



INTERNATIONAL  
HELLENIC  
UNIVERSITY

**TAX AVOIDANCE THROUGH CONTROLLED  
FOREIGN CORPORATIONS IN  
INTERNATIONAL-EU TAX LAW**

**MAKRINA CHOIDOU**

**SCHOOL OF ECONOMICS, BUSINESS ADMINISTRATION & LEGAL  
STUDIES**

A thesis submitted for the degree of

***LLM in Transnational and European Commercial Law, Mediation,  
Arbitration and Energy Law***

January 2016

Thessaloniki – Greece

Student Name:

Makrina Choidou

SID: 11040009

Supervisor: Prof. George Matsos

I hereby declare that the work submitted is mine and that where I have made use of another's work, I have attributed the source(s) according to the Regulations set in the Student's Handbook.

January 2016

Thessaloniki – Greece

## Abstract

This dissertation was written as part of the LLM in Transnational and European Commercial Law, Mediation, Arbitration and Energy Law at the International Hellenic University.

Its aim is to point out the importance of a coherent international tax regime. From 1990, with the advent of globalization, economic changes- especially the rise of cross-border trade-investments and financial flows- influenced international trade competition and the control that governments used to have in their economic outcomes and taxing powers. Tax laws of various jurisdictions, because of the interaction with each other, fostered harmful tax competition. Governments, competing with one another for scarce capital, adopted tax- friendly policies in order to increase investments and cross-border trade. This led to the establishment of tax havens and to an “illegal” flow of capital.

The European Union and the Organization for Economic Co-operation and Development (OECD) aim to avert a “race to the bottom<sup>1</sup>” in tax rates and to pressure tax havens to adopt a uniform –equal to other States tax, financial and banking regulation .A global tax regulation is an important case to limit harmful tax competition and to assign taxing powers. There is a primary need to deal with similar problems in jurisdictions in order to reach quiet similar results by adopting and applying the Model Double Taxation Convention on Income and Capital of OECD. The explanation below of this Model Convention and the different interpretation of various jurisdictions give us a clearer picture about how important is the application of an international tax regime in order to discourage the spread of tax havens and to improve tax policies internationally.

MakrinaChoidou

30/1/2016

---

<sup>1</sup><https://books.google.nl/books?id=34prlaz9rUwC&printsec=frontcover&dq=inauthor:%22Jason+Campbell+Sharman%22&hl=nl&sa=X&ved=0ahUKEwiUx5D5zcTKAhXCvRoKHUvXCUIYQ6AEIIDA#v=onepage&q&f=false>

## PREFACE

“Tax avoidance” and “Tax evasion” are two distinct terms, but occasionally corporate strategies and behaviors associated with them exhibit common characteristics. Elaborating further on the aforementioned terms will enable the reader to apprehend their differences and grasp the variety of the methods that are used in order to achieve tax avoidance or tax evasion.

Tax avoidance is the legitimate minimizing of taxes. The use of legal methods to modify an individual's financial situation in order to lower the amount of income tax owed<sup>2</sup>. This is generally accomplished by claiming the permissible deductions and credits. Tax avoidance is entirely legal and is where you take steps to minimize your tax bill. It is like bending the rules rather than breaking them<sup>3</sup>.

Tax evasion, on the other hand, is the illegal practice of not paying taxes, by not reporting income, reporting expenses not legally allowed, or by not paying taxes owed<sup>4</sup>. Tax evasion often entails taxpayers deliberately misrepresenting the true state of their affairs to the tax authorities to reduce their tax liability and includes dishonest tax reporting, such as declaring less income, profits or gains than the amounts actually earned, or overstating deductions<sup>5</sup>. Tax evasion is an activity commonly associated with the informal economy.

Despite the very different interpretation of the aforementioned terms, according to a recent poll in the UK, voters don't see a distinction between tax avoidance and tax evasion, at least not a moral one. According to a YouGov survey, 59 percent considered avoidance “unacceptable,” while only 32 percent thought it was legitimate<sup>6</sup>. As follows, the distinction between these terms is not always clear. The

---

<sup>2</sup> [http://www.investopedia.com/terms/t/tax\\_avoidance.asp](http://www.investopedia.com/terms/t/tax_avoidance.asp)

<sup>3</sup> <http://www.encyclopedia.com/topic/taxation.aspx>

<sup>4</sup> “What is the difference between tax avoidance and tax evasion” Jean Murray (published at 23/1/2016) <http://biztaxlaw.about.com/od/businessstaxes/f/taxavoidevade.htm><sup>5</sup>  
[https://en.wikipedia.org/wiki/Tax\\_avoidance](https://en.wikipedia.org/wiki/Tax_avoidance)

<sup>6</sup> “Tax Avoidance Or Tax Evasion? There Is A Difference”, Joseph Thorndike,  
<http://www.forbes.com/sites/taxanalysts/2015/03/12/tax-avoidance-or-tax-evasion-there-is-a-difference/>

line between “tax avoidance” and “tax evasion” can be very thin and at times indistinguishable. This opinion is not restricted in UK or in the territory of one’s State, but is a common international opinion.

First of all, it has to be understood that tax evasion is an absolutely illegal practice of avoiding taxes and as a consequence should be distinguished from tax avoidance and should be punished every strategy which aims to evade tax. As far as tax avoidance is concerned, it constitutes an international phenomenon of primary importance which preoccupies both national governments and international organizations and its elimination or “extinction” is a global goal.

Nowadays, in economic crisis international tax avoidance is flourishing rapidly because of everyone’s (individuals, corporations, governments) desire to generate more cash and to increase his profits. The mechanisms that are usually used to avoid tax are various, some of which are: Controlled Foreign Corporations<sup>7</sup> which are established in tax havens, the artificial transfer of losses within multinational groups, the indirect transfer of profits from countries with high tax rates in countries with low tax rates, the abusive use of double tax treaties (treaty-shopping) for pumping tax benefits from their implementation. All the aforementioned mechanisms aim to reduce the imposing tax, by taking advantage of different tax legislation and exploiting the interaction and the “gaps” between the various jurisdictions in order to ensure greater profit. Consequently, their goal is to avoid tax but not tax evasion.

The measures taken at a national and an international level with a view to dealing with tax avoidance vary. The plethora of laws, which are different in every State, creates crucial difficulties in the final resolution of this international phenomenon. Current legal reforms have attempted to adopt a uniform legal mechanism to impede instances of tax avoidance across the globe.

---

<sup>7</sup>see.Chapter1 i- The distinction between CFC and offshore companies.

## Contents

ABSTRACT.....	3
PREFACE.....	4-5
CONTENTS.....	6
INTRODUCTION.....	7
CHAPTER 1 :THE TERM OF CINROLLED FOREIGN CORPORATIONS.....	
I. OECD.....	8-11
II. DINSTICTION BETWEEN CFC ANF OFFSHORE COMPANIES.....	12-16
CHAPTER 2: AN OFFSHORE COMPANY.....	
I.INCENTIVES FOR ESTABLISHING AN OFFSHORE COMPANY.....	17-18
II.FORMS OF AN OFFSHORE COMPANY .....	19-21
CHPTER 3: LEGISLATIVE FRAMEWORK AGAINST TAX AVOIDANCE.....	
I.EUROPEAN REGULATORY FRAMEWORK .....	22-27
II.CFC LEGISLATION.....	28-37
CHAPTER 4 : CFC APPLICATION.....	
I.CFC LEGISLATION IN DIFERRENT COUNTRIES.....	38-40
II.CASE-LAW.....	41-44
CONCLUSION.....	45-46
BIBLIOGRAPHY.....	47-49

## INTRODUCTION

Globalization has benefited our domestic economies. The free movement of capital and labour, the shift of manufacturing bases from high-cost to low-cost locations, the gradual removal of trade barriers, technological and telecommunication developments, have influenced the way that cross-border activities take place<sup>8</sup>. Globalization has facilitates the flourishing of trade and the expansion of foreign direct investments in many countries<sup>9</sup>. Also, globalization impacts countries' corporate income tax regimes<sup>10</sup>.

The interaction of domestic tax systems leads not only to the creation of tax havens, but also to instances of double taxation (non-taxation), which in turn have unfavorable effects on growth and global prosperity<sup>11</sup>. Countries across the world agree on the need to eliminate double taxation by creating a set of agreed international rules that are clear and predictable, giving certainty to both governments and businesses<sup>12</sup>. Not only from EU but also from international perspective a common tax regime is the only way to struggle over harmful tax competition and to allocate taxing powers between various jurisdictions. Also, a coherent international tax law framework is an essential prerequisite in order to stimulate growth across the globe.

---

<sup>8</sup>“Technology, globalization, and international competitiveness: Challenges for developing countries”,Car IDahlman,  
[http://www.un.org/esa/sustdev/publications/industrial\\_development/1\\_2.pdf](http://www.un.org/esa/sustdev/publications/industrial_development/1_2.pdf)

<sup>9</sup> <http://www.oecd.org/ctp/BEPSActionPlan.pdf>

<sup>10</sup> During World War II, states with limited economic power and precarious sovereignty in order to maintain their state entity and strengthen their economic independence, offered favorable conditions of business activity to foreign investors(providing tax reliefs and exemptions on insurance and labor level), in order to attract foreign capital and encourage investment mobility within their territories- this This practice leads to the creation of the first tax havens.

<sup>11</sup> <https://books.google.gr/books?id=EVMaAAAAQBAJ&pg=PA9&lpg=PA9&dq=The+global+economy>

<sup>12</sup> <http://www.oecd.org/ctp/BEPSActionPlan.pdf>

## CHAPTER 1

# THE TERM AND EXPANSION OF CONTROLLED FOREIGN CORPORATIONS (CFC)

### I.OECD

Since at the 1920s, it has been recognized that the interaction of domestic tax systems can lead to overlaps in the exercise of taxing rights that in turn can result in double taxation<sup>13</sup>. Countries, despite their desire not to compromise their taxing sovereignty, aim to eliminate trade distortions and impediments to sustainable economic growth through an equal allocation of taxing rights. There were important differences and frictions between different countries' tax systems that were not taken in account in bilateral tax treaties. Tax sovereignty should be protected through international collaboration on tax matters<sup>14</sup>.

The Organization for Economic Co-operation and Development (OECD) is an international economic organization of 34 countries, founded in 1961 to stimulate economic progress and world trade<sup>15</sup>. Issues that concern OECD are taxation and the operation of tax havens<sup>16</sup>. The common tackling of tax evasion in international level, a loyal cooperation between all states and also the adaptation of a uniform legislation, that regulates international tax issues, constitutes an ultimate goal of OECD.

---

<sup>13</sup><https://books.google.gr/books?id=EVMaAAAAQBAJ&pg=PA9&lpg=PA9&dq=The+global+economy>

<sup>14</sup>“Bringing the International Tax Rules into the 21st Century: The Progress Made So Far”, Luisa Fernanda Ríos, <http://globalsummitryproject.com.s197331.gridserver.com/blog/global-summitry-report/bringing-the-international-tax-rules-into-the-21st-century-the-progress-made-so-far/>

<sup>15</sup>[https://en.wikipedia.org/wiki/Organisation\\_for\\_Economic\\_Co-operation\\_and\\_Development](https://en.wikipedia.org/wiki/Organisation_for_Economic_Co-operation_and_Development)

<sup>16</sup>The OECD Council in 1998 approved the report, “Harmful Tax Competition, An Emerging Global Issue<sup>16</sup>”, which aim was to identify and eliminate harmful features of preferential tax regimes in OECD member countries, develop measures to counter the distorting effects of harmful tax competition on investment and financing decisions and the consequences for national tax bases, also to identify “tax havens” and seek their commitments to the principles of transparency and effective exchange of information.

In 1963 OECD published the Double Taxation Convention on Income and Capital, which was revised in 1977 and led to the establishment of the Model Double Taxation Convention on Income and Capital. The liberalization of capital flows and globalization of business operations were factors that led to another revision in 1992. The free movement of persons, services and capitals are crucial factors that led to the last revision in 2010 and 2014.

The existence of Model Convention has facilitated bilateral negotiations between OECD Member countries and made possible a desirable harmonization between their bilateral conventions for the benefit of both taxpayers and national administrations<sup>17</sup>. The Contracting States by adopting the Model Convention deals with fiscal reforms in global level and promotes a single tax policy for tax avoidance.

The main issue that is regulated in the Model Convention is the phenomenon of double taxation. Income or profits stemming from international activities, such as cross-border investments, may be taxed based on the location where the income is earned or based on the residence of the individual who is entitled the taxable income<sup>18</sup>. As some countries impose taxes at source – where the taxable income is generated, whilst others tax on a residence basis – where the person who receives the income is based – double taxation is a quite frequent phenomenon<sup>19</sup>. Double taxation can be defined *in abstracto* as the imposition of tax levies by two or more jurisdictions on the same declared income stream (in the case of income taxes), asset case or financial transaction<sup>20</sup>. Accordingly, double-taxation occurs when two different countries impose taxes on the same income stream or property for the same period and in the hands of the same taxpayer<sup>21</sup>. Notwithstanding this, double non taxation in both inbound<sup>22</sup> and outbound<sup>23</sup> scenarios constitutes another

---

<sup>17</sup> <http://www.oecd.org/berlin/41215950.pdf>- Introduction of OECD Model Convention

<sup>18</sup>“ SOURCE AND RESIDENCE TAXATION “ Tax Justice Briefing,  
[http://www.taxjustice.net/cms/upload/pdf/Source\\_and\\_residence\\_taxation\\_-\\_SEP-2005.pdf](http://www.taxjustice.net/cms/upload/pdf/Source_and_residence_taxation_-_SEP-2005.pdf)

<sup>19</sup>“ Taxing International Income: An Analysis of the U.S. System and Its Economic Premises” Hugh J. Ault and David F. Bradford. <http://www.nber.org/chapters/c7203.pdf>

<sup>20</sup> [https://en.wikipedia.org/wiki/Double\\_taxation](https://en.wikipedia.org/wiki/Double_taxation)

<sup>21</sup> [http://ec.europa.eu/taxation\\_customs/taxation/individuals/double\\_taxation\\_en.htm](http://ec.europa.eu/taxation_customs/taxation/individuals/double_taxation_en.htm)

<sup>22</sup> <http://www.oecd.org/ctp/BEPActionPlan.pdf> “From an inbound perspective, the concern regarding interest expense deduction is primarily with lending from a related entity that benefits from a low-tax regime, to create excessive interest deductions for the issuer without a corresponding

crucial problem that concerns many States. There is no general EU measures to eliminate double taxation (and non taxation), but most EU countries either assign bilateral tax treaties which are based to the legal text of the Model Double Taxation Convention on Income and Capital or adopt the Model Double Taxation Convention on Income and Capital in their domestic law.

Moreover, domestic tax systems do not always stay in step with the current economic needs due to the increasingly global flow of capital and the rise of digital economy. In this occasion, international corporations, by exploiting legal gaps and mismatches, aim to double non-taxation and undermine the fairness and integrity of tax systems<sup>24</sup>.

Base Erosion and Profit Shifting (BEPS) concerns tax planning strategies that aim to avoid -wholly or partially- the corporate tax and shift profits to low or no-tax locations where sometimes they do not exercise any economic activity. The main object of BEPS is corporate income tax, especially from multinational enterprises (MNEs) and as a consequence it is primarily important for developing countries<sup>25</sup>.

BEPS is a crucial problem which requires common solutions in global level. The G20 finance ministers called on the OECD to develop an action plan to address BEPS issues in a co-ordinated and comprehensive manner. Specifically, this Action Plan should provide countries with domestic and international instruments that will better align rights to tax with economic activity<sup>26</sup>. As called for in the recent OECD report on BEPS, Addressing Base Erosion and Profit Shifting (OECD, 2013), "this Action Plan identifies actions needed to address BEPS, sets deadlines to implement these actions and identifies the resources needed and the methodology to implement these actions". The OECD's Action Plan on BEPS was published in July 2013 with a view to addressing

---

interest income inclusion by the holder. The result is that the interest payments are deducted against the taxable profits of the operating companies while the interest income is taxed favourably or not at all at the level of the recipient, and sometimes the group as a whole may have little or no external debt."

<sup>23</sup> <http://www.oecd.org/ctp/BEPSActionPlan.pdf> " From an outbound perspective, a company may use debt to finance the production of exempt or deferred income, thereby claiming a current deduction for interest expense while deferring or exempting the related income."

<sup>24</sup> <http://www.oecd.org/ctp/beps-about.htm>

<sup>25</sup> <http://www.oecd.org/ctp/beps-about.htm>

<sup>26</sup> <http://www.oecd.org/ctp/BEPSActionPlan.pdf>

perceived flaws in international tax rules<sup>27</sup>. The final BEPS package provides countries with the tools needed to ensure that profits are taxed at the location where economic activities generating the profits are performed and where value is created. Moreover, the BEPS package provides businesses additional operational certainty, by clarifying disputes over the application of international tax rules and leveling compliance requirements. The application of BEPS package establishes the synergies of OECD and G20 countries for a modern international tax mechanism which ensures that profits are taxed at the location where the relevant economic activity take place.

As a conclusion, the role of OECD is very important given the fact that is the one and only international economic organization, which issues legislative arrangements dealing with tax avoidance and put internationally an anti-tax avoidance framework. Through the Model Double Taxation Convention on Income and Capital and the Action Plan on BEPS aim to change the existing international standards on the allocation of taxing rights on cross-border income and capital and resolve the global economy's difficulties that have crucial impact on governments, individuals tax payer and businesses .

---

<sup>27</sup> "10Minutes on the OECD's BEPS project ",<http://www.pwc.com/gx/en/services/tax/tax-policy-administration/beps.html>

## II. DISTINCTION BETWEEN CFCs AND OFFSHORE COMPANIES

As already mentioned, OECD, aiming at a single regulation of international tax issues and trying to deal with tax avoidance, has published the Model Double Taxation Convention on Income and Capital which is not binding, so it should be adopted by States and integrated in their domestic law. Controlled Foreign Corporations is a mechanism that many companies use in order to avoid taxes and to shift income from one jurisdiction to another. The operation and the taxation of Controlled Foreign Corporations (CFC) constitute one of the main configuration topics in Model Double Taxation Convention on Income and Capital. The term of Controlled Foreign Corporations (CFC) is used to describe the companies which restrict or distort the real economic activity. "CFC-Legislation" is used in many countries as a mean to prevent erosion of the domestic tax base and to discourage and preclude residents from shifting income to jurisdictions that do not impose tax or that impose tax at low rates<sup>28</sup>. Because of the non-binding nature of the Model Convention every Contracting State has the discretion to adopt and to modulate the provisions of the Model Convention according to its domestic legislation. As a consequence, rules applicable to CFCs differ from country to country due to different structure of the domestic tax system and different strategies of tax payers. Nevertheless, the key characteristics and operational aspects of CFCs are identical in virtually every jurisdiction. This can be demonstrated more clearly by explaining the main aspects of "Controlled Foreign Corporations".

*"Controlled"*: Any legal entity falling under CFC legislation must be "controlled" directly or indirectly by a domestic taxpayer. Control is the power to exercise sufficient influence over a company either over its management or its policies. According to Public Discussion on Action Plan on Base Erosion and Profit Shifting directed the OECD the definition of control requires two different determinations, the type of control that is required and the level of that control. Legal control is determined according to resident's holding of share capital in order to define the

---

<sup>28</sup> <http://www.oecd.org/tax/aggressive/discussion-draft-beps-action-3-strengthening-CFC-rules.pdf>

<sup>29</sup> "Multinationals will be concerned about additional complexity in controlled foreign company proposals", Tax Policy Bulletin (22/1/2016) <https://www.pwc.com/gx/en/tax/newsletters/tax-policy-bulletin/assets/pwc-additional-complexity-controlled-foreign-company-proposals.pdf>

percentage of voting rights held in a subsidiary, elect the board of directors and thus ensure that a CFC acts in accordance with their instructions. Economic control refers to the right to the profits, capital and assets of a company in special circumstances , like dissolution or liquidation. The notion of the level of control is wider. The goal is to deter every controlling party from shifting profits to a foreign company. But of course, CFC rules demand a minimum level of control in order to be applied, which is customary to be more than 50% of legal or economic interest of resident taxpayers in the foreign entity.

“Foreign”: the domestic tax law of every country defines whether a corporation is foreign or not -it depends upon whether the incorporation theory or the real seat theory is applied by the State.

“Corporation”: the interpretation of the term corporation varies due to the differences of domestic company laws. But the common characteristics which could be distinguished are that corporation is an entity separate and distinct from its owners with legal existence, continuity of existence, and limited liability (private or public)<sup>31</sup> .

By explaining the term of CFC, Contracting Parties are facilitated to discern CFCs from other types of corporations. Regardless of the naming of the foreign corporation in every Contracting State the main characteristics and the goal of CFCs are identical in every jurisdiction. When a corporation fulfilled the aforementioned prerequisites and its operation and taxation led to establishing tax havens could be characterized as Controlled Foreign Corporation (CFC legislation is also applicable).

In Greece is commonly used the term of “offshore” company. This term means far from the coast, because it originated in England, which is a big island. As a consequence, “offshore” means "extra-territorial", and characterized international

---

<sup>30</sup> <http://www.oecd.org/tax/aggressive/discussion-draft-beps-action-3-strengthening-CFC-rules.pdf>

<sup>31</sup> <http://www.businessdictionary.com/definition/corporation.html>

foreign entrepreneurship. In Greece, at firstly ,art. 5 (7) in law no 3091/2002 introduced the notion of “offshore” (eksohoria)<sup>32</sup>:

*“For the purposes of this law an offshore company shall be a company which has its seat in a country abroad and, according to the laws of that country, acts only outside that country and enjoys a particular advantageous tax treatment.”*

Through the comparison between the aforementioned terms arising that the prerequisite of *control* that should be taken by a domestic taxpayer in CFC lacks as a prerequisite from the concept of “offshore” company. Offshore company is a company according to Greek Company Law, operating not in the country of her registered office, but in a *foreign* country utilizing her (foreign) law in order to be engaged exclusively in other States and enjoy favorable tax treatment.

In addition CFC legislation are applicable to cases that put a high risk of base erosion and profit shifting .As the Public Discussion Draft BEPS Action 3 Strengthening CFC rules is mentioned, “ thresholds , such a de minimis amount which the CFC rule would not apply, can therefore help make CFC rules more targeted and effective by ensuring that certain companies are not subject to the rules <sup>33</sup> . Many countries’ rules<sup>34</sup> already include a de minimis threshold under which income that would otherwise be treated as CFC income is not included in the taxable income of the parent company if it falls under a certain ceiling<sup>35</sup> .” Law –tax thresholds, using a comparative approach on a case-by-case basis<sup>36</sup> or black or white list, are applicable in many jurisdictions in order to define

---

<sup>32</sup> Michael Lang/Hans-Jonger Aigner/Ulrich Scheuerle/Markus Stefaner,CFC Legislation-Domestic Provisions, “Tax Treaties and EC Law “,Kluwer Law International, 2006

<sup>33</sup> <http://www.oecd.org/tax/aggressive/discussion-draft-beps-action-3-strengthening-CFC-rules.pdf>

<sup>34</sup> See UK rules, German rules.

<sup>35</sup> <http://www.oecd.org/tax/aggressive/discussion-draft-beps-action-3-strengthening-CFC-rules.pdf>

<sup>36</sup> For instance the German CFC rules demand any level of taxation below 25% as low taxation. On the contrary , Finland issues a list of tax treaty countries .

whether CFC rules are imposed or not and the amount of tax that should be paid according to the applicable law.

On the other hand, in the offshore legislation there is not a precise definition as far as the applicable tax and the operation under which a foreign company could be characterized as an offshore. The concept of “*particularly advantageous treatment*” is not accurate and clear. A lower tax rate could justify the characterization and the taxation of a company as an offshore company due to an advantageous treatment.

Last but not least, the legal consequence of using an offshore company for tax avoidance purposes has nothing to do with legal consequences of using a CFC<sup>37</sup>. Greek measures only prohibit the use of offshore companies in order to buy goods or receive services from them. Also, the annual tax is 15% on the value of immovable property situated in Greece and owned by foreign companies which have no activity in the country of domicile<sup>38</sup>. They do not have any direct effect with tax avoidance. On the other hand according to CFC legislation a foreign corporation ceases to operate at all towards the domestic tax authorities and the provisions of CFC legislation are applicable (in order to have its dividends taxed). CFC legislation creates an effective legal anti-avoidance framework and poses impediments to international tax avoidance<sup>39</sup>. As a consequence, while there is a different naming of these foreign companies, the application of CFC legislation should be determined according to the aim of the company to shift income to jurisdictions that do not impose tax or impose tax at low rates. The adaptation of the Model Double Taxation Convention on Income and Capital (CFC legislation) from all Contracting Parties has a great impact to the creation of a standard package of tax, financial and banking regulations in order to cease the abuse of legal mismatches which derived from the interaction of the various jurisdictions and different interpretation of the domestic

---

<sup>37</sup> <https://books.google.gr/books?id=v1bzwdeFZMIC&pg=PA206&lpg=PA206&dq=michael+lang+Cfc+law&source=bl&ots=2xJHXlvNgU&sig=yw7r6D1CtJwR9yu-HxbDt9glz78&hl=el&sa=X&ved=0ahUKEwjOOJGg27jKAhWBPRoKHY2mAOSQ6AEIKDAB#v=onepage&q=michael%20lang%20Cfc%20law&f=false>

<sup>38</sup> <http://www.taxheaven.gr/laws/circular/view/id/15882>

<sup>39</sup> <https://books.google.gr/books?id=v1bzwdeFZMIC&pg=PA297&lpg=PA297&dq=michael+lang+Cfc+law+greece&source=bl&ots=2xJHXlwGaT&sig=HPp4wvLQwbIIJlymegddNQ8iRVM&hl=el&sa=X&ved=0ahUKEwjIzviR3LjKAhWCOxoKHX5NDH4Q6AEIJjAB#v=onepage&q=michael%20lang%20Cfc%20law%20greece&f=false>

lax. But in the Model Convention the notion of Controlled Foreign Corporation is clarified and the scope of CFC legislation is specific and common in every jurisdiction.

## CHAPTER 2

### AN OFFSHORE COMPANY

#### I. INCENTIVES FOR ESTABLISHING AN OFFSHORE COMPANY

Legislative power is at the core of countries' sovereignty. Every State configures its domestic tax law in order to increase its income revenue and to be healthier. Some States used to give incentives to foreign companies to expand in their territory, in order to foster foreign investments. Legislative provisions and tax systems which furnish advantages to foreign companies incentivize investments via the creation of the so-called "offshore companies".

The advantages that offered the establishing and the operation of an offshore company are various. Firstly, the establishment of an offshore company is a quick, simple and not extravagant procedure, without many formalities and bureaucratic demands.

Furthermore, it is provided complete anonymity to the administrators<sup>40</sup> and shareholders of this company. Offshore company could exercise different activities depending on the different company legislations that are applied in the state of establishment (tax haven).

The avoidance of taxes constitutes the root cause of development of offshore companies. These companies are exempt from inheritance tax, donation tax, transfer and parental benefit in property cases, the tax interest on deposits. Generally, the tax rates are significantly lower in the host State than these in the state of parent's company.

Furthermore, the possibility to invest personal property in offshore companies guarantee the non-satisfaction of the personal creditors and also completely ensure

---

<sup>40</sup> Banks, companies, trusts, or other financial actors in the tax havens are allowed to accept money from basically anywhere without reporting it to the authorities in the country where it originates or from which it is controlled. In some cases, it is actually illegal to disclose that information, but in many places, it is simply because the banks or other entities aren't required to disclose it and there is no mechanism to force them to do so.

the preservation of invested money. While banking secrecy in offshore centers protects the entrepreneurs and prevents controls<sup>41</sup>.

The possibility of transferring profits from countries with high tax rates in jurisdictions with low or no taxation and the absence of exchange restrictions are defining criteria for establishing an offshore company<sup>42</sup>.

In addition the non-application of labor and social security home legislation plays a major role for business entities that intend to operate and employ staff abroad. The creation of an offshore company, often relieves the operator from any liability to pay social security contributions or other employer contributions<sup>43</sup>.

Because of the various motivations and advantages that offshore companies provided, they have rapidly blossomed and is estimated that half of international financial transactions are directly or indirectly connected with offshore companies and International Offshore Financial Center<sup>44</sup> (IOFC). Despite the benefits that the owners derive from, we should not forget that offshore companies aim at tax avoidance and skew developments in the world economy.

---

<sup>41</sup> Banks in tax havens accept deposits without asking questions, shuffling the money around a bit, and then sending it to wherever they'd like to spend it or to wherever they'd like to receive it.

<sup>42</sup> "An Introduction to Transfer Pricing"

[http://www.un.org/esa/ffd/tax/2011\\_TP/TP\\_Chapter1\\_Introduction.pdf](http://www.un.org/esa/ffd/tax/2011_TP/TP_Chapter1_Introduction.pdf)

<sup>43</sup> [https://el.wikipedia.org/wiki/%CE%A5%CF%80%CE%B5%CF%81%CE%AC%CE%BA%CF%84%CE%B9%CE%B1\\_%CE%B5%CF%84%CE%B1%CE%B9%CF%81%CE%B5%CE%AF%CE%B1](https://el.wikipedia.org/wiki/%CE%A5%CF%80%CE%B5%CF%81%CE%AC%CE%BA%CF%84%CE%B9%CE%B1_%CE%B5%CF%84%CE%B1%CE%B9%CF%81%CE%B5%CE%AF%CE%B1)

<sup>44</sup> "TRAINING MANUAL ON ANTI-MONEY LAUNDERING AND COUNTERING THE FINANCING OF TERRORISM", European Union, <http://www.onpcsb.ro/pdf/AM-CTF%20TRAINING%20MANUAL.pdf>

## II. FORMS OF OFFSHORE COMPANIES

Following the analysis detailed above on the motivations and the benefits from the establishment and operation of an offshore company, the activities which an offshore company can carry out constitute an important topic that will be analyzed in this chapter. The variety of activities that can be undertaken by an offshore company facilitate their expansion in many industries. Therefore the establishment of an inclusive legal framework that regulates all their activities is a quite difficult task. Offshore companies are used for a variety of commercial and private purposes. Depending on the purpose that an offshore company serves, there are several different types, some of which will be examined below.

*Holding Companies*: The use of offshore holding companies which are established in offshore centers is a method of international tax planning for the financing of offshore activities. All the activities are concentrated in an International Organization Financial Company (IOFC). It acts as Liquidator Company for profits from activities in third countries, accumulates profits, reinvestment of profits and general tax planning activities<sup>45</sup> and also creates an extensive business network through other affiliated companies. A holding company is founded in the appropriate IOFC in order to gather the profits from foreign subsidiaries, instead of being return to the parent company. IOFC provides tax benefits, such as the deferral of tax in dividends, absence of exchange controls.

*Companies Financial Services*<sup>46</sup>: Financial services company, which is located in an offshore center operates as a diversion channel loans in a foreign subsidiary. Profits are moved from the foreign subsidiary (borrower), which is subject to a jurisdiction with high taxation rates, to the off shore's company jurisdiction with low taxes. Their role is to provide loans to foreign subsidiaries, which pay them back burdened by the interest. The country of domicile of its foreign subsidiary imposes tax on these interest due, which is low to zero so as to accomplished capital flow from one country to an offshore financial center, through the payment of interest and low

---

<sup>45</sup> P.Douvis "Offshore Activities", Athens 2008 p.59

<sup>46</sup> P.Douvis "Offshore Activities ", Athens 2008p.62

withholding tax rate applicable to them. If these funds remain in the foreign subsidiary would be taxed in the country as profits with high tax rate or a higher dividend withholding tax in relation to that imposed on loan interest. The movement of capital in offshore centers, reduces the overall gains that will be taxed at the headquarters of the subsidiary or dividends that will be taxed through the distribution of profits. Therefore, the restriction of the corresponding tax base is achieved and consequently avoidance of a significant amount of tax for the country hosting the borrowing company.

Trading Companies<sup>47</sup>: These companies are mainly active in import and export trade. In this case, a trading company based in a tax haven, import or export, undertakes to deliver the product by the supplier directly to the customer. The commodity does not sent to offshore financial center and thereby avoid duplication of import duties. In contrast, the commercial enterprise buys products or services from a dealer and resell immediately in a foreign subsidiary. The sales' price is considerably higher than the market price, since the ultimate purpose of the transaction is to transfer its profits to offshore financial center, where the applicable tax system is more favorable than this that would be applied in the country of the subsidiary.

Shipping Companies<sup>48</sup>: A large number of offshore centers have adopted favorable regulations for companies engaged in shipping, including chartering and boat rentals. The right to charter boats is reserved and the company does not have to have a permanent establishment in the IOFC. Profits from the operation of ships are taxed at the special low tax rate of offshore financial center and avoid the high taxes that would be imposed by the country of the shipping company if these company carries out the same activities.

Investment Companies<sup>49</sup>: Investment Companies are established in offshore financial centers and regards the investment of capital that has accumulated in them. The aim of these companies is to pay the lowest possible tax or no tax at all for revenue or interest accruing from the various investments. For this reason, the

---

<sup>47</sup> P.Douvis "Offshore Activities" Athens 2008,p.80

<sup>48</sup> P.Douvis "Offshore Activities" Athens 2008, p.78

<sup>49</sup> P.Douvis "Offshore Activities" Athens 2008, p.87-89

invested capital either is invested in countries that have signed a favorable tax treaty with offshore financial center, or are submitted in bonds or deposit in banks. Other types of investments that can be made are: shares, Swiss annuities, collective investments, unit trusts-mutual funds (mutual funds), savings schemes, umbrella funds, investment trusts, hedge funds, eurobonds.

Other activities that are commonly be used by offshore companies are: Banking Companies, Representation Companies, Trusts, Rights Companies authorizations, Insurance Companies, Real Estate, Leasing Companies, Providers Administration Companies.

## CHAPTER 3

### LEGISLATIVE FRAMEWORK AGAINST TAX AVOIDANCE

#### I.EUROPEAN REGULATORY FRAMEWORK

Taxation always constitutes an area of national sovereignty (direct taxation). As a consequence there are a wide range of different tax systems which sometimes constitute the root of international problems such as tax avoidance and tax evasion. These different tax systems between States facilitate the operation of tax havens<sup>50</sup> and preferential treatment of offshore companies located in their territory against companies seated in different States. Moreover, there are also various tax systems at a European level, despite the establishment of the Economic and Monetary Union (EMU). Different tax systems are applicable in every Member State because each of them exercises its authority to impose tax independently, solely by ensuring that it complies with the fundamental principles of the EU included in art. 26 TFEU. As a result, legislative initiatives taken by the EU institutions, which aim to minimize the discretion of Member States on the creation of favorable tax regimes (i.e. which foster the operation of offshore companies) and to combat the consequent tax avoidance, have harmonized the tax systems of Member States and facilitated the cooperation and mutual assistance among them on taxation issues. The EU institutions, exercising their legal jurisdiction stems from art.114-117 TFEU, issue directives in order to eliminate tax avoidance and define a common tax regime.

These directives, which will be examined bellow, aim to harmonize different European tax systems and to create a common tax base in which the tax-rate will be calculated. Unequivocally, a uniform tax system at a European level which imposes equal taxes in every Member State under the same circumstances and regulates tax disputes between Member States in a uniform manner facilitates the handling of tax issues at a global level. The differences between tax systems will be eliminated if Member States adopt these directives and if the EU establishes a uniform tax system for both corporations which are domiciled in an EU Member State and foreign corporations. The following legislative reforms are not directly connected with

---

<sup>50</sup>K.Finokaliwtis/N.Barbas, “ Public Finance “, Athes-Thessaloniki P.2001 p.134

offshore companies and do not directly affect direct taxation, but they aim to resolve certain tax issues at a European level and create an anti-avoidance framework by intra-EU mutual cooperation among Member States.

*Directive 90/434EC which was amended by Directive 2005/19/EC and the last codification was by Directive 2009/133/EC<sup>51</sup>.*

All these directives, starting from the first, which published at 23 of July in 1990, are about the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States.

Initially, the Directive 90/434 / EC attempted to eliminate the unfavorable treatment that a Member State reserved to specific corporate transformations, when they were carried across its borders, compared with the treatment to similar transformations when they took place in its territory.

An important regulation included in art 4 par.1 of Directive according to which capital gains are not being taxed and are calculated by reference to the difference between the real values of the assets and liabilities transferred and their values for tax purposes. Moreover, the receiving company computes any new depreciation and any gains or losses in respect of the assets and liabilities transferred according to the rules that would have applied to the transferring company or companies if the merger, division or partial division had not taken place (art 4 par 3).

Beyond the removal of fiscal restrictions Dir. 2009/133EC introduces an innovation by giving to Member States the possibility to refuse the application of this Directive where the merger, division, transfer of assets, exchange of shares or transfer of the registered office of an SE or SCE has as its objective tax evasion or avoidance (art.15 par.1a)<sup>52</sup>.

This directive provides for the uniform tax treatment of specific corporate transformations – regardless of the Member State at which they take place – and for the transfer of the registered office of an SE or SCE, between Member States. As a result, companies have less incentives to establish offshore companies in tax-havens

---

51 [http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:310:0034:0046:EL:PDF\(Dir. 2009/133 EC\)](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:310:0034:0046:EL:PDF(Dir. 2009/133 EC))  
52 <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32009L0133&from=EN>

(within the EU), as the tax system that is applied in the corporate transformation or in the transfer of a corporation's registered office is common in every Member State (to the extent that it transposes this Directive in its domestic law).

Directive 90/435/EC, as amended by Directives 2003/123/EC and 2006/98/EC and recasted by Directive 2011/96/EU<sup>53</sup>.

The aforementioned Directives referred to the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States. Tax laws of various jurisdictions interact with each other and harmful tax competition is fostering. As a result economic activity is restricted and distorted. Especially, the objective of this Directive is to exempt dividends and other profit distributions paid by subsidiary companies to their parent companies from withholding taxes and to eliminate double taxation of such income at the level of the parent company<sup>54</sup>.

In the annex is included all the legal forms of companies that falls under the provision of this Directive and also the prerequisites to be fulfilled in order to get a company the status of parent company (art 3) . It is also mentioned two different ways of imposing tax on the parent company from dividends received from its subsidiary. In the first case, the Member State of the parent company refrain from taxing distributed profits (art.4 par.1a, exemption method). Alternatively, it could tax such profits, while authorising the parent company to deduct from the amount of tax due that fraction of the corporation tax related to those profits that paid by the subsidiary (art.4 par 1b, the tax credit method). Moreover, pursuant to art.5 "*Profits which a subsidiary distributes to its parent company shall be exempt from withholding tax*" and to art.6 "*The Member State of a parent company may not charge withholding tax on the profits which such a company receives from a subsidiary.*" Mainly, under these provisions it is secured a fiscal neutrality. The profits which a subsidiary distributes to its parent company are exempt from withholding tax in order to allow enterprises to adapt the requirements of internal market to increase their productivity and to improve their competitive at international level.

---

<sup>53</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:345:0008:0016:en:PDF>

<sup>54</sup> <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32011L0096&from=EN>

This Directive aims to eliminate double taxation on income at the level of the parent company and to eliminate tax avoidance by imposing a common tax system for profits paid by a subsidiary. Its goal is to allocate taxing powers between the State of parent company and the State of subsidiary and to reform the imposing tax according a uniform tax regime.

Directive 2003/48/EC as amended by Directives 2006/98/EC and 2014/48/EU<sup>55</sup>.

These directives intend to ensure effective taxation of savings income in the form of cross-border interest payments. These payments are generally included in the taxable income of resident individuals, but Member States cannot sufficiently impose interest on savings which are received in one EU country by individuals who are resident and taxpayers in another EU country in accordance with the laws of the latter country. As a result tax avoidance was occurred in the level of taxation of savings interest received from residents of one Member State in another Member State than that of their residence<sup>56</sup>, so State residence has no competence to tax the saving income. Differences between national tax systems lead to arbitrary discrimination, by providing favorable regulations on taxation of savings interest and consequently creating 'tax havens', and indirectly impede the free movement of capital.

The scope of the Directive concerning the taxation of savings income in the form of interest which is paid in one Member State by beneficial owners who are residents in another Member State. Such earnings are taxed in the country where the beneficial owner has his domicile and is taxpayer (article 1 paragraph 1). Where the beneficial owner is resident in a Member State other than that in which the paying agent is established, the minimum amount of information should be reported by the paying agent to the competent authority of its Member State of establishment (article 8). In turn, the competent authority of the Member State where the economic operator is established shall communicate the information to the competent authority of another Member State where the entity or legal arrangement has its place of effective management.(art.9). This Directive aims to deter tax avoidance and tax

---

<sup>55</sup> <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32014L0048&from=EN>

<sup>56</sup> K.Finokaliotis,"Tax Law"., Athens-Thessaloniki, 2005 p.221

evasion which occurs through saving money in different Member State from residence State in order to be taxed with lower tax rate and to pose impediments to the expansion of tax-havens. A coherent tax system is to be applied in all savings from income in order limit the discretion of Member States to impose different tax rates on savings and to induce tax havens.

Other legislative reforms that should be pinpointed are : Directives 77/799/EC, as amended by Directives 2003/9/EC, 2004/56/EC - repealed by Directive 2011/16/EU as amended by Directive 2014/107/EU which has been adopted by Member States and incorporated in their domestic law. The goal of these directives is to establish a mutual assistance scheme for Member States on direct taxation and the taxation of insurance premiums, with a view to eliminating international tax evasion and avoidance. Via these Directives the European Union has enhanced collaboration between the Member States' tax authorities and has facilitated the exchange of information that is necessitated for the proper assessment of taxes both on income and capital. The last amending, according to Directive 2014/107/EU, aim to deal with the challenge posed by cross-border tax fraud and tax evasion which have increased considerably in recent years<sup>57</sup>. Because of the reduction of national tax revenues, due to unreported and untaxed income, the efficiency and effectiveness of tax collection is of primary importance. For this reason, Directive 2014/107/EU is published in December, 2014 containing an Action Plan to bolster the measures taken against tax fraud and tax evasion, stressing the need to advance the automatic exchange of information as the future European and international standard for transparency and exchange of information on taxation issues<sup>58</sup>. This revised directive broadens the scope for the automatic exchange of tax information and accommodates issues relating to interest, dividends, and other income, as well as account balances and sales proceeds from financial assets. The “automatic exchange” means the systematic communication of predefined information on residents in other Member States to the relevant Member State of residence, without prior request as it is mentioned in art.1 of Dir.2014/107/EU. The Directive ensures that the EU standard for exchange of information on request is aligned to

---

<sup>57</sup> <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32014L0107&from=EN>

<sup>58</sup> <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32014L0107&from=EN>

international standards by providing that Member States can no longer refuse to supply information solely because this information is held by a bank or other type of financial institution<sup>59</sup>. The Directive also includes deadlines and feedback by the Member States that have received information and establishes a regulatory committee, which is competent for implementing the technical aspects of the Directive.

The reference to the aforementioned directives give us a picture of the European tax system which should be uniform and coherent in order to lay the foundation for a mutual cooperation and a common solution to tax issues, such tax avoidance and tax evasion. The incorporation of the directives in the domestic law of every Member State aims to assign the taxing powers and to avoid the risk of double taxation. Pursuant to these Directives the national revenues are taxed from the competent jurisdictions and harmful tax competition is struggled over. The cooperation and the regulation of tax issues in European level facilitate the treatment of these issues in a wider range, across the globe. A mutual effort to trample down tax issues and a common regulatory solution in EU area constitute prerequisite and a key pillar in creating a coherent international tax regime.

---

<sup>59</sup> [http://ec.europa.eu/taxation\\_customs/taxation/tax\\_cooperation/mutual\\_assistance/direct\\_tax\\_directive/index\\_en.htm](http://ec.europa.eu/taxation_customs/taxation/tax_cooperation/mutual_assistance/direct_tax_directive/index_en.htm)

## II.CFC LEGISLATION

As it is aforementioned OECD is the one and only international economic organization which deals with fiscal reforms and promotes a single tax policy for tax avoidance. The goal of Model Tax Convention on Income and Capital is not exclusively the elimination of double taxation but also the handling of tax issues such as tax avoidance and the improvement of tax practices internationally.<sup>60</sup> This Model Convention contains legislative provisions for the taxation of Controlled Foreign Corporations, which cease completely their operations as regard the domestic tax authorities and thus the provisions of the CFC legislation are exclusively applicable to them. CFC rules are the only harmonizing legal text that regulates in a common way the operation and the taxation of income and capital imposed on foreign corporations and settle on a uniform basis in international judicial double taxation.

Sometimes the interpretation of the legal text is difficult and ambiguous so the ECJ undertakes to interpret these rules and to clarify some complex terms. One basic issue is the scope of CFC legislation. CFC rules are applicable to corporations not only if they fulfill the prerequisites in order to be characterized as CFCs<sup>61</sup>, but the application of this tax system is restricted to some of CFCs' transactions. The ECJ specifies the type of arrangements in which CFC legislation is implemented. The European Court of Justice<sup>62</sup> has referred that CFC rules which are applied to cross-border transactions must "specifically target to wholly artificial arrangements which do not reflect economic reality and whose only purpose would be to obtain a tax advantage<sup>63</sup>"

However, the application of CFC rules in arrangements that are not wholly artificial could be justified provided that they aim to prevent tax avoidance.

---

<sup>60</sup> <http://www.oecd.org/berlin/publikationen/43324465.pdf>

<sup>61</sup> CFC is a corporate entity that is registered and conducts business in a different jurisdiction or country than the residency of the controlling owners in order to shift income either from parent jurisdiction or other tax jurisdictions

<sup>62</sup> See. Cadbury Schweppes plc and Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue, C- 196/04.

<sup>63</sup> See. Haribo Lakritzen Hans Riegel BetriebsgmbH and Österreichische Salinen AG v. Finanzamt Linz, Joined Cases C-436/08

For instance, in Thin Cap Group Litigation the ECJ stated that, in determining whether thin cap legislation was justified by the need to prevent abusive practices, the Court should determine “whether the transaction in question represents, in whole or in part, a purely artificial arrangement, the essential purpose of which is to circumvent the tax legislation of that Member State<sup>65</sup>”. Accordingly, CFC legislation which focuses on not completely virtual income of a CFC could be rationalized, if the transaction which produces the taxable income is partially virtual.

On the contrary, the ECJ has suggested that the prevention of tax avoidance does not consist the one and only reason to justify the expansion of tax provisions to partially artificial arrangements. In both *Société de Gestion Industrielle*<sup>66</sup> and *Oy AA*<sup>67</sup> cases, for example, the ECJ stated that the application of CFC rules could be justified by the need to ensure a balanced-equal distribution of taxing powers across Member States notwithstanding that they are not restricted to wholly artificial transactions. So the assessment of every transaction, whether it is artificial or not and whether CFC rule are applicable or not, is a distinct case and made separately from the others.

The OECD Model Tax Convention on Income and Capital contains provisions that regulate the operation and the taxation of Controlled Foreign Corporation which would be explained below in order to be understood the role and the need of application of this Model Law.

The first articles (Articles 1-5), give the necessary definitions for further understanding of its provisions, then is described the extent of the right of each Member State to impose taxes on income class and capital (Articles 6-22) and finally,

---

<sup>64</sup> <http://www.oecd.org/tax/aggressive/discussion-draft-beps-action-3-strengthening-CFC-rules.pdf>

<sup>65</sup> On the contrary, the ECJ has suggested that tax provisions of a Member State may not be restricted to wholly artificial arrangements if they are justified by a reason other than the need to prevent tax avoidance. In both *Société de Gestion*

<sup>66</sup> See. *Société de Gestion Industrielle (SGI) v. Belgian State*, C-311/08 (21 January 2010)

<sup>67</sup> See. *Oy AA*, C-231/05 (18 July 2007) (holding that the freedom of establishment did not prevent Member States from limiting interest deductions for intra-group transfers to payments made to resident companies)

is identified the methods that is used for the avoidance of double taxation (Articles 23A, 23B).

Especially, the Convention applies to all persons who are residents<sup>68</sup> of one or both of the Contracting State (art.1). Article 2 concerns the objective scope of Model Convention which includes the taxes imposed ,regardless of the competent tax authority , on income and capital . The notion of “person”, “company”, “national”, and “business” are explained in art.3 of Model Double Taxation Convention on Income and Capital so as the term of “resident” and “permanent establishment<sup>69</sup>” which are defined in detail in art.4 and 5 correspondingly.

Articles 6-21 regulate the taxation of different forms of income. For instance, art.7 OECD mentions that “the profits of an enterprise of a Contracting State shall be taxable only in that State through a Permanent Establishment situated therein<sup>70</sup>”.

Neither the domestic law of the State of residence nor the one of the source of State overrides the Permanent Establishment’s. This method of taxation is called “piercing the veil approach” and its purpose is to restrict the taxing power of one Contracting State on the business profits of enterprises of other Contracting State<sup>71</sup>. The Contracting State of the permanent establishment has exclusive taxing right to the undistributed profits in contrast with the wider discretion that art.7 (2) provides to the Contracting Parties. Pursuant to art.7(2) an enterprise carries on business in the other State through a permanent establishment situated therein and the profits that attributable to the permanent establishment may be taxed by that other State (according to art23A-B).

Art.10 of Model Double Taxation Convention on Income and Capital concerns the imposition of tax on dividends by analyzing the deemed-divident approach<sup>72</sup>. Neither the State of beneficiary’s residence nor the State of which the company pays the dividends has exclusively the tax right. According to article 10(2) not only the source

---

<sup>68</sup>The notion of resident depends on the domestic law.

<sup>69</sup>Which is a fixed place of business through which the business of an enterprise is wholly or partly carried on, according to art.5 OECD

<sup>70</sup><http://www.oecd.org/ctp/treaties/2014-model-tax-convention-articles.pdf>

<sup>71</sup>Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions “, 4<sup>th</sup> Edition, Volume 1, Kluwer Law International, 2015 p.480

<sup>72</sup> Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions “, 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015 p.398

State is allowed to tax dividends paid by a resident company but also the residence State. The extent of such taxation is restricted by reference to a percentage rate of the gross amount of such dividends, if the payee of the dividend is a resident of that other Contracting State. A low tax rate of 5% is explicitly applicable on dividends which are paid by a subsidiary to its parent company. In order to avoid recurrent taxation and to give incentives to international investments payments of profits by the subsidiary to the foreign parent is taxed less heavily if a company of a State has a stake of almost 25% in a company headquartered in a different State. A high rate of tax is capped at 15% of the gross amount of the dividends in all other cases<sup>73</sup>.

The term of dividends mainly refers to distributions by companies according to the article 3 par.1b. Therefore the definition relates to distributions of profits the title to which constituted by shares, that is holding by company limited by shares<sup>74</sup>. As it is defined in art. 10 par.3 OECD dividends are “income from “jouissance” shares or “jouissance” rights, mining shares, founders’ shares or other rights participating in profits...” which could be taxed both by the Contracting State of the residents who take the dividends and by the State in which the company paying the dividends. As per the provisions of Art 10(4), in the State of source the dividends are taxable as part of profits of the permanent establishment there owned by the beneficial owner-resident in a different State if they are payable on holdings that are part of the assets of the permanent establishment or are connected with that establishment<sup>75</sup>. In this occasion, par. 4 removes any limitations set on the State of source of the dividends by the provisions of Article 10. Paragraph 5 of article 10 rules out the extraterritorial taxation of dividends, deals only with dividends which derived from a company domiciled in a Contracting State but paid in a resident from a different State.

---

<sup>73</sup> “Model Double Taxation Convention between Developed and Developing Countries” United Nations, [http://www.un.org/esa/ffd/documents/UN\\_Model\\_2011\\_Update.pdf](http://www.un.org/esa/ffd/documents/UN_Model_2011_Update.pdf)

<sup>74</sup> Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions”, 4<sup>th</sup> Edition, Volume 1, Kluwer Law International, 2015 p.786

<sup>75</sup> <http://www.oecd.org/ctp/treaties/2014-model-tax-convention-articles.pdf>

<sup>76</sup> <http://www.oecd.org/ctp/treaties/2014-model-tax-convention-articles.pdf>

According to art.11 interest shall be taxable either in source State, where it is concluded the loan, at the rate of 10% of gross amount of the interest, or in the State of the beneficial owner.

Art. 12 defines that Royalties are taxed in the State of beneficial owner. The articles below refer to the taxation of capital gains (art.13), income from employment (art.14), directors fees (art. 16) and pensions (art.18).

Art.22 constitutes the basis for the tax avoidance of double taxation of capital<sup>77</sup>.The notion of “capital” which is explained in art.2 OECD comprises both taxes on the total capital of a person and taxes on elements of the person’s capital. Taxation of immovable sources is primarily assigned to the situs State only if it situated in the other Contracting State. The residence State is not excluded from taxation provided that there is no risk of double taxation and articles 23A-B are applicable.

Articles 23A and 23B aim to the creation of a common tax regime in order to eliminate the risk of double taxation and tax avoidance. They deal with the so-called juridical double taxation, where more than one States impose taxes on the same person for the same income or capital earned<sup>78</sup>. These articles’ goal is to regulate the allocation of taxation rights among Contracting States. This allocation may be carried out by cancelling out either the taxation rights of the State of source or of the location of the permanent establishment, or by the State of residence, or, finally, by splitting the taxation rights between the two States.

The purpose of art.23 is to eliminate double taxation by giving two solutions, exemption method (art.23 A) or credit method (art.23B)

---

<sup>77</sup> Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions “, 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p.1567

<sup>78</sup> Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions “, 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p.1586

## Exemption method (art.23A)

The exemption method is based on the concept that the State in which items of income arises or in which items of capital are situated has a better right of taxation and that the exempting State therefore has to give away<sup>80</sup>. In simple words, the income and the capital, which are taxed in source State, shall be excluded from tax base of the State of residence.

This method aims to create equally competitive conditions in the source state among investors from different countries. But exemption method is not concrete enough and it leads to some legislature gaps and misconstructions. For instance, the State could exercise its right to impose tax regardless of the imposition of tax and the application of an exemption method in another Contracting State. The fact that the State of residence does not impose tax on the income or capital which derived from a different State but also the State of source does not impose tax on income, leads to untaxed income or capital and to double non-taxation.

Another crucial issue that arising by adopting the exemption method is the treatment of foreign losses. The wording of art.23A(1) OECD which states that a Contracting State “shall exempt...from tax” give a wide discretion to Contracting States in order to choose the amount and the kind of the tax that would exempt. The levy of the tax on the foreign income is prohibited but the residence state does not seem to be prevented from deducting foreign losses<sup>81</sup>. The constitutional law of each Contracting State defines whether such losses are taken into consideration in the domestic territory set off against positive domestic income and if so carried forward or back to future or past assessments periods<sup>82</sup>.

Article 23A (2) OECD constitutes an exception to the general rule provided by the first paragraph. For certain types of income (dividends , interests, royalties) the residence State does not exempt the income but preserves the right to tax it and has to grant a credit for the taxes levied in accordance with the articles 10(2) and

---

<sup>80</sup> [http://www.un.org/esa/ffd/wp-content/uploads/2014/10/10STM\\_CRP16\\_Art23Comments.pdf](http://www.un.org/esa/ffd/wp-content/uploads/2014/10/10STM_CRP16_Art23Comments.pdf)

<sup>81</sup> Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions “, 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p. 1619

<sup>82</sup> A deduction of losses in the residence State in the year the losses are incurred and a deduction in the source State in the following years might lead to double deduction.

11(2). But it presupposes that the exemption method has been agreed upon for all other items of income. The State of residence of the shareholders is allowed to tax dividends arising in the other State, but it has to set it off against its own tax on such dividends that has been collected by the State where the dividends originate at a rate fixed as per art.10(2) OECD<sup>83</sup>. This regime is also applicable when the recipient of the dividends is a parent company receiving dividends from a subsidiary. In this occasion, the tax withheld by the State of the subsidiary – and credited in the State of the parent company – is capped at 5 percent of the gross amount of the dividends, according to the provisions of art. 10(2a).

Article 23A(3) designates the method called “exemption with progression” according to which the residence State preserves the right to take the exempt income into account for calculating the tax rate<sup>84</sup>. Article 23A(3) deals with the “proviso safeguarding progression”<sup>85</sup>, which means that the residence State may take into account such items of income or capital that the treaty exempts from tax in that State when calculating the rate of tax on the income or capital that the treaty allows it to tax. As a result, tax exemption only restricts the tax base for the calculation of the amount of income or capital but not the tax base for the calculation of the tax rate<sup>86</sup>. A “proviso safeguarding progression” shall guarantee that the residence State may tax the remaining income at a rate that is adjusted based on the tax payer’s financial capabilities. If a State applies a progressive tax rate framework, then the tax payer should not seek to avail itself of possible loopholes, by dividing his declared income in two different States. In the residence State, the tax rate is still calculated in association with his overall income.

Moreover, we should pinpoint that the “proviso safeguarding progression” is restricted to income or capital of the resident, which means that the tax rate of the resident should not be calculated according to income earned or capital owned by

---

<sup>83</sup>“BASIC APPROACHES TO TAX TREATY NEGOTIATIONS”

[http://www.un.org/esa/ffd/tax/sixthsession/CRP10\\_Section1.pdf](http://www.un.org/esa/ffd/tax/sixthsession/CRP10_Section1.pdf)

<sup>84</sup><http://www.oecd.org/ctp/treaties/2014-model-tax-convention-articles.pdf>

<sup>85</sup>[http://www00.unibg.it/dati/corsi/65076/70347-franze\\_lecture.pdf](http://www00.unibg.it/dati/corsi/65076/70347-franze_lecture.pdf)

<sup>86</sup>Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions “, 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015 p.1644

other persons. In other words, the identity of the taxable person is required<sup>87</sup>. Also the tax law of the residence State is applicable in order to calculate the exempted income or capital.

According to Art.23 A(4) OECD the residence State is no longer bound by art.23A(1) OECD to exempt income or capital from tax if the other Contracting State applies the tax treaty in a way that it feels prevented from taxing the income that it applies the provision of art, 10 (2) or 11(2) to such income<sup>88</sup>. This provision avoids double-non taxation or a very low taxation as a result of a different interpretation of the treaty provision or in the case of a different evaluation of the facts by the Contracting States<sup>89</sup>.

### **Credit method (art.23B)**

The credit method has been constructed in such a manner as to loosen an excessive burden that appears to be unfair or economically detrimental, by reducing it to the level of taxation of the State giving credit<sup>90</sup>. It increases the tax burden on such income or capital to the level that applies in the residence State (in case it is higher). If the tax burden applicable is lower than that of the State where the income originates, the higher taxation of the source State shall prevail<sup>91</sup>. The Credit method ensures the uniform treatment by the residence State of all capital investments, whether made at home or abroad, and accordingly shelters capital export neutrality<sup>92</sup>. Also this method tends to favour the State with the higher level of taxation, seeing that lower taxes imposed by the source State rather taxpayer

---

<sup>87</sup> Ekkehari Reimer /Alexander Rust, "Klaus Vogel on Double Taxation Conventions ", 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p.1647

<sup>88</sup> <http://www.oecd.org/ctp/treaties/2014-model-tax-convention-articles.pdf>

<sup>89</sup> Ekkehari Reimer /Alexander Rust, "Klaus Vogel on Double Taxation Conventions ", 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p<sup>89</sup> p.1652-5

<sup>90</sup> See Vogel, K, Intertax 216,393 et seq. (1988)

<sup>91</sup> [https://books.google.gr/books?id=4jZ1z4JnvAAC&pg=PA103&lpg=PA103&dq=Credit+method+\(art.23B\)&source=bl&ots=zO-VMmPP4w&sig=9U5uO8bK94-5PyMaphFsehyvaJ4&hl=el&sa=X&ved=0ahUKEwi65NjvqpjKAhXDVRQKHb\\_fA0cQ6AEILTAC#v=onepage&q=Credit%20method%20\(art.23B\)&f=false](https://books.google.gr/books?id=4jZ1z4JnvAAC&pg=PA103&lpg=PA103&dq=Credit+method+(art.23B)&source=bl&ots=zO-VMmPP4w&sig=9U5uO8bK94-5PyMaphFsehyvaJ4&hl=el&sa=X&ved=0ahUKEwi65NjvqpjKAhXDVRQKHb_fA0cQ6AEILTAC#v=onepage&q=Credit%20method%20(art.23B)&f=false)

<sup>92</sup> [https://books.google.gr/books?id=NNuRoFV5kxkC&pg=PA55&lpg=PA55&dq=Credit+method+\(art.23B\)&source=bl&ots=3Rpbi-vXSD&sig=Pmnbmo8pPTJsAaZZLSJBQDUwQQ&hl=el&sa=X&ved=0ahUKEwi65NjvqpjKAhXDVRQKHb\\_fA0cQ6AEIMTAD#v=onepage&q=Credit%20method%20\(art.23B\)&f=false](https://books.google.gr/books?id=NNuRoFV5kxkC&pg=PA55&lpg=PA55&dq=Credit+method+(art.23B)&source=bl&ots=3Rpbi-vXSD&sig=Pmnbmo8pPTJsAaZZLSJBQDUwQQ&hl=el&sa=X&ved=0ahUKEwi65NjvqpjKAhXDVRQKHb_fA0cQ6AEIMTAD#v=onepage&q=Credit%20method%20(art.23B)&f=false)

benefit the residence State. That constitutes the main reason that developing countries give priority to applying the credit method<sup>93</sup>.

Article 23B (1) mentions two methods of credit, full credit and the ordinary credit. According to full credit method, the residence State allows a deduction from its own tax on the income or capital of its resident an amount equal to the tax paid in the other State on the income derived from or the capital owned in, that other State, but the deduction is restricted to the appropriate proportion of its own tax.<sup>94</sup> Article 23B does not described in detailed the computing and operation of the credit and as a consequence the calculation of the income or capital tax is made according to the domestic legislation<sup>95</sup>. But there are some basic rules in order to calculate the credit on the income tax which should be applied in every jurisdiction and thus they will be explained bellow. Firstly, credit is allowed for income tax only against income tax and for capital tax only against capital tax<sup>96</sup>. Moreover, credit allowed shall be equal to the tax paid. The tax paid in violation of a tax treaty cannot be credited<sup>97</sup>. For instance, if the resident pays more tax than he was obliged, or if the legislation of the other Contracting State grants reduction only the amount which was actually paid after the reduction shall be deducted as a credit. Also the tax liability must be final – to the extent the taxpayer can claim a refund a credit is excluded<sup>98</sup>.

The person entitled to claim the credit is the person who was liable to pay the foreign tax and who himself paid it or arranged for some third party to pay in his head<sup>99</sup> (direct credit). However, where a treaty or domestic law expressly provides for it an indirect credit for taxes paid by a foreign subsidiary against taxes payable by its domestic parent company is allowed.

---

<sup>93</sup>Widmer, M., 22 RIW/AWD 569 (1976), see also the explanation concerning the tax sparing credit infra m.no 62 et. seq

<sup>94</sup><http://www.oecd.org/ctp/treaties/2014-model-tax-convention-articles.pdf>

<sup>95</sup>See in that regard , e.g. , Belgian Hof van Cassatie of 22 January 2010, F08.01000.F :DTC/Belgium/Czech Republic

<sup>96</sup>Ekkehari Reimer /Alexander Rust, "Klaus Vogel on Double Taxation Conventions ", 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p. 1605

<sup>97</sup>Ekkehari Reimer /Alexander Rust, "Klaus Vogel on Double Taxation Conventions ", 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p.1629

<sup>98</sup>Wassermeyer, F. in : Wassermeyer, Art.23A OECD at.m.no 95.

<sup>99</sup>[https://books.google.gr/books?id=4jZ1z4JnvAAC&pg=PA103&lpg=PA103&dq=Credit+method+\(art.23B\)&source=bl&ots=zO-VMmPP4w&sig=9U5uO8bK94-5PyMaphFsehyvaJ4&hl=el&sa=X&ved=0ahUKEwi65NjvqpjKAhXDVRQKHb\\_fA0cQ6AEILTAC#v=onepage&q=Credit%20method%20\(art.23B\)&f=false](https://books.google.gr/books?id=4jZ1z4JnvAAC&pg=PA103&lpg=PA103&dq=Credit+method+(art.23B)&source=bl&ots=zO-VMmPP4w&sig=9U5uO8bK94-5PyMaphFsehyvaJ4&hl=el&sa=X&ved=0ahUKEwi65NjvqpjKAhXDVRQKHb_fA0cQ6AEILTAC#v=onepage&q=Credit%20method%20(art.23B)&f=false)

Article 23B(2) is similar to 23A(3) according to which the residence State may take income that it has to exempt under one of the distributive rules into account for calculating the tax rate. The above explanation of art.23A(3) also applies in art. 23B(2). According to " proviso safeguarding progression" the resident State may take the exempt income or capital into account for calculating the tax rate on the remaining income or capital. Art 23B(2) relates to exemption by reason of a complete distributive rule only<sup>100</sup>.

In addition there are some other important provisions that is included in Model Convention in art.24,25,26,27 OECD. According to art.24 OECD discrimination is prohibited and the application of national law of the Contracting State which provides worse or different settings to non-nationals, while they are under the same conditions with the nationals, is precluded. The establishing of a mutual agreement procedure for elimination double taxation and for a common interpretation of the convention as well as the exchange of information between the tax authorities of the Contracting States are defined correspondingly in art.25 and 26 OECD in order to foster the application of the Model Convention.

By explaining above the main provision of Model Convention it is understood that OECD by publishing this legal text aims to create a coherent international tax regime. This Model Convention assigns tax powers and fosters the mutual cooperation in tax regime. Via a common tax system the spread of tax havens is discouraged and problems presented by countries' tax sovereignty are eliminated. The States which have adopted this Model Convention and the aforementioned Directives – at an EU level – have established an efficient legal framework with a view to reducing instances of tax avoidance and creating defensive mechanisms against international tax issues. The institution and application of a common tax scheme that regulates not only the tax basis for worldwide income, but also the taxation of different types of foreign companies, and which aims at the equal development of anti-avoidance legal frameworks by all States constitutes the only way to combat tax avoidance.

---

<sup>100</sup> Ekkehari Reimer /Alexander Rust, "Klaus Vogel on Double Taxation Conventions ", 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015p .1644

## CHAPTER 4

### CFC APPLICATION

#### I.CFC LEGISLATION IN DIFERENT COUNTRIES

As it is aforementioned CFC legislation is a Model Convention that is adopted by Contracting States and integrated in their domestic legislation. It is not a binding legal text with mandatory force and thus, every Contracting Party adopts some of these provisions and modulates them according to its domestic tax systems and its interests. In European countries sometimes it is followed a common application and interpretation of OECD Model Convention such as the calculation of “low” tax rate, the assessing of the shareholders threshold in order to control of the corporation etc. Some countries have a “black list”<sup>101</sup> of harmful countries, such as Italy, while others exempt listed countries from the CFC rules<sup>102</sup>.

For instance, Germany’s CFC legislation was founded in sections 7-14 of the 1972 Foreign Tax Act (AStG), and was updated by the Annual Tax Act 2010. The CFC rules are applicable if a German resident taxpayer owns more than 50% of a foreign company<sup>103</sup>, and the foreign company receives “passive income”; which is subject to “low tax” at a rate of less than 25%<sup>104</sup>. Germany does not have a black or white list of countries but it follows the deem-dividend approach. German shareholders are being taxed for their CFC income as deemed-dividend, to which exemption and other dividend relief mechanisms are not applicable. Although, CFC income is included in the corporate tax income base<sup>105</sup>. Art.20(1) AStG stipulates the priority of the CFC legislation over tax treaties pinpointing the great importance of the Model Double Taxation Convention on Income and Capital<sup>106</sup>.

---

<sup>101</sup> which includes certain specified EU territories or entities including Malta, Cyprus and Luxembourg .

<sup>102</sup> [http://www.m-i-tax.de/content/Wichtige\\_Links/Alumni\\_Netzwerk/documents/cfcrules\\_000.pdf](http://www.m-i-tax.de/content/Wichtige_Links/Alumni_Netzwerk/documents/cfcrules_000.pdf)

<sup>103</sup> the threshold is reduced to 1% (or less) if the foreign company is engaged in the business of certain financial transactions

<sup>104</sup> [http://www.m-i-tax.de/content/Wichtige\\_Links/Alumni\\_Netzwerk/documents/cfcrules\\_000.pdf](http://www.m-i-tax.de/content/Wichtige_Links/Alumni_Netzwerk/documents/cfcrules_000.pdf)

<sup>105</sup> “Germany:Federal Tax Court Rules CFC income is not subject to trade tax”, Alexander Linn, <http://www.internationaltaxreview.com/Article/3470294/Germany-Federal-Tax-Court-rules-CFC-income-is-not-subject-to-trade-tax.html>

<sup>106</sup> “Business and Taxation Guide to Germany” Praxity, <file:///C:/Users/Toshiba/Downloads/tax%20guide%20-%20germany.pdf>

In Greece, the New Greek Income Tax Code for the first time introduces provisions pertinent to Controlled Foreign Companies (“CFCs”) in art.66 of the Income Tax Code<sup>107</sup>. The conditions to impose tax charges on the undistributed profits of the CFC accrued by the Greek taxpayer are as follows: i) the relevant taxpayer owns directly or indirectly 50% of the shares of the Foreign Company or effectively controls it; ii) the Foreign Company is subject to taxes at the country where it is incorporated at a tax rate which is below 50% of the respective tax rate in Greece – that is less than 13% - or iii) the aforementioned country to be listed as a non-cooperative country and over 50% of the income of the Foreign Company to arise from transactions at which the controlled company is its counterparty. Also in Greece there is a black-list, which includes countries with preferential tax regimes<sup>108</sup>. The legislative framework used for the calculation of the exact tax rate imposed on the undistributed earnings. The undistributed profits of the CFC will be taxed as business income in the hands of the Greek taxpayer<sup>109</sup>

The United Kingdom first introduced profits of CFCs into the UK tax net by the Finance Act 1984 but recently undertaken a complete overhaul of its CFC rules as part of the effort to increase the overall competitiveness of the UK tax regime<sup>110</sup>. Under UK tax law a CFC is any company which is resident outside the UK, subject to tax at a lower<sup>111</sup> level, and is controlled (more than 50%) by UK residents. Some types of companies and income assume derogations from provisions of the CFC rules. The aforementioned derogations aim to identify the extent to which certain types of profits (i.e. trading profits, finance income, etc.) should be treated as potentially taxable in the UK<sup>112</sup>. The said provisions utilise a string of charge gateways to different types of profits in order to flag any profits diverted from the

---

<sup>107</sup> “Income Tax” <http://www.tovima.gr/files/1/2013/07/02/neos.pdf>

<sup>108</sup> <https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-guide-to-cfc-regimes-210214.pdf>

<sup>109</sup> For legal entities the rate is 26% for individuals the rate is 26% up to EUR 50,000 and 33% on the excess.

<sup>110</sup> <http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-guide-to-cfc-regimes-210214.pdf>

<sup>111</sup> [http://www.m-itax.de/content/Wichtige\\_Links/Alumni\\_Netzwerk/documents/cfcrules\\_000.pdf](http://www.m-itax.de/content/Wichtige_Links/Alumni_Netzwerk/documents/cfcrules_000.pdf) the foreign co’s tax rate must amount to at least 22.5%.

<sup>112</sup> [http://www.olswang.com/media/20300344/mxj\\_cfc\\_article.pdf](http://www.olswang.com/media/20300344/mxj_cfc_article.pdf)

UK that will then be apportioned and charged on the relevant UK corporate interest-holders<sup>113</sup>. There are also several entity level exemptions. That is, taking into account the fact that most of the CFCs are being established for purely commercial reasons and, accordingly, it would be inequitably onerous for them to comply with such rules.<sup>114</sup> In case where no exemption is applicable and CFC profits are apportioned to the UK, the payable UK corporation tax is reduced by any apportioned “creditable tax”<sup>115</sup>. The creditable tax is the aggregate of the double tax relief that would be available if the CFC’s chargeable revenue was subject to UK corporation tax.

As the CFC legislation constitute a Model Convention the interpretation and the application could differ in every Contracting Party, providing them the discretion to adjust the model law according to their domestic law and interests. The Model Double Taxation Convention on Income and Capital contains lots of defined terms and a number of targeted anti-avoidance rules, so specific interpretation should be sought in relation to the jurisdiction of each Contracting Party.

---

<sup>113</sup> “Technical briefin New UK CFC rules” <http://www.blickrothenberg.com/getmedia/7051b915-1db7-40d1-8d12-fb1199ad3220/New-UK-CFC-rules.pdf.aspx>

<sup>114</sup> “Controlled Foreign Companies: an overview”  
<https://www.gov.uk/guidance/controlled-foreign-company-an-overview>

<sup>115</sup> <http://www.blickrothenberg.com/getmedia/7051b915-1db7-40d1-8d12-fb1199ad3220/New-UK-CFC-rules.pdf.aspx>

## II. CASE LAW

As it is explained below the different tax jurisdictions interact with each other and thus encourage harmful tax competition and erosion of national tax base. Not only OECD is urged to counter the distorting effects of this harmful tax competition but also the intervention of the Court is essential in order to resolve tax issues and limit problems presented by countries engaging in harmful tax practices. The reference in some preliminary ruling of European Court of Justice and the different ruling of every's Contracting State court pinpoint the need of an international tax regime. The role of the judiciary in protecting and the securing the rights of individuals and legal entities is of paramount importance. Notwithstanding this, courts set the guidelines for the consistent interpretation and application of legal provisions, by setting legal precedents and ensure that fundamental legal principles are being respected. Therefore, courts across all Member States should use their best endeavors to ensure that the authority to impose taxes is distributed properly among different States and jurisdictions.

In Case c-446/03 the request was submitted in proceedings between Marks & Spencer plc and the United Kingdom tax authority concerning the latter's rejection of a claim for tax relief by Marks & Spencer, which sought to deduct from its taxable profits in the United Kingdom losses incurred by its subsidiaries established in Belgium, Germany and France<sup>116</sup>. Under United Kingdom legislation resident companies in a group may set off their profits and losses among themselves but are not allowed to do so where the losses are incurred by subsidiaries which are not resident in the United Kingdom<sup>117</sup>. The Court rules that, although direct taxation is within the competence of Member States, they are still under the obligation to comply with the principles and provisions of EU law. The divergent tax treatment of subsidiaries by every Member State discourages corporations from creating subsidiaries outside the UK and impedes the proper and due application of the

---

<sup>116</sup><http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62003CJ0446>

<sup>117</sup>[http://ec.europa.eu/dgs/legal\\_service/arrets/03c446\\_en.pdf](http://ec.europa.eu/dgs/legal_service/arrets/03c446_en.pdf)

freedom of establishment. In order for such restrictions to be permissible, the relevant Member State shall call upon the existence of a legitimate objective that is compatible with the Treaty and justify them by drawing on overriding public interest reasons<sup>118</sup>. Consequently, it is contrary to freedom of establishment to preclude the possibility to deduct from its taxable profits in that Member State the losses incurred by its non-resident subsidiary<sup>119</sup>. This preliminary ruling secures a balance allocation of taxing powers between the various Member States, by avoiding the double use of losses and tax avoidance. The ECJ “convicts” the harmful tax practices and minimize the wide tax discretion that Member States used to have. It eliminates the discriminatory tax laws for foreign corporations and assigns equally the tax right.

Also in case c-324/00<sup>120</sup> (Lankhorst-Hohorst) the ECJ ruling to the question that was raised in proceedings brought by Lankhorst-Hohorst GmbH a company established in Germany, against the Finanzamt Steinfurt, a German tax authority, concerning the payment of corporation tax. LT BV<sup>121</sup> granted Lankhorst-Hohorst a loan but the following years the balance sheet of Lankhorst-Hohorst showed a deficit not covered by equity capital and the Finanzamt Steinfurt took the view that the interest paid to LT BV was equivalent to a covert distribution of profits<sup>122</sup> and taxed Lankhorst-Hohorst on them as such at the rate of 30%<sup>123</sup>. The Court judges that the fact that *“interest paid by a resident subsidiary on loan capital provided by a non-resident parent company is taxed as a covert dividend at a rate of 30%, whereas, in the case of a resident subsidiary whose parent company is also resident and receives a tax credit, interest paid is treated as expenditure and not as a covert dividend”* constitutes an obstacle to the freedom of

---

<sup>118</sup> [http://ec.europa.eu/dgs/legal\\_service/arrets/03c446\\_en.pdf](http://ec.europa.eu/dgs/legal_service/arrets/03c446_en.pdf)

<sup>119</sup> <http://curia.europa.eu/juris/document/document.jsf?jsessionid=9ea7d0f130d57909f1f11a84400eade9bc3c7ce52d8.e34KaxiLc3eQc40LaxqMbN4Oc3yRe0?text=&docid=57067&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=856304>

<sup>120</sup> <http://curia.europa.eu/juris/document/document.jsf?jsessionid=9ea7d0f130d5e9ff4b3a320c49be9b8ce8bf1f5e6b71.e34KaxiLc3eQc40LaxqMbN4Oc3mRe0?text=&docid=47587&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=318845>

<sup>121</sup> The sole shareholder in Lankhorst-Hohorst is Lankhorst-Hohorst BV which has its registered office in the Netherlands

<sup>122</sup> It is Defined in Paragraph 8a of the KStG.

<sup>123</sup> <http://curia.europa.eu/juris/document/document.jsf?text=&docid=47587&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=356213>

establishment which is not justified by pressing reasons of public interest.<sup>124</sup> The ECJ allocates the taxing power concerned, with a view to mitigating the risk of double taxation being applicable. Furthermore, it promotes the application of the principle of proportionality, which would require that the two Member States concerned consensually reach an agreement in order to avoid double taxation<sup>125</sup>. This ruling limits harmful tax practices and issues presented by countries and fiscally sovereignty territories engaging in harmful tax competition.

In Case C-294/99<sup>126</sup> the applicant in the main proceedings (*Athinaiki Zithopiia AE*), - whose main share capital is holding from a Netherlands company- claimed a refund because article 106 (2) and (3) of the Income Tax Code, which states that *“in the event of distribution of profits by a subsidiary to its parent company, in order to determine the taxable profits of the subsidiary its total net profits, including income and non-taxable income-when income falling within those two categories would not be taxable if they remained with the subsidiary and were not distributed to the parent company”* and was applied in this case constitute a withholding tax which is prohibited Article 5(1) of the Directive 90/435/EEC .

The court, studying the Directive 90/435/EEC, national legislation and the double taxation agreement concluded by the Hellenic Republic and the Kingdom of the Netherlands, rules that national legislation about the distribution of profits by a subsidiary to its parent company constitute withholding tax when it concerns the determination taxable profits of the subsidiary (its total net profits), including income which has been subject to special taxation entailing extinction of tax liability and non-taxable income must be reincorporated into the basic taxable amount, when income falling within those two categories would not be taxable on the basis of the national legislation if they remained with the subsidiary and were not

---

<sup>124</sup><http://curia.europa.eu/juris/document/document.jsf?text=&docid=46243&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=332347>

<sup>125</sup><http://curia.europa.eu/juris/document/document.jsf?text=&docid=47587&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=356213>

<sup>126</sup><http://curia.europa.eu/juris/document/document.jsf?text=&docid=46243&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=332347>

distributed to the parent company<sup>127</sup>. In this case the ECJ protect corporation from double taxation and restrict the wide tax power of the State.

It should be pinpointed that, according to settled case-law, although direct taxation falls within their competence, States must none the less exercise that competence consistently with Community law and, in particular, avoid any discrimination on grounds of nationality<sup>128</sup>.

The reference in case law from different jurisdiction illustrates how difficult is to harmonize different tax systems, even if we focus solely on EU Member States. Every State aims to increase its revenue, either by making discriminations against foreign companies in order to support domestic corporations, or by giving “illegal” tax incentives to foreign investments-companies in order to shift the competence tax jurisdiction and to pay tax in most favored tax systems. Therefore, the aforementioned preliminary ruling of the ECJ, which regulates tax issues at an EU level and interprets the applicable law according to the fundamental EU principles, is of paramount importance. Moreover, a common international tax system that designates a uniform way of imposing tax is equally essential. Tax harmonization across the EU will facilitate global harmonization which, through the adaptation of a uniform tax system, especially for foreign corporations, will lead to the consistent treatment of tax issues, such as tax avoidance, across the globe.

---

<sup>127</sup> <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:61999CJ0294&from=EN>

<sup>128</sup> (Case C-80/94 Wielockx [1995] ECR I-2493, paragraph 16, Case C-107/94 Asscher [1996] ECR I-3089, paragraph 36, Royal Bank of Scotland, paragraph 19)

## CONCLUSION

This thesis begins with elaborating on the notion of an offshore company, in order to demonstrate that, owing to the divergence of different tax systems, foreign corporations can exercise different activities and be subject to different tax regimes according to the jurisdiction of either the resident or the source State of their incorporation. Taking advantage of the complexity and great variety of tax systems, tax havens are constantly increasing, giving the opportunity to many companies and individuals to avoid or evade tax. The reference in some domestic legislations and cases highlights the wide discretion of States when it comes to imposing taxes and exercising their tax authority. The existence and the operation of an international economic organization, such as the OECD, are of primary importance. The OECD provides a platform to compare policy experiences, seek answers to common problems, identify good practices and coordinate domestic and international policies. The OECD sought to exert pressure on tax havens to adopt a standard package of tax, financial and banking regulation, with a view to averting a “race to the bottom” in tax rates<sup>129</sup>. Undoubtedly, the Model Double Taxation Convention on Income and Capital and the Action on BEPS constitute legal texts that should be adopted and applied globally. From the interpretation of the provisions of the Model Double Taxation Convention on Income and Capital it is clear that this Model Law assigns tax powers in an equitable manner and establishes a common tax system without discriminations. The adaptation of this Model Convention and its consistent application from every Contracting State can reduce the frequency of undesired occurrences in the field of tax law, which derived from the exploitation of different tax systems. Furthermore, it will harmonize the provisions of tax laws in various jurisdictions which interact with each other. Also, the issue of double taxation or

---

<sup>129</sup> [https://books.google.gr/books?id=nb1lzmC6xb8C&pg=PR6&lpg=PR6&dq=%E2%80%A2+Reuven+S.+AviYonah,+%E2%80%9CInternational+Tax+as+International+Law:+An+Analysis+of+the+International+Tax+Regime%E2%80%9D,+Cambridge+University+Press,+2007&source=bl&ots=sixqiw3k\\_q&sig=btIP0tN3KRka2F1Gi2kyJRAYcqM&hl=el&sa=X&ved=0ahUKewiY85eqyr\\_KAhULWBoKHdvjBikQ6AEIOjAE#v=onepage&q=%E2%80%A2%20Reuven%20S.%20AviYonah%2C%20%E2%80%9CInternational%20Tax%20as%20International%20Law%3A%20An%20Analysis%20of%20the%20International%20Tax%20Regime%E2%80%9D%2C%20Cambridge%20University%20Press%2C%202007&f=false](https://books.google.gr/books?id=nb1lzmC6xb8C&pg=PR6&lpg=PR6&dq=%E2%80%A2+Reuven+S.+AviYonah,+%E2%80%9CInternational+Tax+as+International+Law:+An+Analysis+of+the+International+Tax+Regime%E2%80%9D,+Cambridge+University+Press,+2007&source=bl&ots=sixqiw3k_q&sig=btIP0tN3KRka2F1Gi2kyJRAYcqM&hl=el&sa=X&ved=0ahUKewiY85eqyr_KAhULWBoKHdvjBikQ6AEIOjAE#v=onepage&q=%E2%80%A2%20Reuven%20S.%20AviYonah%2C%20%E2%80%9CInternational%20Tax%20as%20International%20Law%3A%20An%20Analysis%20of%20the%20International%20Tax%20Regime%E2%80%9D%2C%20Cambridge%20University%20Press%2C%202007&f=false)

non-taxation is handled by establishing mutual cooperation mechanisms among every state and by allocating efficiently the authority to impose taxes. By imposing taxes under an international tax regime, every Contracting State facilitates the equal economic development of every country and assists with the reduction of tax havens. The provisions of the Model Convention create an anti-tax avoidance framework according to the fundamental principles that are designated by EU law and every domestic legislation. However, unless this Model Convention assumes binding force, it will not be possible to harmonize the tax system of every Contracting State and achieve mutual cooperation on tax issues such as tax avoidance and tax evasion, to the desired extent. Besides, a prominent international tax academic and practitioner in the United States , David Rossenbloom, has stated that *“an international tax regime will constitute the triumph of international law”*.

## BIBLIOGRAPHY

- P.Douvis, "Offshore Activities" Athens 2008
- A.Ligomenou/E.B Zacharaki, " Offshore companies and tax havens", Athens,2009
- N.Barbas, "Direct Taxation and European Law", Athens-Thessaloniki, 2005
- GMichailidis, " Direction of Bussiness income Tax at Community level",Thessaloniki, 2005
- K.Finokaliwtis, "Tax Law ", 3<sup>rd</sup> Edition, Athens-Thessaloniki,2008
- K.Finokaliwtis/N.Barbas, " Public Finance ", Athes-Thessaloniki,2001
- P.Stagkos/E.Saxpekidou, " Law of the European Communities and the European Union", Athens-Thessaloniki,2000
- Michael Lang/Hans-Jonger Aigner/Ulrich Scheuerle/Markus Stefaner,"CFC Legislation", Domestic Provisions Tax Treaties and EC Law ",Kluwer Law International, 2006
- Michael Lang/Pasquale Pistone/Josef Schuch/Claus Staringer/Alfred Storck"Corporate Income Taxation in Europe: The Common Consolidated Corporate Tax ",Edward Elgar Publishing, 2013 (e-book)
- Jason Campbell Sharman, "Havens in a Storm: The Struggle for Global Tax Regulation", Cornell University Press, 2006 (e-book)
- Ronen Palan , "The Offshore World: Sovereign Markets, Virtual Places, and Nomad Millionaires ", Cornell University Press, 2006 (e-book)
- Reuven S. Avi-Yona, "International Tax as International Law: An Analysis of the International Tax Regime", Cambridge University Press, 2007(e-book)
- Ekkehari Reimer /Alexander Rust, "Klaus Vogel on Double Taxation Conventions ", 4<sup>th</sup> Edition, Volume 1, Kluwer Law International, 2015

- Ekkehari Reimer /Alexander Rust, “Klaus Vogel on Double Taxation Conventions“, 4<sup>th</sup> Edition, Volume 2, Kluwer Law International, 2015
- OECD, “Action Plan on Base Erosion and Profit Shifting” OECD Publishing, 2013 (e-book)
- Kevin Holmes, “International Tax Policy and Double Taxation Treaties”, IBFD 2007 (e-book)
- Frank Podgens, “Income from International Private Employment”, IBFD, 2006 (e-book)
- [www.un.org](http://www.un.org)
- [www.oecd.org](http://www.oecd.org)

*(Model Double Taxation Convention on Income and Capital, Action Plan on Base Erosion and Profit Shifting -Public Discussion Draft BEPS Action 3: Strengthening CFC Rules 12 May 2015, Project on Harmful Tax Competition the 2004 Progress Report)*

- [www.investopediacom](http://www.investopediacom)
- [www.encyclopedia.com](http://www.encyclopedia.com)
- <http://biztaxlaw.about.com/od/businessstaxes/f/taxavoidevade.htm> [www.forbes.com](http://www.forbes.com)
- [www.businessdictionary.com](http://www.businessdictionary.com)
- [www.taxheaven.gr](http://www.taxheaven.gr)
- [www.onpcsb.ro](http://www.onpcsb.ro)
- <http://eur-lex.europa.eu>

*(Directives: 2009/133EC, 90/435EC, 2006/98EC, 2001/96EU, 2003/48EC, 2014/48EC, 77/799EC, 2014/107EU)*

- <http://ec.europa.eu> [www.revenue.ie](http://www.revenue.ie)
- [www.irs.gov](http://www.irs.gov)
- [www.unibg.it](http://www.unibg.it)
- [www.lindeverlag.at](http://www.lindeverlag.at)

- [www.m-i-tax.de](http://www.m-i-tax.de)
- <http://curia.europa.eu>

*(c- 196/04, 436/08, 524/04, 231/05, 311/08, 446/03, 324/00, 294/99, 80/94)*

- [www.tovima.gr](http://www.tovima.gr)
- [www.gov.uk](http://www.gov.uk)
- [www.olswang.com](http://www.olswang.com)
- [www.blickrothenberg.com](http://www.blickrothenberg.com)
- [ww.deloitte.com](http://ww.deloitte.com)