENT OF CAPITAL?

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Abstrakt
Příspěvek se zabývá problematikou dvojího zdanění a možného porušení svobody volného pohybu kapitálu jako jedné ze základních svobod ES. Některé dohody o zamezení dvojího zdanění umožňují, aby ČR, jako stát dlužníka, zdaňovala až 10% úroků ze smluv o úvěru. Text smluv o zamezení dvojího zdanění patří do pravomoci členských států. Nicméně při výkonu svých práv se státy musí řídit normami ES. Pokud vůči jiným státům ČR úroky nedaní, neměla by danit ani když je tato možnost dána smlouvou.

Klíčová slova
smlouva o zamezení dvojího zdanění, daň, volný pohyb kapitálu, úrok

Abstract
Essay covers the issue of double taxation and possible breach of free movement of capital as one of the basic freedoms of EC. Some contracts on avoiding double taxation enables CZ, as a borrower's state, to tax 10% of interests from the loan contract. The wording of contracts is under a national power. Nonetheless, while executing its power, shall the memberstate comply with ES laws. If interests flowing to other states are not taxed, CZ shall not tax even a part of interests despite given such a possibility by a contract.

Key words
contract on avoiding double taxatin, tax, free movement of capital, interest

Taxes are one of the biggest issues to businessmen all over the world. Tax laws are widely criticized, often due to their complicatedness. The occurrence of an international element in the legal relationship makes the issue even more complicated, as a new question, what tax laws to apply, is arisen. Taxation in both states is the worst solution, as it means an increasing price of the transaction and leads to restriction of international trade. States are familiar with this problem and it's unwanted consequences, therefore they are concluding the international agreements in order to prevent the problem. The contracts avoiding double taxation are not concluded with all states. On purpose are the agreements not signed with states which can be indicated as so called „tax paradises[1]". This approach is logical. If the agreement on avoiding double taxation is concluded with „tax paradise" state, the other state would loose a part of its income. Whereas the impact of such an agreement concluded between two „normal" states is equal, while a tax paradise would be a part of such an agreement a part of profits of companies would undoubtedly be transferred to tax paradise state and „normal" state would suffer. Not-concluding agreements on avoiding double taxation with the paradise states means control over all transfers to tax paradise state and tax income.

Even in European Union can be distinguished some states with features of a tax paradise. For example Cyprus and Luxembourg. Also the Netherlands differ in some tax areas from standard approaches. Nevertheless, none of these states is a typical tax paradise. The Czech Republic has concluded agreements on avoiding double taxation with all EU member states. Not concluding such an agreement would have meant impairing of a competitive position of the Czech Republic due to higher taxation of transactions and consequentially higher costs. It would be in the EU unacceptable and against basic principles of EC.

Let's take a look at bilateral agreements on avoiding double taxation signed by the Czech Republic with other EU memberstates with a particular focus on the regime of interests. There ate two types of agreements. The first type is concluded for example with Germany (18/1984Sb.). The relevant provision (Art. II sub. 2) on taxation of interests from loan contract is : „*Interests having its source in one memberstate and being payed in other memberstate may be taxed in the second state only.* " The second type of agreement has the Czech Republic agreed, for example, with Cyprus (30/1981Coll.). The relevant provision(Art.

1 Tax paradise is called a state with no or very low tax rates.

11 sub. 1) and 2)) is :„*1. Interest having its source in one memberstate and being payed to person with address/seat in other memberstate may be taxed in the second state..*
2 Interests being received from one memberstate by a person with address/seat in other memberstate , who is it's real owner, may be taxed in first state at a rate not exceeding 10% of the amount of interests brutto. “

There is a clear important difference between these two quoted types of agreements. In relationships under first type of agreement will the interests be taxed only in the lender's state. Whereas under second type of agreement 10% of interests may be taxed in the borrower's state and 90% of interests in the lender's state. It is obvious, that from the economical point of view the second type is less favorable than first one. Lender can optimize his tax duty, but only if all interests flow to his country. If a part of interests is kept and subjected to taxation in the borrower's state, the lender, in most cases, is not be able to optimize his duty.

Nowadays, there are two main sources for concluding a contract on avoiding double taxation. United nations drafted a UN Model double taxation convention[2]. The second source is OECD model convention with respect to taxes on income and on capital[3]. Both models enables borrower's state to keep a part of taxes. UN model is unspecific in this issue and leave it up to parties to agree. OECD declares 10% of interests. There is a reason for such a consent. The motive lies on protection before tax paradise states, as described above. But doesn't it create a restriction to free movement of a capital? Isn't it a discrimination of some capital sources?

Free movement of capital is one of the four basic freedoms in the EC. The area of free movement of capital has become the most liberalized aspect of internal market. The most important legal act was the Direction 88/361, which fixed a principle of overall and unconditional deregulation of movement of capital. The Direction allow states to impose protective measures if there is a short-term transfer of capital „*of a huge extent, which causes hardships in monetary policy*“. Protective measures might be imposed in specified areas and might not last more than 6 months.

Let's see some decisions and opinion of general advocate, which may clarify the view of ECJ on the matter.

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2 http://unpan1.un.org/intradoc/groups/public/documents/un/unpan002084.pdf
3 http://www.oecd.org/dataoecd/52/34/1914467.pdf

Opinion of general advocate in case Columbus Container Services BVBA&Cc. (C298/05)

Under German law is the tax authority allowed, based on the contract on avoiding double taxation, to replace the regime of liberation from tax by charging a tax, should the taxes in abroad be very low. The preliminary ruling question was considering whether such a rule does not interfere with a freedom of movement. Although this question is not at stake, it may show the point of view in such a matters. Quotation form the opinion:" *The prohibition to create restriction of freedom of movement applies even on tax laws. Despite direct taxes are not covered by EC laws and EC authorities do not apply powers over the matters, must memberstates live up to the EC laws when applying their power*." As a result memberstate was not empowered to draft a tax law whose purpose was taxation of income artificially „created" in abroad, since it was against the freedom of movement. According to the ECJ, although the national law does not prohibit the taxpayer to perform his right of free movement, it is of such a „*nature, that might discourage some people to move abroad*" and as a consequence, is capable to create a obstacle in freedom of free movement. In case Cadbury Schweppes and Cadbury Schweppes Overseas ECJ held that different (higher) taxation and disadvantagedness flowing from such laws for companies – taxpayers owning a daughter company, which is taxed in other memberstate by lower taxes, may prevent such companies from establishing a daughter companies in abroad, which is a limitation of freedom of settlement.

ECJ distinguishes between division *power to taxation* between memberstates, where different approaches are legal and do not interfere with freedom of movement and *execution of power to taxation*, where memberstates must comply with EC laws. From the foregoing it seems that memberstates keep not only opportunity to prevention of double taxation, but also the choice of mechanism to prevent double taxation, which basically means the method of liberating of taxes or the mechanism of crediting taxes payed in other memberstate.

Liberating from income tax does support seating in abroad and investment going in abroad, compared to home investments. Utilization of different methods to prevent double taxation may not be criticized. At present EC laws allows memberstates to determine the tax base. Under my opinion shall memberstates be given the right to use different methods to prevent double taxation depending on type of income, but freedom of free movement must be complied.

Judgement in Meilicke case (C-292/04)

This case was about taxation of dividends flowing form other state, than the state of domicile of recipient. ECJ found, that reviewed tax law may discourage investments in companies in other memberstates. The reasoning says: „*Conversely, that legislation is liable to have a restrictive effect as regards those companies, in that it constitutes an* ***obstacle*** *to their raising capital in Germany. Since dividends of non-German origin receive* ***less favorable tax treatment*** *than dividends distributed by companies established in Germany, the shares of companies established in other Member States are less attractive to investors residing in Germany than shares in companies which have their seat in that Member State*"

It flows from the highlighted text that ECJ considers the obstacles while acquiring the capital to be obstacles of free moment of capital.

Decision on Manninen case (C-319/02)

This case was also about taxation of dividends flowing from foreign companies . ECJ held that direct taxes belongs to the powers of memberstates, but while executing this power shall memberstates live up to the EC laws[4]. Another important outcome was that ECJ admitted that basic freedoms might be restricted if it is necessary for keeping the cohesion of the tax system. „*However, for an argument based on such justification to succeed, a direct link had to be established between the tax advantage concerned and the offsetting of that advantage by a particular tax levy*[5]*. ECJ also held „ The case-law further shows that an argument based on the need to safeguard the cohesion of a tax system must be examined in the light of the objective pursued by the tax legislation in question (Case C-9/02 De Lasteyrie du Saillant [2004] ECR I-0000, paragraph 67)".*

Analysis and conclusion

Free movement of capital is one of the four basic freedoms, which are grounds of EC internal

4 Also Case C-80/94 Wielockx [1995] ECR I-2493, paragraph 16; Case C-264/96 ICI [1998] ECR I-4695, paragraph 19; and Case C-311/97 Royal Bank of Scotland [1999] ECR I-2651, paragraph 19

5 see, to that effect, Case C-484/93 Svensson and Gustavsson [1995] ECR I-3955, paragraph 18; Asscher , paragraph 58; ICI , paragraph 29; Case C-55/98 Vestergaard [1999] ECR I-7641, paragraph 24; Case C-436/00 X and Y [2002] ECR I-10829, paragraph 52.

market. Free movement of capital is confirmed in articles 56-60 of EC Treaty (Nice version). These provisions prohibit all restrictions of movement of capital and payments, both between memberstates and between memberstate and third state. Provision of article 58 EC Treaty empowers states to distinguish between residents and non-residents and to take a measure to prevent infringement of national laws. But measures and differentiation may only be applied if none of basic EC freedoms is infringed.

It flows from above mentioned decisions, that difference between contracts on prohibition of double taxation can, from EC point of view, be considered to be an obstacle in obtaining a capital and therefore an obstacle of free movement of capital. Two questions remain. Is such an obstacle acceptable under art. 59 EC treaty? Does this field fall under EC competence ?

Article 58 EC Treaty lays a ground for tax residents and non-residents with a different rate. It can be considered as measure against infringement of national laws, eventually for protecting unitary character of national tax laws. The contract with Cyprus was obviously agreed in order to prevent leaking of capital from the Czech republic. It is no excuse, that the contract has been agreed under any model contract. Model contracts only allow state to conclude such a provision, it is not a duty. Moreover, the main rule in the model contracts still is, that interests are taxed in the country of lender. Admissibility of restriction of free movement of capital was mentioned in Manninen case. ECJ held that it is necessary to compare the aims of restrictions with necessity of protection of tax unity. Under my opinion there is no necessity to protect tax unity. If all interests may flow to Germany, there is no reason why the same should not apply towards Cyprus (it is multiplied by a fact, that both states are EC memberstates). The Czech Republic is obviously protecting it's tax income, but it, in the same time, implicitly means, that the Czech Republic is willing to obstruct the free movement of capital. This is not a matter of only the Czech Republic. None of states has concluded all tax contracts in similar regime, which means unequal position among states. From my point of view, it is a restriction of free movement of capital incompatible with art. 56 EC Treaty. This concluded can be made under present situation, when it is distinguished between ***allocating*** *of tax powers* among memberstates, under which a different approach to residents and non-residents does not fall within the framework of free movement of capital under EC Treaty and between ***execution*** *of tax powers* by memberstates, when memberstates are obliged to comply with EC rules.

That brings me neatly to the question, whether contracts on avoiding the double taxation are under powers of EC authorities. It flows from the previous paragraph, decisions and contracts themselves, that wording of contracts on avoiding the double taxation is beyond the powers of EC authorities. At least for today. We may suppose a change in the future and extending the EC power over this issue as well, for as this essay shows, double taxation may create a restriction of free movement of capital.

On the other hand, the execution of tax powers is governed by EC rules. If the provision of the contract on avoiding the double taxation enables all interests to be taxed by lender's state and the same regime is applied with other stated, it is under my opinion to conclude, that if a memberstate does not employ this regime, in other words if the memberstate wants to keep a part of interests and to tax this part, then such a memberstate is creating a restriction of free movement of capital and is in breach of art. 56 EC Treaty.

Conclusion

Using 2 types of contract on prevention of double taxation is unsuitable from economic view, as it means discrimination of some of capital flows or at least unequal position. The tougher regime may be considered as restriction of free movement of capital. The contracts on avoiding the double taxation do not fall under EC's powers. Memberstates are allowed to agree contracts on avoiding the double taxation in any wording. But if from the wording of contract on avoiding the double taxation flows that it is up to the state to choose whether it will apply tougher regime compared to the other states, then the memberstate is obliged to live up to the EC commencements and choose the regime he has with third states (softer). Only such a choice would mean no restriction of free movement of capital and therefore no infringement of art. 56 EC Treaty.

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