European Union Court of Justice case
Romanian transfer pricing regulation does not violate EU law regarding the right of establishment because of balanced allocation of taxing right
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In this case, the Italian company *SC Impresa Pizzarotti & C SPA Italia* ("**Impresa**") received two loans totaling EUR 13.7 million from its Romanian branch *Impresa Pizzarotti & C SPA Italia Surcursala Cluj* ("**Impresa Cluj**"). The Romanian branch granted the loans without receiving any interest. The Romanian tax authorities argued that Impresa Cluj and Impresa should be regarded as associated enterprises under Article 11(2) Codul fiscal.[1] Therefore, the Romanian tax authorities argue that, in accordance with Article 29 (3) Codul fiscal, the Romanian branch should have granted the loan to Impresa at a market-conform interest rate in accordance with transfer pricing ("**TP**") regulation.

Impresa Cluj argues that the Romanian TP regulation is violating articles 49 and 63 of the Treaty on the Functioning of the European Union ("**TFEU**"), respectively the right of establishment and the free movement of capital, insofar the Romanian TP regulation determines that TP rules are applicable to the provision of funding between a branch located in a jurisdiction and its mother company located in another jurisdiction, since the TP regulation would not apply if the branch and its parent company are both located in the same jurisdiction.

The Romanian national court requested a preliminary ruling from the EU Court of Justice regarding the following question: "*Do articles 49 and 63 of the TFEU interfere with national transfer pricing regulation if the loan between a branch and mother company located in different member states is requalified as a revenue-generating transaction resulting in application of mandatory transfer pricing regulation whereas a loan between a branch and mother company located in the same member state cannot be requalified as a revenue-generating transaction and thus does not imply application of transfer pricing regulation?*"

According to established case-law of the EU Court of Justice, a tax provision that is restricting Article 49 TFEU (i.e. the right of establishment) is only acceptable if the provision is related to situations which are not objectively comparable or in a situation in which the provision is justified by compelling reasons recognized by Union law to serve general interest. In addition, the provision should be proportionate to the objective pursued.

The EU Court of Justice argues that transfer pricing regulation is necessary to ensure a balanced distribution of taxing rights between member states. This importance justifies the difference in treatment between the situation in which the branch and mother company are both located in the same member state and the situation in which the branch and mother company are located in different states. The latter situation could lead to an unbalanced distribution of taxing rights between different members states if branches are allowed to transfer their profits as favorable economic benefit to mother companies in a different member state. Therefore, restriction of the right of establishment by applying transfer pricing regulation is justified in view of a compelling reason to serve the general interest.

The EU Court of Justice states that the application of transfer pricing regulation is proportionate to guarantee a balanced distribution of taxing rights. In addition, the Court argues that transfer

[1] Codul fiscal is the Romanian Tax Code

pricing regulation does not exceed the objective pursued since the taxpayer has the opportunity to provide compelling reasons to justify deviation from the market-conform interest rate.

Therefore, the Romanian TP regulation does not violate the right of establishment as laid down in Article 49 TFEU in subject case, since TP regulation is necessary to ensure a balanced distribution of taxing rights between different member states.