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**A: Anti-avoidance  
measures of general  
nature and scope**  
– GAAR and  
other rules

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**Alfredo Garcia Prats, Werner Haslehner, Volker Heydt, Eric Kemmeren, Georg Kofler, Michael Lang, Jürgen Lüdicke, João Nogueira, Pasquale Pistone, Stella Raventos-Calvo, Emmanuel Raingeard de la Blétière, Isabelle Richelle, Alexander Rust, Rupert Shiers and Piergiorgio Valente<sup>1</sup>**

## Summary and conclusions

While the EU Treaties do not contain a general anti-abuse rule, the Court of Justice of the European Union (ECJ) uses the concept of abuse of law when interpreting the EU Treaties in multiple substantive areas of law, including direct taxation. Current EU mechanisms for protection against abusive practices have that case law as a common root. This report therefore starts by evaluating the emergence of the concept of abuse in the case law of the ECJ with regard to the fundamental freedoms. In this respect, the Court has accepted that discriminatory anti-avoidance rules can be justified by overriding reasons in the general interest but only where such rule specifically relates to wholly artificial arrangements aimed at circumventing the application of the legislation of the member state concerned. Moreover, general and special anti-abuse provisions are enshrined in secondary EU law instruments. This concerns the general anti-avoidance rule for the area of corporate taxation, which was introduced by the Anti-Tax Avoidance Directive (ATAD) and will be effective from 1 January 2019, and the more specific rules in the Parent-Subsidiary Directive (PSD), the Merger Directive (MD) and the Interest-Royalty Directive (IRD). This report explains the scope of these provisions, their interpretation and application, and their relationship with primary EU law, tax treaties and national law. Finally, this report provides a brief outlook on the impact of EU law on domestic tax systems in this field, stressing that general anti-abuse measures might create tensions with fundamental taxpayers' rights, such as the right to legal certainty and the freedom to arrange one's economic affairs.

<sup>1</sup> This report was prepared within and by the members of the ECJ Task Force of the Confédération Fiscale Européenne (CFE) with the support of CFE's President, Piergiorgio Valente. Although this report has been drafted jointly within the ECJ Task Force, its content does not necessarily reflect the position of all members of the group.

## 1. Introduction

### 1.1 Is there an EU GAAR?

The purpose of any anti-avoidance clause (and *a fortiori*) of a GAAR is to protect the proper functioning of certain legal systems' rules. It provides a useful tool that can be used to deprive the legal effects of any arrangements that, although meeting the material conditions set by the law, do not meet its underlying rationale. A GAAR provides the legal systems with an extra layer of protection against practices that exploit certain loopholes, omissions or deficiencies in the wording of legal provisions.

The EU treaty system does not contain a GAAR as such,<sup>2</sup> but the Court of Justice of the European Union (EC) uses the concept of abuse of law when interpreting the EU Treaties<sup>3</sup> in multiple, substantive areas of law, including taxation.<sup>4</sup> By contrast, in secondary law, we find a multiplicity of anti-abuse provisions, with different shapes and forms. On direct taxation (and this report refers solely to this field), we also find GAARs in multiple instruments.

The goal of this EU report is to review the EU mechanisms for protection against abusive practices that, regardless of their appearance, have a function similar to a domestic GAAR. The wording of these EU mechanisms has a common root: the case law of the Court of Justice of the European Union (EC). Thus, this report will start by analysing the emergence of the concept of abuse in the case law of the Court. Secondly, it will focus on the fight against abuse in the field of primary EU Law (and, in particular, on assessing the compatibility of domestic tax law provisions – on direct taxation – with the Fundamental Freedoms). Thirdly, it will examine (general and special) anti-abuse provisions enshrined in secondary EU law instruments. Lastly, it will provide an outlook on the impact of EU law on domestic tax systems in this field.

<sup>2</sup> The word "abuse" is only used in the field of competition law, but in a different context: Art. 102 of the Treaty on the Functioning of the European Union (TFEU) ("Any abuse by one or more undertakings of a dominant position within the internal market or in a substantial part of it shall be prohibited as incompatible with the internal market in so far as it may affect trade between member states") and Art. 104 TFEU (which refers to the prohibition of abuse of dominant position).

<sup>3</sup> Those are the Treaty on the European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU), and their predecessors. The consolidated versions of the TEU and the TFEU can be found in [2016] OJ C 202, p.1.

<sup>4</sup> For detailed analyses on the various issues, see, e.g. D. Weber, *Tax Avoidance and the EC Treaty Freedoms: A Study of the Limitations under European Law for the Prevention of Tax Avoidance* (Kluwer Law International, 2005); L. De Broe, *International Tax Planning and Prevention of Abuse* (IBFD Amsterdam, 2007); R. de la Feria and S. Vogenauer (eds.), *Prohibition of Abuse of Law – A New General Principle of EU Law?* (Hart Publishing, 2011); A. P. Dourado (ed.), *Tax Avoidance Revisited in the EU BEPS Context*, EATLP International Tax Series Vol. 15 (IBFD Amsterdam, 2017). It should be noted that the EU concept of abuse is not relevant for purely domestic taxation when no EU rules are involved and that, consequently, member states are not obliged to combat abuse in those areas; as the Court noted, "it is clear that no general principle exists in European Union law which might entail an obligation of the member states to combat abusive practices in the field of direct taxation and which would preclude the application of a provision such as that at issue in the main proceedings where the taxable transaction proceeds from such practices and European Union law is not involved" (EC, 29 March 2012, C-417/10, *3M Italia, EU:C:2012:184*, para. 32).

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## 1.2 Origins of the concept of abuse

As mentioned, the EU treaties do not contain a GAAR and references to the concept of abuse are very scarce. However, many domestic EU countries have long-standing traditions of prohibiting abuse or abusive practices, apart from the mere teleologic (or corrective) interpretation of their positive rules. Thus, and not surprisingly, it did not take much time for the ECJ to import the concept and to use it within the framework of EU Law.

In *Van Binsbergen*<sup>5</sup> the ECJ held, for the first time, that a Member state is allowed to take measures that restrict the freedom to provide services insofar as these rules are aimed at preventing the circumvention of domestic rules. Without referring to the concept of "abuse", the ECJ held that EU law does not protect an activity that is "entirely or principally directed towards its territory ... for the purpose of avoiding [its domestic rules]".<sup>6</sup> It repeated this ruling in a series of cases regarding the freedom to provide services (in particular broadcasting services),<sup>7</sup> the freedom of establishment,<sup>8</sup> the free movement of goods<sup>9</sup> and the free movement of workers.<sup>10</sup> For the ECJ, an abusive practice (such as circumvention, U-turn, undue entitlement) should be considered as being excluded from the sphere of protection of EU law. However, it did not provide much guidance on how an abusive practice should be characterised.<sup>11</sup>

Further clarification appeared only in *Emsland-Stärke*<sup>12</sup> with the introduction of a two-pronged test, relying on an objective and a subjective element. This test mirrored the *abus de droit* doctrine that could be found in some civil law systems in continental Europe.<sup>13</sup> The Court stated:

"A finding of an abuse requires, firstly, a combination of objective circumstances in which, despite formal observance of the conditions laid down by the Community rules, the purpose of those rules has not been achieved.

It requires, secondly, a subjective element consisting in the intention to obtain an advantage

<sup>5</sup> ECJ, 3 December 1974, C-33/74, *Van Binsbergen*, EU:C:1974:131.

<sup>6</sup> ECJ, 3 December 1974, C-33/74, *Van Binsbergen*, EU:C:1974:131, para.13.

<sup>7</sup> ECJ, 18 March 1980, C-52/79, *Debaveu*, EU:C:1980:83; ECJ, 25 July 1991, C-288/89, *Stichting Collectieve Antennevoorziening Gouda*, EU:C:1991:323; ECJ, 16 December 1992, C-211/91, *Commission v. Belgium*, EU:C:1992:526; ECJ, 3 February 1993, C-148/91, *Veronica Omroep Organisatie*, EU:C:1993:45; ECJ, 10 September 1996, C-11/95, *Commission v. Belgium*, EU:C:1996:316; ECJ, 10 September 1996, C-222/94, *Commission v. United Kingdom*, EU:C:1996:314; ECJ, 5 June 1997, C-56/96, VT4, EU:C:1997:284 and ECJ, 9 July 1997, C-34/95, C-35/95 and C-36/95, *De Agostini and TV-Shop*, EU:C:1997:344.

<sup>8</sup> ECJ, 7 February 1979, C-115/78, *Knoors*, EU:C:1979:31; ECJ, 6 October 1981, C-246/80, *Broekmeulen*, EU:C:1981:218; ECJ, 22 September 1983, C-271/82, *Auer*, EU:C:1983:243; ECJ, 19 January 1988, C-292/86, *Gullung*, EU:C:1988:15; ECJ, 27 September 1988, C-81/87, *Daily Mail*, EU:C:1988:456; ECJ, 27 September 1989, C-130/88, *Van de Bijl*, EU:C:1989:349; ECJ, C-61/89, 3 October 1990, *Bouchoucha*, EU:C:1990:343; ECJ, 9 March 1999, C-212/97, *Centros*, EU:C:1999:126 and ECJ, 30 September 2003, C-167/01, *Inspire Art*, EU:C:2003:512.

<sup>9</sup> ECJ, 10 January 1985, C-229/83, *Leclerc*, EU:C:1985:1.

<sup>10</sup> ECJ, 23 March 1982, C-53/81, *Levin*, EU:C:1982:105; ECJ, 27 March 1985, C-249/83, *Hoeckx*, EU:C:1985:139; ECJ, 3 June 1986, C-139/85, *Kempf*, EU:C:1986:223 and ECJ, 21 June 1988, C-39/86, *Lair*, EU:C:1988:322 and ECJ, 26 February 1991, C-292/89, *Antonissen*, EU:C:1991:80.

<sup>11</sup> For a detailed overview of the Court's position at the time see, for instance, K. Ottersbach, *Rechtsmissbrauch bei den Grundfreiheiten des europäischen Binnenmarktes* (Nomos Baden-Baden, 2001), p 259.

<sup>12</sup> ECJ, 14 December 2000, C-110/99, *Emsland-Stärke*, EU:C:2000:695.

<sup>13</sup> See L. Leclercq, "Interacting principles: the French abuse of Law concept and the EU notion of abusive practices", 61 *Bulletin for International Taxation* (2007), p. 235.

from the Community rules by creating artificially the conditions laid down for obtaining it. The existence of that subjective element can be established, *inter alia*, by evidence of collusion between the Community exporter receiving the refunds and the importer of the goods in the non-member country.<sup>14</sup>

This test became the model for assessing abuse in EU law and became applicable to all domains subjected to the Court's jurisdiction, such as company law,<sup>15</sup> common agriculture policy<sup>16</sup> or social security.<sup>17</sup> It is still used and referred to in the most recent decisions.<sup>18</sup> The prohibition of abuse, following this test, is now integrated into several secondary law provisions<sup>19</sup>.

The scope of application of this prohibition is very broad and covers rights and advantages provided both by primary and secondary law.<sup>20</sup>

EU law cannot be relied on for abusive or fraudulent ends.<sup>21</sup> In other words, fraud or abusive acts cannot trigger the application of any EU Law provision.<sup>22</sup> Therefore, the refusal of a right or an advantage stemming from EU law, based on the prohibition of abuse, does not require a specific legal basis.<sup>23</sup> In *Kofoed*,<sup>24</sup> regarding the applicability of the anti-abuse provision of the Merger Directive by a member state that failed to transpose it to domestic law,<sup>25</sup> the ECJ held that, in the absence of that domestic provision, it was up to the referring court to check whether the domestic law of that country entailed "a provision or a general principle prohibiting the abuse of rights or other provisions on tax evasion or tax avoidance which might be interpreted in accordance with" the above-mentioned anti-abuse provision.<sup>26</sup> The Court has, however, subsequently emphasised the necessity to seek a domestic anti-abuse rule to be interpreted in accordance with the non-transposed anti-abuse clause of a directive. This notwithstanding, *Cussens* may imply that any right or advantage can be

<sup>14</sup> ECJ, 14 December 2000, C-110/99, *Emsland-Stärke*, EU:C:2000:695, paras. 52 and 53.

<sup>15</sup> See ECJ, 12 May 1998, C-367/96, *Kefalas*, EU:C:1998:222, and ECJ, 23 March 2000, C-373/97, *Diamantis*, EU:C:2000:150.

<sup>16</sup> ECJ, 3 March 1993, C-8/92, *General Milk Products*, EU:C:1993:82.

<sup>17</sup> ECJ, 2 May 1996, C-206/94, *Paletta*, EU:C:1996:182.

<sup>18</sup> See ECJ, 14 April 2016, C-131/14, *Cervati and Malvi*, EU:C:2016:255, paras. 33 and 34.

<sup>19</sup> See *infra* Chapter 3.

<sup>20</sup> See ECJ, 22 November 2017, C-251/16, *Cussens*, EU:C:2017:881, para. 30, stating that "it is apparent from the Court's case law that the principle that abusive practices are prohibited is applied to the rights and advantages provided for by EU law, irrespective of whether those rights and advantages have their basis in the Treaties [...], in a regulation [...] or in a directive [...]. It is thus apparent that that principle is not of the same nature as the rights and advantages to which it applies".

<sup>21</sup> ECJ, 12 May 1998, C-367/96, *Kefalas*, EU:C:1998:222, para. 20; ECJ, 23 March 2000, C-373/97, *Diamantis*, EU:C:2000:150, para. 33; and ECJ, 3 March 2005, C-32/03, *Fini H*, EU:C:2005:128, para. 32. See also ECJ, 11 October 1977, C-125/76, *Cremer*, EU:C:1977:148, para. 21; ECJ, 3 March 1993, C-8/92, *General Milk Products*, EU:C:1993:82, para. 21; and ECJ, 14 December 2000, C-110/99, *Emsland-Stärke*, EU:C:2000:695, para. 51.

<sup>22</sup> ECJ, 18 December 2014, C-131/13, C-163/13 and C-164/13, *Italmoda*, EU:C:2014:2455, para. 55.

<sup>23</sup> ECJ, 18 December 2014, C-131/13, C-163/13 and C-164/13, *Italmoda*, EU:C:2014:2455, para. 62. In the words of the Court, said refusal "is simply the consequence of the finding that, in the event of fraud or the abuse of rights, the objective conditions required in order to obtain the advantage sought are not, in fact, met". See ECJ, 22 November 2017, C-251/16, *Cussens*, EU:C:2017:881, para. 32.

<sup>24</sup> ECJ, 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408.

<sup>25</sup> Council Directive (EEC) 90/434 of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different member states, [1990] OJ L 225, p. 1.

<sup>26</sup> ECJ, 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408, para. 46.

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denied based on the EU general principle of the prohibition of abusive practices, regardless of any specific EU or domestic law provision.<sup>27</sup>

If a right or an advantage has already been granted, following an abusive practice, “the transactions involved in it must be redefined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive practice”. Normally, it is the referring court that must “redefine those transactions so as to re-establish the situation that would have prevailed in the absence of the elements constituting that abusive practice”,<sup>28</sup> which should be done in accordance with the domestic law legal provisions. This orientation of the ECJ is particularly important as it is, subsequently, taken into account in the design of the general and specific clauses that can be found in secondary law (as shown below).

In said cases (in which an advantage has already been improperly received), the request to give it back (namely as a repayment) should be considered as the mere consequence of the failure to meet the objective conditions to obtain that right or advantage and thus does not breach the principles of legality,<sup>29</sup> protection of legitimate expectations or legal certainty.<sup>30</sup>

The prohibition of abusive practices is currently described by the Court as a general principle of EU law and, as such, has an inherent general and comprehensive character.<sup>31</sup> It applies to harmonised and non-harmonised areas and does not require transposition (a specific domestic law clause embodying that prohibition), even in fields where harmonisation required the transposition of EU law into domestic systems, such as VAT.<sup>32</sup>

### 1.3 Abuse and taxation

In tax matters, *Halifax*<sup>33</sup> is considered the first case where the Court relied upon the *Emsland-Stärke*<sup>34</sup> test, also with an objective and subjective prong.<sup>35</sup> Concerning the latter, the Court further specified that “it must also be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage”.<sup>36</sup> This clarification is particularly relevant for two different reasons. Firstly, it clarifies that the subjective

<sup>27</sup> See ECJ, 22 November 2017, C-251/16, *Cussens*, EU:C:2017:881, paras. 25-44.

<sup>28</sup> ECJ, 22 December 2010, C-103/09, *Weald Leasing*, EU:C:2010:804, paras 48 and 52.

<sup>29</sup> See ECJ, 4 June 2009, C-158/08, *Pometon*, EU:C:2009:349, para. 28: “The obligation to repay is not a penalty, but simply the consequence of a finding that the conditions required to obtain the advantage derived from the Community rules were created artificially, thereby rendering the advantage received a payment that was not due and thus justifying the obligation to repay it”.

<sup>30</sup> ECJ, 18 December 2014, C-131/13, C-163/13 and C-164/13, *Italmoda*, EU:C:2014:2455, para. 60; ECJ, 22 January 2015, C-401/13 and C-432/13, *Balazs*, EU:C:2015:26, paras 49 and 50 and the case-law cited; and ECJ, 19 April 2016, C-441/14 DI, EU:C:2016:278, paras 38-40.

<sup>31</sup> See ECJ, 22 November 2017, C-251/16, *Cussens*, EU:C:2017:881, para. 31.

<sup>32</sup> See ECJ (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:121, paras. 70 and 71.

<sup>33</sup> ECJ (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:121. See, however, also ECJ, 12 July 1988, 138/86, *Direct Cosmetics Ltd*, EU:C:1988:383, for an earlier case using the expression “tax avoidance”.

<sup>34</sup> ECJ, 14 December 2000, C-110/99, *Emsland-Stärke*, EU:C:2000:695.

<sup>35</sup> ECJ (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:12, paras 74 and 75.

<sup>36</sup> ECJ (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:12, para. 75.

element is something to be derived from objective elements.<sup>37</sup> Secondly, it states that the tax advantage has to be an “essential aim” of the conduct. Not the exclusive, but the essential aim. This has been repeated in *Part Service*,<sup>38</sup> *Ampliscientifica*<sup>39</sup> and subsequent case law. Recently, the Court stated that, to assess the “essential aim”, a national court may:

“take account of the purely artificial nature of the transactions and the links of a legal, economic and/or personal nature between the operators involved [...], those aspects being such as to demonstrate that the accrual of a tax advantage constitutes the principal aim pursued, notwithstanding the possible existence, in addition, of economic objectives arising from, for example, marketing, organisation or guarantee considerations”.<sup>40</sup>

This requirement has a decisive influence on current secondary law anti-abuse provisions, which we will examine subsequently. However, in these clauses, the threshold was set much lower, and they only require the tax advantage to be “one of the principal aims”.

This abuse test was also applied in case law on direct taxation. In the earliest cases, the test was applied in a different manner and context. The Court did not assess a potential abuse of EU law provisions, but merely whether member states had properly transposed the domestic anti-abuse law provisions of the corporate tax directives. The first references to abuse can be found in *Denkavit*<sup>41</sup>, but as a mere allegation by the parties. References can also be found in *Leur-Bloem*<sup>42</sup>, where the Court required domestic anti-abuse provisions not to be applied automatically (i.e. by reference to abstract criteria that would exclude certain categories of persons or situations), but rather to allow for a case-by-case analysis and for judicial review. Apart from these two cases, abuse remained apparently absent from the Court’s case law.<sup>43</sup>

It took more than one decade to re-enter the Court decisions but, since then, it has been applied profusely. This return happened with *Kofoed*<sup>44</sup>. In this case, the Court went further and clearly stated that the anti-abuse clauses of the directives are no more than a reflection of “the general Community law principle that abuse of rights is prohibited”.<sup>45</sup> And from this breakthrough recognition, we have now a settled and very detailed case law on abuse, both in secondary and in primary law. In what concerns the latter, it is invoked mainly in two different settings: firstly, to assess whether a specific situation falls within the scope of a specific treaty provision (such as a fundamental freedom), and secondly, as grounds for justification of a discriminatory domestic tax rule. This will be our focus in the next section.

<sup>37</sup> More emphatically, Advocate General Poiares Maduro stated that “what matters is not the actual state of mind of [the taxpayer], but the fact that the activity, objectively speaking, has no other explanation but to secure a tax advantage” (see Opinion AG Poiares Maduro, 7 April 2005, C-255/02, *Halifax plc*, EU:C:2005:200, para. 70).

<sup>38</sup> ECJ, 21 February 2008, C-425/06, *Part Service*, EU:C:2008:108, paras. 42-45.

<sup>39</sup> ECJ, 22 May 2008, C-162/07, *Ampliscientifica and Amplifin*, EU:C:2008:301, para. 30.

<sup>40</sup> ECJ, 22 November 2017, C-251/16, *Cussens*, EU:C:2017:881, para. 60.

<sup>41</sup> ECJ, 14 December 2006, C-170/05, *Denkavit Internationaal and Denkavit France*, EU:C:2006:783.

<sup>42</sup> ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369.

<sup>43</sup> For a review of the case law of that period see, e.g. CFE ECJ Task Force, “Opinion Statement of the CFE ECJ Task Force on the Concept of Abuse in European Law, Based on the Judgments of the European Court of Justice Delivered in the Field of Tax Law – November 2007”, 48 *European Taxation* (2008), pp. 33 et seq.

<sup>44</sup> ECJ, 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408.

<sup>45</sup> ECJ, 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408, para. 38.

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## 2. Avoidance and fundamental freedoms

### 2.1 Scope of the fundamental freedoms

The Court held that, also in the area of direct taxation, EU nationals cannot rely on the fundamental freedoms to avoid the national legislation of the member states. EU nationals are not protected by the fundamental freedoms if they try to circumvent the national tax rules.<sup>46</sup> However, taxpayers are allowed to make use of different tax rules in different member states. They cannot be deprived of the right to rely on the provisions of the Treaty on the grounds that they are benefitting from tax advantages which are legally provided by the rules in force in another member state.<sup>47</sup> Setting up a company in another member state and transferring genuine economic activities to another member state does not constitute abuse of the fundamental freedoms, even if the goal of the transaction is to benefit from a more favourable tax regime.<sup>48</sup>

### 2.2 Fight against abuse as grounds for justification

Member states are generally free to introduce anti-avoidance clauses without violating any of the fundamental freedoms if they treat cross-border and domestic situations equally. However, in many circumstances specific anti-avoidance rules are not necessary in a purely domestic situation, while there is a particular need for such rules in a cross-border setting. If member states introduce discriminatory anti-avoidance rules and restrict the fundamental freedoms, the question arises as to whether discriminatory anti-avoidance rules can be justified by overriding reasons related to the general interest.

In *Avoir fiscal*, the Court held in 1986 that the fight against tax avoidance cannot justify a discriminatory treatment by stating that "the risk of tax avoidance cannot be relied upon in this context. Article [49 TFEU] does not permit any derogation from the fundamental principle of freedom of establishment on such a ground".<sup>49</sup> Later on, the Court pointed out that the fight against tax avoidance constitutes an overriding requirement in the general interest capable of justifying a discriminatory treatment. In *ICl v. Colmer*, the Court was not required to elaborate on the exact meaning and scope of the justification because the domestic anti-avoidance rules were clearly disproportionate, but the Court had already made it clear that the scope of anti-avoidance rules must be limited to cover only wholly artificial arrangements: "As regards the justification based on the risk of tax avoidance, suffice it to note that the legislation at issue in the main proceedings does not have the specific purpose of preventing wholly artificial arrangements, set up to circumvent UK tax

<sup>46</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 35;

<sup>47</sup> ECJ, 11 December 2003, C-364/01, *Barbier*, EU:C:2003:665, para 71; ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 36.

<sup>48</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 37 et seq.

<sup>49</sup> ECJ, 28 January 1986, 270/83, *Commission v. France*, EU:C:1986:37, para. 25.

legislation, from attracting tax benefits..."<sup>50</sup> In *Cadbury Schweppes*, the Court dealt with the justification in much more detail. It started by reiterating that "a national measure restricting freedom of establishment may be justified where it specifically relates to wholly artificial arrangements aimed at circumventing the application of the legislation of the member state concerned".<sup>51</sup> The Court then analysed the purpose of the freedom of establishment and came to the conclusion that article 49 TFEU allows the taxpayer to carry on his activities in the other member state, thereby participating, on a stable and continuous basis, in the economic life of the other member state. The Court concluded that the freedom presupposes actual establishment in the host member state and the pursuit of genuine economic activities.<sup>52</sup> The finding as to whether a genuine economic activity exists must be based on objective factors which are ascertainable by third parties. With regard to setting up a company, it must be verified whether the company physically exists in terms of premises, staff and equipment or whether it can be regarded as having the characteristics of a mere letterbox or front subsidiary.<sup>53</sup>

A wholly artificial arrangement requires both a subjective and an objective element: A domestic anti-avoidance rule may only be applied if the taxpayer had the intention to obtain a tax advantage and objective circumstances show that, despite formal observance of the conditions laid down by Union law, the objective pursued by the freedom of establishment has not been achieved.<sup>54</sup> In addition, the national anti-avoidance rule must be suitable to achieve that purpose and must not go beyond what is necessary to achieve that objective.<sup>55</sup> Consequently, a general presumption of abuse is not permitted. Abuse must be established on a "case-by-case basis".

At the same time, the Court made it clear that member states are not allowed to apply their anti-abuse legislation if the taxpayer shifts genuine economic activities to other member states, even if the sole purpose of this transfer is the reduction of his or her tax liability.

*Eurowings*<sup>56</sup> and *Cadbury Schweppes*<sup>57</sup> show that tax jurisdiction shopping is, in principle, part of a non-harmonised internal market. member states may not penalise the use of

<sup>50</sup> ECJ, 16 July 1998, C-264/96, *Imperial Chemical Industries v. Colmer*, EU:C:1998:370, para. 26. See also ECJ, 21 November 2002, C-436/00, *X and Y*, EU:C:2002:704 para. 61; ECJ, 12 December 2002, C-324/00, *Lankhorst-Hoherst*, EU:C:2002:749, para. 37; ECJ, 11 March 2004, C-9/02, *de Lasteyrie du Saillant*, EU:C:2004:138, para. 50. The ECJ does not clearly distinguish between denying the application of the fundamental freedom – as a wholly artificial arrangement is not covered by the freedom of establishment – and the fight against wholly artificial arrangements as grounds of justification, see J. Englisch in: H. Schaumburg and J. Englisch (eds.), *Europäisches Steuerrecht* (Cologne, 2015), para. 7.254.

<sup>51</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 51.

<sup>52</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 53 et seq.

<sup>53</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 67 et seq.

<sup>54</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 64; Here the Court referred to its reasoning in the *Emsland Stärke* and the *Halifax* judgements.

<sup>55</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 59 et seq.

<sup>56</sup> ECJ, 26 October 1999, C-294/97, *Eurowings Luftverkehr*, EU:C:1999:524.

<sup>57</sup> ECJ, 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544.

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low-tax regimes in other jurisdictions if the economic activity is genuine.<sup>58</sup> The Court stated in *Eurowings* that “[a]ny tax advantage resulting for providers of services from the low taxation to which they are subject in the member state in which they are established cannot be used by another member state to justify less favourable treatment in tax matters...Such compensatory tax arrangements prejudice the very foundation of the single market”.<sup>59</sup>

The jurisprudence on “wholly artificial arrangements” makes it difficult for the member states to find a justification for anti-avoidance rules which only apply to cross-border situations. The Court saw the need to extend its jurisprudence to cases in which the taxpayer exercised a genuine economic activity, but where the particular transaction led to a shift of tax revenue to a country where the profit was not generated. The fight against abuse in these circumstances helped to ensure a balanced allocation of taxing rights.<sup>60</sup>

In its *Marks & Spencer* judgment, the Court regarded the fight against tax avoidance in combination with other objectives as a justification for discriminatory provisions. All three objectives, taken together, were capable of justifying the different treatment of cross-border losses in comparison with domestic losses.<sup>61</sup> With regard to the risk of tax avoidance, the Court stated that “the possibility of transferring the losses incurred by a non-resident company to a resident company entails the risk that, within a group of companies, losses will be transferred to companies established in the member states which apply the highest rates of taxation and in which the tax value of the losses is therefore the highest.”<sup>62</sup> In *Oy AA*, the Court further explained that member states may apply their anti-avoidance legislation to safeguard a balanced allocation of taxing rights.<sup>63</sup> It held that “the objectives of safeguarding the balanced allocation of the power to impose taxes between member states and the prevention of tax avoidance are linked. Conduct involving the creation of wholly artificial arrangements which do not reflect economic reality with a view to escaping the tax normally due on the profits generated by activities carried out on national territory is such as to undermine the right of the member states to exercise their tax jurisdiction in relation to those activities and jeopardise a balanced allocation between member states of the power to impose taxes.”<sup>64</sup> The Court went on to state that the application of anti-avoidance rules

<sup>58</sup> Opinion of AG Léger, 2. May 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 56: “The fact that the tax system may also be classified as State aid incompatible with the common market does not alter that analysis. As the Commission stated in its observations, the Treaty contains specific provisions, in Articles 87 EC and 88 EC [now: Articles 107 and 108 TFEU], intended to check the compatibility of such a measure with the common market and to eliminate its harmful effects on that market. The fact that such a tax system does not comply with the rules of the Treaty cannot therefore entitle a member state to take unilateral measures intended to counter its effects by limiting freedom of movement”; AG Geelhoed, 29 June 2006, C-524/04, *Thin Cap Group Litigation*, EU:C:2007:16, para. 63: “In principle, it is quite valid, and indeed fundamental to the idea of an internal market, for taxpayers to seek to arrange their (crossborder) tax affairs in a manner most advantageous to them. However, this is only permissible insofar as the arrangement is genuine; that is to say, not a wholly artificial construct aimed at abusing and circumventing national tax legislation.” See also B. Terra and P. Wattel, *European Tax Law*, 6<sup>th</sup> edition (Alphen aan den Rijn, 2012), p. 916; J. Englisch in: H. Schaumburg and J. Englisch (eds.), *Europäisches Steuerrecht* (Cologne, 2015), para. 7.255.

<sup>59</sup> ECJ, 26 October 1999, C-294/97, *Eurowings Luftverkehr*, EU:C:1999:524, paras 44 et seq.

<sup>60</sup> B. Terra and P. Wattel, *European Tax Law*, 6<sup>th</sup> edition (Alphen aan den Rijn, 2012), p. 923 et seq.; J. Englisch in: H. Schaumburg and J. Englisch (eds.), *Europäisches Steuerrecht* (Cologne, 2015), para. 7.256 et seq.

<sup>61</sup> ECJ, 13 December 2005, C-446/03, *Marks & Spencer*, EU:C:2005:763, para. 51.

<sup>62</sup> ECJ, 13 December 2005, C-446/03, *Marks & Spencer*, EU:C:2005:763, para. 49.

<sup>63</sup> ECJ, 18 July 2007, C-231/05, *Oy AA*, EU:C:2007:439.

<sup>64</sup> ECJ, 18 July 2007, C-231/05, *Oy AA*, EU:C:2007:439, para. 62.

can be justified, even if the activity is not devoid of any substance: “Even if the legislation at issue in the main proceedings is not specifically designed to exclude purely artificial arrangements from the tax advantage it confers – arrangements devoid of economic reality, created with the aim of escaping the tax normally due on the profits generated by activities carried out on national territory – such legislation may nevertheless be regarded as proportionate to the objectives pursued, taken as a whole.”<sup>65</sup>

These findings are especially relevant in the area of thin-capitalisation and transfer pricing, where all operators exercise a genuine economic activity, but where excessive debt-financing or transactions which go beyond the arm's length standard could lead to an unjustified shift of tax revenue from a high-tax to a low-tax jurisdiction.<sup>66</sup> In *Thin Cap Group Litigation*, the Court recognised the OECD arm's length standard test as the right way to distinguish between abusive tax base erosion through interest deduction, on the one hand, and genuine business financing, on the other.<sup>67</sup> In *SGI*, the Court permitted the application of domestic anti-avoidance rules which did not specifically target wholly artificial arrangements, but rather had the objective of curbing tax base erosion, because such legislation also preserved a balanced allocation of taxing powers:<sup>68</sup> “... it must be held that to permit resident companies to transfer their profits, in the form of unusual or gratuitous advantages, to companies with which they have a relationship of interdependence that are established in other member states may well undermine the balanced allocation of the power to impose taxes between the member states.”<sup>69</sup> Secondly, as regards the prevention of tax avoidance, it should be recalled that a national measure restricting freedom of establishment may be justified where it specifically targets wholly artificial arrangements designed to circumvent the legislation of the member state concerned. ... In that context, national legislation which is not specifically designed to exclude from the tax advantage it confers such purely artificial arrangements – devoid of economic reality, created with the aim of escaping the tax normally due on the profits generated by activities carried out on national territory – may nevertheless be regarded as justified by the objective of preventing tax avoidance, taken together with that of preserving the balanced allocation of the power to impose taxes between the member states”.<sup>70</sup>

While the Court generally allowed the member states to recharacterise transactions which did not meet the arm's length test, it required the member states to grant to the taxpayer the opportunity to provide evidence of any commercial justification that there may have been for the arrangement, without being subject to undue administrative constraints.<sup>71</sup> In addition, the national measure must not go beyond what is necessary. If a transaction does not meet the arm's length standard, then the corrective tax measure must be confined

<sup>65</sup> ECJ, 18 July 2007, C-231/05, *Oy AA*, EU:C:2007:439, para. 63.

<sup>66</sup> See J. Englisch in: H. Schaumburg and J. Englisch (eds.), *Europäisches Steuerrecht* (Cologne, 2015), para. 7.256.

<sup>67</sup> ECJ, 13 March 2007, C-524/04, *Test Claimants in the Thin Cap Group Litigation*, EU:C:2007:161, paras 47 et seq.; B. Terra and P. Wattel, *European Tax Law*, 6<sup>th</sup> edition (Alphen aan den Rijn, 2012), p. 927.

<sup>68</sup> B. Terra and P. Wattel, *European Tax Law*, 6<sup>th</sup> edition 2012, Alphen aan den Rijn, p. 926.

<sup>69</sup> ECJ, 21 January 2010, C-311/08, *SGI*, EU:C:2010:26, para. 63.

<sup>70</sup> ECJ, 21 January 2010, C-311/08, *SGI*, EU:C:2010:26, para. 65 et seq.

<sup>71</sup> ECJ, 13 March 2007, C-524/04, *Test Claimants in the Thin Cap Group Litigation*, EU:C:2007:161, para. 82; ECJ, 21 January 2010, C-311/08, *SGI*, EU:C:2010:26, para. 71.

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to the part that exceeds the standard.<sup>72</sup> This finding can be generalised for all domestic anti-abuse measures. The proportionality principle implies that the application of the anti-avoidance rule should not lead to a punishment. It should reinstate the situation as if the abuse had not occurred, but should not amount to a higher tax liability than the one without the abusive transaction.<sup>73</sup>

### 3. Avoidance and secondary EU law

#### 3.1 Article 6 ATAD

##### 3.1.1 *Introduction*

While several targeted anti-avoidance rules had been included in partially harmonising tax directives before, the first general anti-avoidance rule was introduced with the ATAD Directive,<sup>74</sup> adopted on 12 July 2016 and effective from 1 January 2019.<sup>75</sup> The GAAR's three paragraphs read:

1. For the purposes of calculating the corporate tax liability, a member state shall ignore an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the applicable tax law, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one step or part.
2. For the purposes of paragraph 1, an arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality.
3. Where arrangements or a series thereof are ignored in accordance with paragraph 1, the tax liability shall be calculated in accordance with national law."

<sup>72</sup> EC, 21 January 2010, C-311/08, *SGI*, EU:C:2010:26, para. 72: "Secondly, where the consideration of such elements leads to the conclusion that the transaction in question goes beyond what the companies concerned would have agreed under fully competitive conditions, the corrective tax measure must be confined to the part which exceeds what would have been agreed if the companies did not have a relationship of interdependence."

<sup>73</sup> B. Terra and P. Wattel, *European Tax Law*, 6<sup>th</sup> edition 2012, Alphen aan den Rijn, p. 930.

<sup>74</sup> Council Directive (EU) 2016/1164 of 12 July 2016, laying down rules against tax avoidance practices that directly affect the functioning of the internal market, [2016] OJ L 193, p. 1.

<sup>75</sup> While the Directive itself entered into force in August 2016, it only requires member states to transpose the GAAR into national law by 31 December 2018, resulting in the effective application of the GAAR to taxpayers as of 1 January 2019. However, some member states obviously consider that their existing domestic rules already reflect art. 6 ATAD, so that no specific implementation is necessary (see, e.g. the branch reports for the Czech Republic and the Netherlands).

### 3.1.2 Scope

#### A. General

Article 6 ATAD is a real GAAR with a very broad application. The sole major limitation of its scope is that it only applies in the field of corporate taxation, excluding non-corporate income taxation.<sup>76</sup> This follows both from the scope of the ATAD as a whole, which defines its scope in article 1 with “all taxpayers that are subject to corporate tax in one or more member states”, and the further reference in article 6(1) to “corporate tax liability”. This seemingly arbitrary limitation<sup>77</sup> cannot be easily explained with the stated rationale for the ATAD to coordinate member states’ BEPS responses,<sup>78</sup> since BEPS recommendations (in particular the PPT clause) were not limited to corporations, or the additional goal to tackle aggressive tax planning in order to strengthen the internal market.<sup>79</sup> It is probably best explained by the historical development of the ATAD, which was originally proposed in December 2015 as a split-off from the wider corporate harmonisation project.<sup>80</sup>

It is notable in the context of EU tax legislation that the GAAR is not limited to cross-border arrangements, but equally tackles tax avoidance schemes that affect only one member state, potentially opening questions on the legitimacy of the exercise of EU competences.

#### B. Relationship to other anti-avoidance rules

##### (1) Relationship to TAARs and SAARs in EU Law

It is clear from the Directive’s context that article 6 is intended to fill in gaps left open by more targeted anti-abuse rules.<sup>81</sup> But this does not result in the inapplicability of article 6 ATAD in areas that are covered by more specific anti-abuse rules. It is uncertain whether article 6 can require the denial of a tax advantage in circumstances that fall within the scope of another TAAR found in EU legislation<sup>82</sup> or whether those more specific provisions decisively define the meaning of “abuse” within their field and leave no room for the

<sup>76</sup> However, if member states, when transposing art. 6 ATAD, make it applicable to other situations (e.g. individual income taxation), then the Court will, in principle, have competence to give an interpretation of EU law also in these cases if asked by a domestic court, so that also cases regarding individuals or other taxes could end up before the ECJ (see generally ECJ, 18 October 1990, C-297/88 and C-197/89, *Dzodzi*, EU:C:1990:360, paras 29 et seq., and specifically in the area of direct taxation ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369, paras 16 et seq., ECJ, 22 December 2008, C-48/07, *Les Vergers du Vieux Tauves*, EU:C:2008:758, paras 21 et seq., and ECJ, 4 June 2009, C-439/07 and C-499/07, *KBC Bank NV*, EU:C:2009:339, paras 55 et seq.).

<sup>77</sup> Critically, e.g., J. Hey, “Harmonisierung der Missbrauchsabwehr durch die ATAD”, 94 *Steuer und Wirtschaft* (2017), p. 248 (at p. 261).

<sup>78</sup> Recital 2 of the ATAD.

<sup>79</sup> Recital 3 of the ATAD.

<sup>80</sup> See the Report of the European Council on Tax Issues, Doc. 15187/15 FISC 187, ECOFIN 968 (9 December 2016), para. 27. On this development, in particular, see K. Kószeghy, “Corporate Tax Harmonisation: C(C)CTB 2.0?”, in W. Haslehner, G. Kofler and A. Rust (eds), *EU Tax Law and Policy in the 21st Century* (Kluwer Law International 2017), pp. 305-333. In this context, it is notable that the final wording of the GAAR matches the original proposal made by the Council in 2015 much closer than the subsequent Commission proposal – with the one exception of the limitation to corporate taxation of the provision’s scope. Compare art. 5 of the Council Proposal of 2 December 2015, Doc. 14544/15 FISC 171, with art. 7 of the Commission Proposal of 28 January 2016, COM (2016)26 final.

<sup>81</sup> See recital 11 of the ATAD.

<sup>82</sup> See further *infra* Chapter 3.2.

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application of article 6. “Filling the gaps” can be understood to mean gaps in the scope of other anti-abuse rules or, additionally, gaps in the strength of these rules. At the very least, however, gaps in the scope of existing GAARs are being filled by article 6: where member states have not yet created GAARs that have been modelled as opening clauses (e.g. in the MD and the IRD),<sup>83</sup> article 6 ATAD requires them to adopt such a GAAR.

With respect to SAARs, including the other ATAD rules, which are characterised by precisely defined conditions for their application, article 6 is less likely to have an impact, as its effect is constrained by the purpose-defining conditions of such SAAR. For example, if one considers a two-year holding period to be a SAAR to prevent access to a benefit for short-term investors, the GAAR cannot be used to deny a benefit to a taxpayer who held shares for two years and one day, even if the only reason for the taxpayer to keep the shares has been to avail itself of the tax benefit: the purpose of the relevant tax rule is precisely to deny the benefit *only* if the specific conditions for the SAAR’s application are fulfilled.<sup>84</sup> Granting the benefit after two years and one day thus cannot be seen as defeating the object or purpose of the relevant provision.

## *(2) Relationship to national law*

Article 3 ATAD specifies that the Directive does not preclude the application of provisions “aimed at safeguarding a higher level of protection for corporate tax bases”, clearly leaving scope for national (general and special) anti-abuse rules to be more restrictive of taxpayer freedom than article 6.<sup>85</sup>

National legislation further necessarily “colours” the meaning of abuse, since a condition for the application of a GAAR implementing article 6 is its defeating the “object or purpose of the applicable tax law”.<sup>86</sup> The reference is evidently to domestic (corporate) tax law.<sup>87</sup> It follows that a structure that may be abusive in one member state would not necessarily be viewed as abusive in every other member state, since the object or purpose of the national corporate tax law may differ. One member state may create corporate tax law that relies strongly on private law arrangements, while another’s corporate tax law may mostly work by reference to economic reality. The object or purpose with respect to a tax advantage in the first case may thus be to grant the advantage whenever the private law conditions are fulfilled; while, in the latter case, a tax advantage will only be legitimately obtained if the arrangement is economically the one that the law intends to benefit. In the former case, the

<sup>83</sup> See *infra* Chapter 3.2.

<sup>84</sup> Cf. F. Debelva and J. Luts, “The General Anti-Abuse Rule of the Parent-Subsidiary Directive”, 55 *European Taxation* (2015), p. 223 (at p. 232), who base this result generally on the *lex specialis* character of the SAAR.

<sup>85</sup> Whether such more restrictive rules would be compatible with primary EU law is another question. L. De Broe and D. Beckers doubt whether art. 3 can be deemed applicable to art. 6 since ECJ case law would not allow more stringent rules (“The General Anti-Abuse Rule of the Anti-Tax Avoidance Directive: An Analysis Against the Wider Perspective of the European Court of Justice’s Case Law on the Abuse of EU Law”, 26 *EC Tax Review* [2017], p. 133 [at p. 141]). As they point out, however, that case law only applies to cross-border situations, while art. 6 has a wider scope of application.

<sup>86</sup> See further *infra* Chapter 3.1.3.B.

<sup>87</sup> It is noted here in passing that there is a deviation from the original Commission proposal, which referred instead to “the applicable tax provisions”. The change came presumably in order to avoid confusion as to whether the relevant object or purpose is that of the provisions that the taxpayer relied on or the object and purpose of the provisions the taxpayer circumvented (and which are therefore arguably not “applicable” to the arrangement). On the question whether the relevant “object or purpose” is that of a certain (the applied/circumvented?) concrete tax provision or that of the corporate tax system as a whole, see *infra* Chapter 3.1.3.B.

arguable “non-genuineness” of the arrangement (the 3<sup>rd</sup> condition)<sup>88</sup> is irrelevant for the application of the GAAR because the tax advantage has been obtained in line with the laws object or purpose (the 2<sup>nd</sup> condition).<sup>89</sup>

Several member states appear to have taken the position that no legislative action will be required to implement article 6 since they already have domestic GAARs or equivalent judicial anti-abuse doctrines that are open to interpretation in line with the Directive in the future if they are not already at least as stringent as article 6.<sup>90</sup> As the concrete content of that provision is highly uncertain<sup>91</sup> – uncertainty that is a deliberate, if not necessary feature of a GAAR – and will remain so for years to come, until the ECJ has had the opportunity to rule on its application in concrete cases, the need for and extent of any legislative action will also remain debatable.

### 3.1.3 *Conditions*

#### A. *Introduction*

The application of article 6 ATAD requires the fulfilment of three main conditions: The first criterion, that there be an “arrangement or series of arrangements”, is rather trivial. The second is that such arrangement had the purpose of achieving a tax advantage that defeats the object or purpose of the applicable tax law. One may consider this the “subjective” element of the GAAR. The third is that the arrangement or series thereof are non-genuine, which could be described as the “objective” element of the GAAR.

#### B. *Arrangement or series of arrangements*

“Arrangements” is deliberately drafted to include all possible actions taken by a taxpayer. An explanation of the term can be seen in the Commission’s recommendation on aggressive tax planning, which defined the term as “any transaction, scheme, action, operation, agreement, grant, understanding, promise, undertaking or event”.<sup>92</sup> It should not be considered an actual entry-barrier to the application of a GAAR, but merely clarifies that the test of genuineness of a taxpayer’s actions is not confined to singular steps, but may require a broader view.

#### C. *Defeating object or purpose*

The second condition appears to be divided into three separate elements: (1) the taxpayer’s purpose, (2) the tax advantage and (3) the object or purpose of the applicable tax law. While the first is a “subjective” element, the condition overall is more accurately described as an “objective” one, since the main part of that condition is not the taxpayer’s

<sup>88</sup> See *infra* Chapter 3.1.3.C.

<sup>89</sup> See *infra* Chapter 3.1.3.B.

<sup>90</sup> E.g. Luxembourg’s legislative advisory council (*Conseil d’Etat*) took that position already in the legislative process of adopting the – virtually identically worded – TAAR in Directive 2015/121/EU, which amended the Parent-Subsidiary Directive by including a minimum abuse standard (see *infra* Chapter 3.B). See also D. Gutmann et al, “The Impact of the ATAD on Domestic Systems: A Comparative Survey”, 57 European Taxation (2017), pp. 2 (at pp. 9 et seq.).

<sup>91</sup> See further concerning the conditions and consequences of art. 6 *infra* Chapters 3.1.3. and 3.1.5.

<sup>92</sup> Commission Recommendation of 6 December 2012 on aggressive tax planning, C(2012)8806 final.

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purpose, but the object or purpose of the national tax law, which is an objective criterion.<sup>93</sup>

The first element refers to the taxpayer's "main purpose or one of the main purposes" of obtaining a tax advantage. This could be a fairly low threshold to pass, as it only definitely excludes situations in which obtaining a "tax advantage" was merely incidental in the mind of the taxpayer. It seems moot to enter into a deep exploration of what "a main purpose" is in practice, however: If an arrangement is devoid of valid economic reasons (the 3<sup>rd</sup> condition) and were to obtain a tax advantage that defeats the law's object or purpose (the main element of the 2<sup>nd</sup> condition), then it would be implausible to argue that such an arrangement would not have, at least as one of its main purposes, the obtainment of such tax advantage. At the same time, protecting a taxpayer in such circumstances by granting the unintended tax advantage simply because the arrangement in question can be argued to have an additional purpose, next to achieving a tax advantage, appears frivolous.

The meaning of "tax advantage" could be more problematic, but it needs to be interpreted broadly as well: article 6 applies in the context of the calculation of corporate tax liability; any reduction in tax liability that stems from a taxpayer's arrangement relative to another more appropriate ("genuine") arrangement thus qualifies as a "tax advantage".

The third and most important element of the 2<sup>nd</sup> condition is also its most difficult to apply. Object and purpose of a law are notoriously difficult to determine. A few observations need to be made:

- Firstly, since article 6 refers to a tax advantage that defeats the "object or purpose" of the law, it is sufficient if either the object or the purpose is defeated. It would be no acceptable defence for a taxpayer to say that a claimed tax advantage may not be what the law intended (purpose), but clearly falls within the law's scope (object).
- Secondly, it is not entirely clear which object and purpose are to be assessed: those of the concrete provision – which could be either the provision that the taxpayer relies on (which would grant an advantage) or the provision that the tax administration relies on (which would deny that advantage) – or those of the corporate tax regime as a whole. The wording suggests the latter, in particular when read in the historical context of the change from the original Commission proposal, which referred to the object or purpose of the "otherwise applicable tax provisions". Yet the overall object or purpose of corporate tax law is probably too abstract and remote to allow the necessary analysis.<sup>94</sup>
- Thirdly, a problem arises when the object or purpose of the relevant law changes over time.<sup>95</sup> If an arrangement was put into place to achieve a tax advantage that is no longer in line with its "new" purpose, but was accepted under the law's "old" purpose, can the GAAR apply? The phrase "having been put into place" arguably establishes a link between the arrangement's creation and the purpose of the law, suggesting that the GAAR is

<sup>93</sup> The priority of the objective element of the applicable tax law's object and purpose is indicated both by the wording, which puts this element at the determinative end of the condition, and by reference to the explanation provided in Pt. 4.5 of the Commission Recommendation of 6 December 2012 on aggressive tax planning, C(2012)8806 final (noting that "the purpose of an arrangement or series of arrangements consists in avoiding taxation where, regardless of any subjective intentions of the taxpayer, it defeats the object, spirit and purpose of the tax provisions that would otherwise apply").

<sup>94</sup> Cf. K.-D. Drüen, "Missbrauch nach Art 6 der Anti-BEPS-Richtlinie", in S. Kirchmayr, G. Mayr, K. Hirschler and G. Kofler (eds.), *Anti-BEPS-Richtlinie: Konzernsteuerrecht im Umbruch?* (Linde Vienna, 2017), p. 75 (at p. 82).

<sup>95</sup> The EU Parent-Subsidiary Directive (PSD) may serve as an instructive example: Up until its amendment in 2014, its sole purpose was the prevention of double taxation; following the introduction of an anti-hybrid clause, its clear objective is now also to prevent double non-taxation.

confined to arrangements that defeated the law's purpose at the time of their creation. Another way of putting this is to say that the subjective test of the taxpayer's intentions necessarily needs to be fulfilled at the time of the creation of an arrangement. If the Union legislature had wanted to establish a requirement for a taxpayer to permanently re-examine its arrangements as to their continued appropriateness from a tax perspective, one would have expected it to have made that clear, e.g. by adding "or maintained" to the above-mentioned phrase.

#### D. Non-genuine arrangement

The third necessary condition for the application of article 6 is that the arrangement in question is "not genuine having regard to all relevant facts and circumstances". The term is defined in the second paragraph as referring to arrangements as "non-genuine to the extent that they are not put into place for *valid commercial reasons* which *reflect economic reality*". "Genuineness" thus depends on the economic reality of an arrangement, marking this condition out as an objective element of the GAAR. Therefore, it is tempting to understand non-genuineness as the equivalent to the artificiality test applied in the ECJ's consistent case law. This reading is supported by the Commission's original proposal for the Directive, which noted "the proposed GAAR is designed to *reflect the artificiality tests*" of the ECJ<sup>96</sup> and, in recital 11, explains that "the application of GAARs should be limited to arrangements that are '*wholly artificial (non-genuine)*'"<sup>97</sup>, suggesting the equivalence of the terms "non-genuine" and "wholly artificial". However, one cannot easily ignore the fact that the adopted directive did not retain the wording on which these arguments for equivalence are based. Ultimately, the interpretation will depend on whether the ECJ will continue to see "wholly artificial arrangements" as the threshold for the application of a presumption of abuse within the EU. The wording of the Directive certainly allows for such interpretation.

It is notable that article 6 considers the possibility of arrangements being only partially non-genuine. This follows from the use of the words "to the extent that" instead of "where", which is used, for instance, in article 7 to carve out CFCs with substantive economic activity. This will allow the application of the GAAR to situations that are not entirely artificial, but are so only in part: for instance, where a transaction between related parties is characterised by economic activity, but the price agreed between the parties is artificially inflated.

The reference to "valid commercial reasons" in order to delimit the term non-genuine is a further source of uncertainty. Firstly, it creates a confusing link between the condition of non-genuineness (the 3<sup>rd</sup> condition) and the "one of the main purposes" requirement (2<sup>nd</sup> condition).<sup>98</sup> Secondly, the reference to valid commercial reasons is coloured by the conditional phrase "which reflect economic reality". Presumably this means that the subjective reasons that the taxpayer defends should be reflected by the economic reality of the relevant arrangement. Taken together, this arguably results in a test of whether the taxpayer had "valid economic reasons" for the chosen arrangement.<sup>99</sup> The limits of this inquiry, especially in light of the fact that a taxpayer remains free to "choose the most tax efficient structure for its commercial affairs",<sup>100</sup> needs to be further defined. In particular, the

<sup>96</sup> Commission Proposal of 28 January 2016, COM(2016) 26 final, p. 9 (emphasis added).

<sup>97</sup> Commission Proposal of 28 January 2016, COM(2016) 26 final, recital 11 (emphasis added).

<sup>98</sup> See *supra* Chapter 3.1.3.C.

<sup>99</sup> This corresponds to the formulation in recital 11, which suggests the member state may "consider all valid economic reasons" in assessing whether an arrangement was "genuine".

<sup>100</sup> Recital 11 of the ATAD.

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question of the burden of proof is equally unresolved in article 6, as are the boundaries for second-guessing commercial decisions by the tax administration.

### 3.1.4 Relationship to primary law

Article 6 appears to stretch the limits of the ECJ's jurisprudence on the compatibility of assumptions of abuse against taxpayers exercising their rights under the TFEU. While the ECJ has generally limited the application of GAARs to "wholly artificial arrangements"<sup>101</sup> with the "sole",<sup>102</sup> "essential"<sup>103</sup> or "principal"<sup>104</sup> aim of tax avoidance,<sup>105</sup> article 6 requires EU member states to ignore arrangements where such avoidance is only "one of the main purposes", thereby establishing a stricter standard than may be allowed by primary EU law.<sup>106</sup> In this, the text of article 6 fully corresponds to the Council's proposal from December 2015. By contrast, the Commission proposal of 28 January 2016 had suggested confining the GAAR to situations where the "essential" purpose of an arrangement was the obtaining of an unintended tax advantage.

Does that mean that the GAAR goes beyond the standard set by ECJ case law? There is no clear answer to this question, but a few observations can be made:

Firstly, for reasons of the hierarchy of norms, it would appear that it is unable to do so, since the provisions of any directive need to comply with the fundamental freedoms as well. This means that article 6 ATAD needs to be interpreted in light of the relevant ECJ case law when implemented and applied by national tax administrations. It is true that the ECJ does not directly test national legislation against primary EU law if it is based on fully harmonising secondary EU law,<sup>107</sup> however, the condition of "exhaustive harmonisation" of an area for that exclusion of primary EU law – as the immediate yardstick – is, in our view, not (yet) fulfilled.<sup>108</sup> Furthermore, the ECJ would still interpret the provisions of the Directive in light of primary EU law, even if the national provision was not itself directly measured against it. Even so, it is likely that the ECJ would assign the EU legislature greater latitude in designing anti-abuse provisions than member states, in light of the lower risk of fragmentation connected with such legislation.

<sup>101</sup> ECJ (Grand Chamber), 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 51.

<sup>102</sup> ECJ (Grand Chamber), 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 61 ("... wholly artificial arrangement *solely for tax purposes*") (emphasis added).

<sup>103</sup> ECJ (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:121, para. 75.

<sup>104</sup> ECJ, 21 February 2008, C-425/06, *Part Service*, EU:C:2008:108, para. 45.

<sup>105</sup> See also *supra* Chapter 2.

<sup>106</sup> Note, however, that the ECJ also refers to "one of the main purposes" in the context of the subjective element of determining an abusive situation in ECJ (Grand Chamber), 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 62. For further discussion of this point, see, e.g., D. Weber, "The New Common Minimum Anti-Abuse Rule in the EU Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect", 44 *Intertax* (2016), pp. 98 et seq.; A. P. Dourado, "Aggressive Tax Planning in EU Law and in the Light of BEPS: The EC Recommendation on Aggressive Tax Planning and BEPS Actions 2 and 6", 43 *Intertax* (2015), pp. 42 et seq.

<sup>107</sup> ECJ, 12 November 2015, C-198/14, *Visnapuu*, EU:C:2015:751, para. 40; ECJ, 8 March 2017, C-14/16, *Euro Park Service*, EU:C:2017:177, para. 19; ECJ, 7 September 2017, C-6/16, *Egiom SAS*, EU:C:2017:641, paras. 15-18; ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, paras 45-46.

<sup>108</sup> For a potentially different view see L. De Broe and D. Beckers, "The General Anti-Abuse Rule of the Anti-Tax Avoidance Directive: An Analysis Against the Wider Perspective of the European Court of Justice's Case Law on Abuse of EU Law", 26 *EC Tax Review* (2017), p. 133 (at p. 142).

Secondly, the change from the Commission proposal is not so definitive as to clearly mark out a deviation from the Commission's intent to confine the application of article 6 ATAD (article 7 in that proposal) to wholly artificial arrangements. As pointed out above, that condition was apparent from recital 9, which noted that "[w]ithin the Union, the application of GAARs should be limited to arrangements that are 'wholly artificial' (non-genuine)". It is clear from this that the use of the term "non-genuine" is understood by the Commission as a reflection of the "wholly artificial" standard set by the ECJ. Since the wording of the GAAR in its final version still confines its application to "non-genuine" arrangements, that standard would appear to be retained, irrespective of the seemingly lower threshold of "one of the main purposes" being the obtainment of an unintended tax advantage.

Thirdly, the fact that article 6 requires member states to adopt a GAAR that applies in a uniform manner "in domestic situations, within the Union and vis-à-vis third countries"<sup>109</sup> suggests that the ECJ's jurisprudence in the context of the fundamental freedoms – which is always preconditioned on a divergent application of an anti-abuse rule – may be of very limited relevance. However, to the extent that a member state's tax administration did apply the GAAR more strictly in a cross-border context (which article 6 – as a minimum standard – would allow), such a discriminatory approach could only be justified within the potentially narrower boundaries of said case law.<sup>110</sup>

### 3.1.5. Consequences

Article 6(3) ATAD prescribes two consequences of its application: Firstly, the non-genuine arrangements shall be "ignored".<sup>111</sup> Secondly, "the tax liability shall be calculated in accordance with national law".<sup>112</sup> It is unclear how the two parts relate to each other.<sup>113</sup> One could read it to mean that the consequences are up to the member state's national law, subject to the limit that such national law must not recognise the arrangement as the basis for taxation. Alternatively, the first element could be merely programmatic without constraining the member states' freedom to regulate the taxation consequences of an abusive arrangement.

In this context, another deviation from the Commission proposal is telling: The Commission had suggested that tax liability be "calculated by reference to economic substance in accordance with national law". Member states reverted to the wording of the Council's proposal, reportedly because some of them do not recognise a concept of "economic substance" in their national law.<sup>114</sup> While preserving more flexibility for the member states,

<sup>109</sup> Recital 11 of the ATAD.

<sup>110</sup> An interesting question is what would happen in the case of a member state that applied its GAAR too leniently in domestic situations and more strictly – in line with the wording of art. 6 – in cross-border situations, if such a case were to reach the ECJ questioning the harsher treatment's compatibility with the fundamental freedoms.

<sup>111</sup> Art. 6(1) and art. 6(3) ATAD.

<sup>112</sup> Art. 6(3) ATAD.

<sup>113</sup> Cf. L. De Broe and D. Beckers, "The General Anti-Abuse Rule of the Anti-Tax Avoidance Directive: An Analysis Against the Wider Perspective of the European Court of Justice's Case Law on Abuse of EU Law", 26 *EC Tax Review* (2017), p. 133 (at p. 143), who see a contradiction between the obligation to ignore the non-genuine arrangements and the right to calculate tax liability in accordance with national law.

<sup>114</sup> A. Rigaut, "Anti-Tax Avoidance Directive (2016/1164): New Policy Horizons", 56 *European Taxation* (2016), p. 497 (at p. 503).

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this does not seem to serve the goal of a uniform application of the anti-abuse concept across the EU. The Commission's wording would have made clear that member states could only apply their national law to the extent that it recognises such a concept. The wording adopted in the final version of article 6(3) results in (even) greater uncertainty.

### **3.2 General and specific anti-abuse reservations in the company tax directives**

#### **3.2.1 Introduction**

The Court's case law on the fundamental freedoms in cases such as *Cadbury Schweppes*<sup>115</sup> and *Thin Cap Group Litigation*<sup>116</sup> focuses on the potential justification of discriminatory domestic measures based on the grounds that they serve to counter abusive practices. The issue is, however, quite different in the harmonised areas of direct taxation, especially with regard to the various anti-abuse provisions in the company tax directives. To curb improper use of the directives based on those anti-avoidance provisions, member states need to implement the respective obligation or exercise the respective authorisation of secondary EU law in domestic law.<sup>117</sup> The main issue, therefore, is whether such domestic implementing provisions comply with the standards set out in Union legislation.<sup>118</sup>

It should first be noted that all three company tax directives – the Parent-Subsidiary

<sup>115</sup> ECJ (Grand Chamber), 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544.

<sup>116</sup> ECJ (Grand Chamber), 13 March 2007, C-524/04, *Thin Cap Group Litigation*, EU:C:2007:161.

<sup>117</sup> However, the existence of a domestic general anti-abuse law or even an unwritten abuse of rights doctrine (e.g. *fraus legis* oder "substance-over-form") may suffice to "implement" the anti-abuse reservations of the company tax Directives. See ECJ, 5 July 2007, C-321/05, *Kofed*, EU:C:2007:408, paras. 44-46. While it is not entirely clear if member states, after *Cussens*, could instead rely on the general principle of prohibition of abuse to address the abusive use of the company tax Directives (see for VAT ECJ, 22 November 2017, C-251/16, *Cussens*, EU:C:2017:881, paras 25-44), AG Kokott has recently rejected the idea that non-implemented anti-avoidance provisions of the company tax directives could be applied directly by member states (see the Opinions of AG Kokott of 1 March 2018 in Cases C-115/16, *N Luxembourg* 1, EU:C:2018:143, paras 98-113, C-116/16, *T Danmark*, EU:C:2018:144, paras 94-109, C-117/16, *Y Denmark*, EU:C:2018:145, paras 94-109, C-118/16, *X Denmark*, EU:C:2018:146, paras 108-123, C-119/16, *C Danmark* I, EU:C:2018:147, paras 96-111, and C-299/16, *Z Denmark*, EU:C:2018:148, paras 98-113).

<sup>118</sup> W. Schön, "Rechtsmissbrauch und Europäisches Steuerrecht", in: P. Kirchhof and H. Nieskens (eds.), *Festschrift für Wolfram Reiß* (Otto Schmidt Cologne, 2008), p. 571 (at p. 572).

Directive (PSD),<sup>119</sup> the Interest-Royalty Directive (IRD)<sup>120</sup> and the Merger Directive (MD)<sup>121</sup> – address specific issues relevant to the smooth functioning of the internal market in the tax area: In their respective scopes of application, the PSD eliminates juridical and economic double taxation of qualified cross-border inter-company profit distributions, the IRD likewise eliminates source taxation of qualified interest and royalty payments between connected enterprises, and the MD makes sure that certain cross-border reorganisations benefit from deferred taxation and the carry-over of tax assets. All these directives, however, contain a number of targeted provisions that address certain tax planning or policy concerns. For example, companies that are not subject to domestic corporate tax or that are exempt are excluded from the scope of the directives,<sup>122</sup> as are dual-resident companies that are treaty residents of a third country.<sup>123</sup> Moreover, both the PSD and the IRD enable member states to foresee a minimum holding period.<sup>124</sup> The PSD also (1) permits member states to choose the indirect credit method instead of exemption in order to avoid economic double taxation (and hence to address concerns regarding foreign low-taxation, e.g. through switch-over clauses), (2) addresses “hybrid financial instruments” by imposing an obligation on parent companies’ member states that have chosen the exemption method to tax profit distributions “to the extent that such profits are deductible by the subsidiary”,<sup>125</sup> and (3) permits member states to counteract double benefits (i.e. cost deduction and exemption of dividends).<sup>126</sup> The IRD moreover (1) requires that the recipient of the interest or royalty payment is also the “beneficial owner”<sup>127</sup> and (2) permits member states to exclude certain payments that might raise issues with regard to the delimitation between debt and equity,<sup>128</sup> and to not apply the withholding tax exemption to the excessive (non-arm’s length) portion of interest or royalty payments.<sup>129</sup>

<sup>119</sup> Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different member states (recast), [2011] OJ L 345, p. 8, as amended by Council Directive 2013/13/EU, [2013] OJ L 141, p. 30, Directive 2014/86/EU, [2014] OJ L 219/40, and Council Directive (EU) 2015/121 of 27 January 2015, [2015] OJ L 21, p. 1.

<sup>120</sup> Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different member states, [2003] OJ L 157, p. 49, as amended by Council Directive 2006/98/EC, [2005] OJ L 157, p. 203, and Council Directive 2013/13/EU, [2013] OJ L 141, p. 30. An amending proposal was presented by the Commission in late 2011, but has not yet been adopted (see COM(2011) 714 final [11 November 2011], and for the current state of discussions in Council “BEPs: Presidency roadmap on future work”, Dok. 10998/17 FISC157 (7 July 2017), paras 19 et seq.).

<sup>121</sup> Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different member states and to the transfer of the registered office of an SE or SCE between member states, [2009] OJ L 310/34, as amended by Council Directive 2013/13/EU, [2013] OJ L 141, p. 30.

<sup>122</sup> Art. 2(a)(iii) PSD, Art. 3(a)(ii) IRD and art. 3(c) MD. For the interpretation of these criteria in the PSD see, e.g. ECJ, 18 June 2009, C-303/07, *Aberdeen Property Fininvest Alpha*, EU:C:2009:377, para. 27, and ECJ, 8 March 2017, C-448/15, *Wereldhave*, EU:C:2017:180, paras 22 et seq., and for a recent analysis P. Arginelli, “The Subject-to-Tax Requirement in the EU Parent-Subsidiary Directive (2011/96)”, 57 *European Taxation* (2017), pp. 334-341.

<sup>123</sup> Art. 2(a)(ii) PSD, article 3(a)(ii) IRD and article 3(b) MD.

<sup>124</sup> See art. 3(2)(b) PSD and article 1(10) IRD. For the interpretation of this criterion in the PSD see, e.g. ECJ, 17 October 1996, C-283/94, C-291/94 and C-292/94, *Denkavit, VITIC, Voormeier*, EU:C:1996:387.

<sup>125</sup> See art. 4 of the PSD as amended by Directive 2014/86/EU of 8 July 2014, [2014] OJ L 219, p. 40.

<sup>126</sup> See art. 4(2) PSD and for a recent analysis ECJ, 26 October 2017, C-39/16, *Argenta Spaarbank NV*, EU:C:2017:813.

<sup>127</sup> Art. 1(1), (4) and (5) IRD.

<sup>128</sup> Art. 4(1) IRD.

<sup>129</sup> Art. 4(2) IRD.

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In addition, all three company tax directives contain more general anti-abuse rules, i.e. article 1(2) to (4) PSD, article 5 IRD and article 15(1)(a) MD. While since 2015 the PSD has contained a mandatory minimum standard of anti-abuse that member states have to apply, the IRD and the MD still merely authorise member states to counter abuse, i.e. they contain so-called “opening clauses” (however, the mandatory anti-abuse provision of article 6 GAAR might arguably also apply to those situations<sup>130</sup>). Those authorisations, however, may only be exercised in compliance with the fundamental provisions of the treaty, especially the fundamental freedoms.<sup>131</sup> Moreover, it seems that the idea of “wholly artificial arrangements” has also entered into the field of harmonised direct tax law as the standard of review.<sup>132</sup> Indeed, when it comes to distinguishing permissible tax planning and “abuse” within the field of direct tax directives, the Court has referred to *Halifax*<sup>133</sup> and *Cadbury Schweppes*<sup>134</sup> and noted that the respective provision in the MD “reflects the general Community law principle that abuse of rights is prohibited. Individuals must not improperly or fraudulently take advantage of provisions of Community law. The application of Community legislation cannot be extended to cover abusive practices; that is to say, transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by Community law”.<sup>135</sup>

In any event, however, it is in the field of harmonised Union law where a prudent approach is required: As the Court has clearly established, “Community legislation must be certain and its application foreseeable by those subject to it” and that this requirement of legal certainty must be observed “all the more strictly in the case of rules liable to entail financial consequences, in order that those concerned may know precisely the extent of the obligations which they impose on them”.<sup>136</sup> Moreover, all three general anti-abuse rules in the company tax directives have a number of interpretative requirements in common:

- Firstly, it is only by way of exception and in specific cases that member states may refuse to apply or withdraw the benefit of all or any part of the provisions of a directive.<sup>137</sup> Anti-abuse rules must hence be subject to strict interpretation.<sup>138</sup> Also, generally, if a specific provision in a directive addresses a certain abuse concern (e.g. through a minimum holding period or the disallowance of certain deductions), then that also

<sup>130</sup> See *supra* Chapter 3.1.

<sup>131</sup> See ECJ, 8 March 2017, C-14/16, *Euro Park Service*, EU:C:2017:177, and ECJ, 7 September 2017, C-6/16, *Egiom SAS*, EU:C:2017:641; for specific clauses in direct tax directives, see also, e.g. ECJ, 18 September 2003, C-168/01, *Bosal*, EU:C:2003:479, para. 26; ECJ, 23 February 2006, C-471/04, *Keller Holding*, EU:C:2006:143, para. 45; ECJ, 12 December 2006, C-446/04, *FII Group Litigation*, EU:C:2006:774, para. 46; ECJ, 2 September 2015, C-386/14, *Groupe Steria*, EU:C:2015:524, para. 39.

<sup>132</sup> See, e.g. ECJ, 7 September 2017, C-6/16, *Egiom SAS*, EU:C:2017:641, para. 30.

<sup>133</sup> ECJ (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:121, paras 68 and 69.

<sup>134</sup> ECJ (Grand Chamber), 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 35.

<sup>135</sup> ECJ, 5 July 2007, C-321/05, *Kofod*, EU:C:2007:408, para. 38; see also, e.g., ECJ, 10 November 2011, C-126/10, *Foggia*, EU:C:2011:718, para. 50, and for the PSD, e.g. ECJ, 26 October 2017, C-39/16, *Argenta Spaarbank NV*, EU:C:2017:813, para. 60.

<sup>136</sup> See, e.g. ECJ (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:121, para. 72.

<sup>137</sup> ECJ, 5 July 2007, C-321/05, *Kofod*, EU:C:2007:408, para. 37; ECJ, 11 December 2008, C-285/07, A.T., EU:C:2008:705, para. 31; ECJ, 20 May 2010, C-352/08, *Zwijnenburg*, EU:C:2010:282, para. 45.

<sup>138</sup> See, e.g. ECJ, 20 May 2010, C-352/08, *Zwijnenburg*, EU:C:2010:282, para. 46; ECJ, 8 March 2017, C-14/16, *Euro Park Service*, EU:C:2017:177, para. 49; ECJ, 7 September 2017, C-6/16, *Egiom SAS*, EU:C:2017:641, para. 26; ECJ, 26 October 2017, C-39/16, *Argenta Spaarbank NV*, EU:C:2017:813, para. 51; ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, para. 59.

implies that domestic measures that target the same issue and go beyond those authorisations may not be justified based on a directive's more general anti-abuse provisions.<sup>139</sup>

- Secondly, a general presumption of fraud and abuse cannot justify a fiscal measure which compromises the objectives of a directive.<sup>140</sup> Consequently, in order to determine whether the planned operation has the objective of avoidance, the competent national authorities cannot confine themselves to applying predetermined general criteria, but must carry out a general examination of each particular case.<sup>141</sup> Such an examination must be open to judicial review.<sup>142</sup>
- Thirdly, the imposition of a general tax measure automatically excluding certain categories of taxpayers from the tax advantage, without the tax authorities being obliged to provide even *prima facie* evidence of fraud and abuse, would go further than is necessary to prevent fraud and abuse.<sup>143</sup>
- Fourthly, the principle of proportionality requires that tax advantages in the context of a company tax directive be denied to the taxpayer only insofar as necessary in order to prevent a threat of tax avoidance or to redress tax avoidance that has already occurred,<sup>144</sup> implying that the benefits of a directive may not be denied if the main purpose of a transaction (e.g. a merger) was to avoid a tax outside the scope of that directive (e.g. a domestic indirect tax).<sup>145</sup>

### 3.2.2 Parent-Subsidiary Directive

The original text of the Parent-Subsidiary-Directive already contained a general anti-abuse reservation in article 1(2), according to which “[t]his Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud

<sup>139</sup> See ECJ, 26 October 2017, C-39/16, *Argenta Spaarbank NV*, EU:C:2017:813, paras 62 and 63, where the Court dealt with art.r 4(2) PSD and noted that the domestic rule at issue was “contrary to [art. 4(2) PSD] in that it goes beyond the measures that the EU legislature held to be appropriate to avoid the abuse by parent companies resulting from the possibility of carrying out a double tax deduction” and that, hence, the general anti-abuse rule of (former) art. 1(2) PSD “must be interpreted as not authorising member states to apply a domestic provision [...] to the extent that that provision goes beyond what is necessary for the prevention of fraud and abuse”. For a more detailed discussion, see F. Debelva and J. Luts, “The General Anti-Abuse Rule of the Parent-Subsidiary Directive”, 55 *European Taxation* (2015), p. 223 (at p. 232).

<sup>140</sup> ECJ, 7 September 2017, C-6/16, *Eqiom SAS*, EU:C:2017:641, para. 31.

<sup>141</sup> ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369, para. 41; ECJ, 11 December 2008, C-285/07, A.T., EU:C:2008:705, para. 31; ECJ, 20 May 2010, C-352/08, *Zwijnenburg*, EU:C:2010:282, para. 44; ECJ, 10 November 2011, C-126/10, *Foggia*, EU:C:2011:718, para. 37; ECJ, 8 March 2017, C-14/16, *Euro Park Service*, EU:C:2017:177, para. 55; ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, para. 61.

<sup>142</sup> See, e.g., ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369, para. 41.

<sup>143</sup> See also ECJ, 8 March 2017, C-14/16, *Euro Park Service*, EU:C:2017:177, paras 55 and 56; ECJ, 7 September 2017, C-6/16, *Eqiom SAS*, EU:C:2017:641, para. 32; ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, paras 62 and 69-70.

<sup>144</sup> Opinion AGJ. Kokott, 16 July 2009, C-352/08, *Zwijnenburg*, EU:C:2009:483, para. 67.

<sup>145</sup> ECJ, 20 May 2010, C-352/08, *Zwijnenburg*, EU:C:2010:282, para. 54.

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or abuse".<sup>146</sup> Addressing both the member state of the subsidiary and that of the parent company, this clause makes reference to domestic and tax treaty rules that are "required" for the "prevention of fraud or abuse". It was also clear from this provision's wording that, whilst member states may take such measures, they are not compelled to do so.<sup>147</sup>

The Parent-Subsidiary-Directive, however, was the first (and, so far, only)<sup>148</sup> company tax directive that has undergone an overhaul of its anti-abuse provision. Following the EU's Action Plan to strengthen the fight against tax fraud and tax evasion, and its call for a review of anti-abuse provisions in EU legislation,<sup>149</sup> the Commission has proposed amending the PSD in order to introduce a mandatory minimum standard to counter abusive transactions, and the Council has adopted such a provision in 2014.<sup>150</sup> Currently, therefore, article 1

<sup>146</sup> The notion of "fraud" (and similarly "tax evasion"), likely only has declarative meaning, because in any event the benefits of a directive will not be available in cases of illegal activities. For a recent discussion for the oftentimes confusing terminology see, e.g. A. Cordewener, "Anti-Abuse Measures in the Area of Direct Taxation: Towards Converging Standards Under Treaty Freedoms and EU", 26 *EC Tax Review* (2017), pp. 60-66.

<sup>147</sup> For extensive analysis of (former) art. 1(2) see G. Kofler, *Mutter-Tochter-Richtlinie* (LexisNexis, 2011) art. 1 paras. 60-88.

<sup>148</sup> The new anti-abuse provision in the PSD will, however, be taken into consideration by the Council "in its future work on a possible anti-abuse provision to be included in [the IRD]." See Annex II in the political agreement in Dok. 16435/14 FISC 221 ECOFIN 1157 (5 December 2014).

<sup>149</sup> See Action 15 in the Communication from the Commission "An Action Plan to strengthen the fight against tax fraud and tax evasion", COM(2012)722 final (6 December 2012).

<sup>150</sup> See Council Directive (EU) 2015/121 of 27 January 2015, [2015] OJ L 21, p. 1, and for a detailed review of the legislative history, see D. Weber, "The New Common Minimum Anti-Abuse Rule in the EU Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect", 44 *Intertax* (2016), pp. 98 et seq., and O. Marres and I. de Groot, "The General Anti-Abuse Clause in the EU Parent-Subsidiary Directive", in: D. Weber (ed.), *EU Law and the Building of Global Supranational Tax Law: EU BEPS and State Aid* (IBFD Amsterdam, 2017), p. 225 (at pp. 225 et seq.).

contains a mandatory minimum anti-abuse standard in paragraphs 2 and 3,<sup>151</sup> while the previous optional anti-abuse reservation was slightly reworded and moved to paragraph 4:<sup>152</sup> “2. Member states shall not grant the benefits of this Directive to an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of this Directive, are not genuine having regard to all relevant facts and circumstances.

An arrangement may comprise more than one step or part.

3. For the purposes of paragraph 2, an arrangement or a series of arrangements shall be regarded as not genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality.

4. This Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of tax evasion, tax fraud or abuse.”

Article 1(2) and (3) aim to guarantee that the application of anti-abuse rules is proportionate and serves the specific purpose of tackling an arrangement or a series of arrangements

<sup>151</sup> The member states had to implement the new requirement into domestic laws by 31 December 2015, and some member states have done so through specific rules (see, e.g. the branch reports for Denmark and Luxembourg). Conversely, however, if member states have not implemented that requirement into domestic law, the traditional perspective is that the obligation imposed by the Directive does not have direct effect, but rather requires implementation in domestic law (art. 288(3) TFEU). This is because “direct effect” does not operate against individuals or companies, i.e. a member state may not invoke, against an individual or a company, a provision of a directive, the necessary implementation of which in national law has not yet taken place (see generally, e.g. ECJ, 26 February 1986, 152/84, *M. H. Marshall*, EU:C:1986:84, ECJ, 11 June 1987, Case 14/86, *Pretore di Salò*, EU:C:1987:275, para. 19), a perspective that the Court has also embraced with regard to the anti-abuse reservation in art. 15 MD (see ECJ, 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408, para. 42); There is yet also no clear guidance from the Court that this necessity of implementation of anti-abuse rules in the company tax Directives is obsolete based on a general principle of EU law that abusive practices are prohibited (see, however, for the area of VAT ECJ, 22 November 2017, C-251/16, *Cussens*, EU:C:2017:881, paras. 25-44), but AG Kokott has recently rejected the idea that non-implemented anti-avoidance provisions of the company tax directives could be applied directly by member states (see the Opinions of AG Kokott of 1 March 2018 in Cases C-115/16, *N Luxembourg* 1, EU:C:2018:143, paras 98-113, C-116/16, *T Denmark*, EU:C:2018:144, paras 94-109, C-117/16, *Y Denmark*, EU:C:2018:145, paras 94-109, C-118/16, *X Denmark*, EU:C:2018:146, paras 108-123, C-119/16, *C Denmark* 1, EU:C:2018:147, paras 96-111, and C-299/16, *Z Denmark*, EU:C:2018:148, paras 98-113). In any event, the obligation to interpret national law in accordance with EU law (e.g. an existing domestic GAAR) also exists where the result prescribed is not favourable to the individual or company, so that an interpretative inverse vertical direct effect may be created (see, e.g. ECJ, 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408, para. 45). Once implemented into domestic law, however, it is argued that articles 1(2) and (3) PSD will “override” (pre-existing and new) tax treaty provisions that would be more beneficial for taxpayers (so, e.g. D. Weber, “The New Common Minimum Anti-Abuse Rule in the EU Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect”, 44 *Intertax* (2016), pp. 98 [at pp. 104-105], and O. Marres and I. de Groot, “The General Anti-Abuse Clause in the EU Parent-Subsidiary Directive”, in: D. Weber (ed.), *EU Law and the Building of Global Supra-national Tax Law: EU BEPS and State Aid* [IBFD Amsterdam, 2017], p. 225 [at pp. 243-245]; contra, e.g. F. Debela and J. Luts, “The General Anti-Abuse Rule of the Parent-Subsidiary Directive”, 55 *European Taxation* (2015), p. 223 [at p. 231-232], based, *inter alia*, on the wording of article 1(2), which only refers to the benefits of “this” Directive).

<sup>152</sup> It is, however, disputed which domestic anti-abuse provisions would be permissible under art. 1(4) PSD and whether those could be further-reaching than art. 1(2) PSD (so that the latter provision would indeed only be a minimum standard) or whether they could only be limited to other, say, more specific situations (e.g. targeted anti-abuse rules for certain transactions). See for that discussion, with a strong preference for the latter interpretation, e.g. D. Weber, “The New Common Minimum Anti-Abuse Rule in the EU Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect”, 44 *Intertax* (2016), pp. 98 (at pp. 101-103).

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which are not genuine, i.e. which do not reflect economic reality.<sup>153</sup> From a policy perspective, the provision's aim was to "make it obligatory for member states to adopt the common anti-abuse rule" (in light of the diverging approaches and the fact that some member states do not have any domestic or agreement-based provisions for the prevention of abuse), to achieve a common standard for anti-abuse provisions against the abuse of the PSD that "will ensure clarity and certainty for all taxpayers and tax administrations" and to guarantee "an equal application of the EU Directive without possibilities for 'directive-shopping' (i.e. to avoid that companies invest through intermediaries in member states where the anti-abuse provision is less stringent or where there is no rule)".<sup>154</sup> Nevertheless, a number of uncertainties arise with regard to each of its tests, i.e. that

- the main purpose or one of the main purposes of the arrangement is to obtain a tax advantage ("main purpose test"),
- the tax advantage defeats the object or purpose of the Directive ("object or purpose of the Directive test"), and
- the arrangement is not genuine having regard to all relevant facts and circumstances ("genuineness test"), i.e. that there are no valid commercial reasons which reflect economic reality for the arrangement ("commercial reasons test").

The general framework and each single component of article 1(2) and (3) are intensely discussed in literature and opinions vary widely,<sup>155</sup> also with regard to the remaining leeway for member states to enact anti-abuse provisions and potential conflicts of the Directive's article 1(2) and (3) and domestic implementing rules with the fundamental freedoms, e.g. where the application results in a discriminatory withholding taxation of cross-border dividends.<sup>156</sup> The wording of article 1(2) and (3) takes clear inspiration from the Court's case law<sup>157</sup> (but also deviates from it<sup>158</sup>) and the Commission's recommendation on aggressive tax planning,<sup>159</sup> but leaves ample room for interpretation. Since it is nearly identical to article 6 ATAD<sup>160</sup> and has certain similarities to the recently introduced "principal purposes test"

<sup>153</sup> Recital 6 of the Preamble of Council Directive (EU) 2015/121 of 27 January 2015, [2015] OJ L 21, p. 1.

<sup>154</sup> See the explanation in the Commission's Proposal for a Council Directive amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different member states, COM(2013) 814 final (25 November 2013).

<sup>155</sup> See, e.g., F. Debelva and J. Luts, "The General Anti-Abuse Rule of the Parent-Subsidiary Directive", 55 *European Taxation* (2015), pp. 223-234; R. J. S. Tavares and B. N. Bogenschneider, "The New De Minimis Anti-abuse Rule in the Parent-Subsidiary Directive: Validating EU Tax Competition and Corporate Tax Avoidance", 43 *Intertax* (2015), pp. 484-494; D. Weber, "The New Common Minimum Anti-Abuse Rule in the EU Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect", 44 *Intertax* (2016), pp. 98-129; C. Brokelind, "Legal Issues in Respect of the Changes to the Parent-Subsidiary Directive as a Follow-Up of the BEPS Project", 43 *Intertax* (2017), pp. 816-824; O. Marres and I. de Groot, "The General Anti-Abuse Clause in the EU Parent-Subsidiary Directive", in: D. Weber (ed.), *EU Law and the Building of Global Supranational Tax Law: EU BEPS and State Aid* (IBFD Amsterdam, 2017), p. 225 (at pp. 229 et seq.).

<sup>156</sup> For a brief discussion, see F. Debelva and J. Luts, "The General Anti-Abuse Rule of the Parent-Subsidiary Directive", 55 *European Taxation* (2015), p. 223 (at pp. 228-230) (assuming that's art. 1(2) and (3) comply with primary law, but that domestic implementing provisions must also comply with the fundamental freedoms).

<sup>157</sup> See, e.g. *supra* Chapter 2.

<sup>158</sup> See for detailed analysis, e.g. L. De Broe and D. Beckers, "The General Anti-Abuse Rule of the Anti-Tax Avoidance Directive: An Analysis Against the Wider Perspective of the European Court of Justice's Case Law on Abuse of EU Law", 26 *EC Tax Review* (2017), pp. 133-144.

<sup>159</sup> Commission Recommendation of 6.12.2012 on aggressive tax planning, C(2012)8806 final.

<sup>160</sup> See *supra* Chapter 3.1.

(PPT) of article 29 OECD MC, interpretative guidelines might be derived from the interpretation and application of those provisions.<sup>161</sup> While, however, article 29 OECD MC seems to focus on the perspective of the state ("benefit"), article 1(2) PSD arguably targets only situations in which the taxpayer obtains an overall "tax advantage", taking into account the tax position in all relevant member states (e.g. if the "benefit" of a lower withholding tax in one member state would be offset by a lower tax credit in the other member state). Conversely a "tax advantage" is not obtained if the "genuine" arrangement, e.g. direct ownership, would have triggered the same (low) tax burden in the source State.<sup>162</sup>

Certainly, the main (but not only)<sup>163</sup> focus of that provision is the perspective of the subsidiary's state of residence and its claim to tax outbound dividends,<sup>164</sup> i.e. the phenomenon of "directive shopping". Such "directive shopping" includes the interposition of a qualified EU company to trigger the application of the directive with the aim of eliminating withholding taxation of dividends that indirectly benefit non-qualified persons (e.g. individuals, non-qualified EU parent companies or third-country parent companies).<sup>165</sup> However, the mere fact that the ultimate shareholder is not a qualified company does not make an arrangement "not genuine" or "artificial".<sup>166</sup> Indeed, the ECJ in *Cadbury Schweppes* has relied on an evaluation of objective factors, in particular evidence of physical existence in terms of premises, staff and equipment that reflects economic reality, i.e. an actual establishment carrying on genuine economic activities and not a mere "letterbox" or "front" subsidiary.<sup>167</sup> The Commission, moreover, noted that "objective factors for determining whether there is adequate substance include such verifiable criteria as the effective place of management and tangible presence of the establishment, as well as the real commercial risk assumed by

<sup>161</sup> For art. 6 GAAR, see *supra* Chapter 3.1 and, e.g. L. De Broe and D. Beckers, "The General Anti-Abuse Rule of the Anti-Tax Avoidance Directive: An Analysis Against the Wider Perspective of the European Court of Justice's Case Law on Abuse of EU Law", 26 *ECTax Review* (2017), pp. 133–144, and for the wording and discussion of the PPT, see OECD/G20 Base Erosion and Profit Shifting Project, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances – Action 6: 2015 Final Report* (OECD Paris, 2015).

<sup>162</sup> See Opinion AG Kokott, 19 January 2017, C-6/16, *Egiom*, EU:C:2017:34, para. 26 with footnote 14, where a holding of a French subsidiary not through an interposed EU company but rather directly by the Swiss parent would likewise not have triggered a withholding tax because of art. 15 of the EU-Swiss Agreement, [2004] OJ L 385, p. 30 (now art. 9 of the EU-Swiss Agreement, [2015] OJ L 333, p. 12]).

<sup>163</sup> The Commission, however, might have taken a narrower perspective when it confirmed "that the proposed amendments to art. 1, paragraph 2 of the Parent Subsidiary directive are not intended to affect national participation exemption systems in so far as these are compatible with the Treaty provisions". See Annex III in the political agreement in Dok. 16435/14 FISC 221 ECOFIN 1157 (5 December 2014). See, for analysis, also D. Weber, "The New Common Minimum Anti-Abuse Rule in the EU Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect", 44 *Intertax* (2016), p. 98 (at pp. 107–108), and O. Marres and I. de Groot, "The General Anti-Abuse Clause in the EU Parent-Subsidiary Directive", in: D. Weber (ed.), *EU Law and the Building of Global Supranational Tax Law: EU BEPS and State Aid* (IBFD Amsterdam, 2017), p. 225 (at pp. 240–242).

<sup>164</sup> See also example 1 in the Commission's MEMO/15/4609 (23 November 2013).

<sup>165</sup> For a continuum of situations with regard to the interposition of an intermediate holding company, see R. J. S. Tavares and B. N. Bogenschneider, "The New De Minimis Anti-Abuse Rule in the Parent-Subsidiary Directive: Validating EU Tax Competition and Corporate Tax Avoidance", 43 *Intertax* (2015), p. 484 (pp. 487–488).

<sup>166</sup> See instructively ECJ, 7 September 2017, C-6/16, *Egiom SAS*, EU:C:2017:641

<sup>167</sup> See *supra* chapter 2 and ECJ (Grand Chamber), 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para. 68; see also, e.g. L. De Broe, *International Tax Planning and Prevention of Abuse* (IBFD Amsterdam, 2007), pp. 1014 et seq.

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it”,<sup>168</sup> but likewise admitted that “it is not altogether certain how those criteria may apply in respect of, for example, intra-group financial services and holding companies whose activities generally do not require a significant physical presence”.<sup>169</sup> Also, the mere existence of “substance” (e.g. office space, employees) in itself is likely not sufficient to exclude abuse if it does not bear a relation to the income in question.<sup>170</sup>

It will eventually be for the Court’s case law to undertake this complicated line-drawing. Although some cases are still pending before the Court,<sup>171</sup> there is already some clarity as to the interpretation of (former) article 1(2) (now article 1(4)) with regard to the Directive’s exemption from withholding taxation (article 5) in *Eqiom*<sup>172</sup> and *Deister Holding and Juhler Holding*.<sup>173</sup>

- *Eqiom* concerned a French rule that denied the withholding tax exemption of dividends if the non-resident parent company is controlled directly or indirectly by one or more residents of States that are not members of the Union, unless the parent company provides proof that the principal purpose or one of the principal purposes of the chain of interests is not to benefit from the exemption. Focusing on article 1(2), the Court inquired whether national tax legislation, “satisfies that requirement of necessity”,<sup>174</sup> and noted – referring to *Cadbury Schweppes*<sup>175</sup> and *SIAT*<sup>176</sup> – that “in order for national legislation to be regarded as seeking to prevent tax evasion and abuses, its specific objective must be to prevent conduct involving the creation of wholly artificial arrangements which do not reflect economic reality, the purpose of which is unduly to obtain a tax advantage”.<sup>177</sup> Employing a narrow interpretation of article 1(2), rejecting a general presumption of

<sup>168</sup> One might indeed wonder if the place of management of a company alone is sufficient to defeat the notion of artificiality. See, e.g. W. Schön, “Rechtsmissbrauch und Europäisches Steuerrecht”, in: P. Kirchhof and H. Nieskens (eds.), *Festschrift für Wolfram Reiß* (Otto Schmidt Cologne, 2008), p. 571 (at pp. 587 et seq.).

<sup>169</sup> Commission’s Communication on “The application of anti-abuse measures in the area of direct taxation – within the EU and in relation to third countries”, COM(2007)785, p. 4.

<sup>170</sup> See, in that direction, the Council Resolution of 8 June 2010 on the coordination of the Controlled Foreign Corporation (CFC) and thin capitalisation rules within the European Union, [2010] OJ C 156, p. 1, noting as one potential indicator that suggests that profits may have been artificially diverted to a CFC that “there is no proportionate correlation between the activities apparently carried on by the CFC and the extent to which it physically exists in terms of premises, staff and equipment”. See also Opinion AG Kokott, 19 January 2017, C-6/16, *Eqiom*, EU:C:2017:34, para. 26, noting that “even where there is a physical presence, one might conclude, in light of the financial and staffing set-up, that the arrangement is artificial. In this regard, what appears to be relevant is, for instance, the actual authority of the company organs to take decisions, to what extent the company is endowed with its own financial means and whether any commercial risk exists.”

<sup>171</sup> One pending case concerns the German anti-abuse provision in § 50d(3) EStG: See C-440/17, GS (referred to by the Finanzgericht Köln, 17 May 2017, 2 K 773/16). See also the pending case C-116/16, *T Dammark*, on the relationship between former art. 1(2) and the “beneficial ownership” concept in tax treaties. For a contextual analysis of these references see A. Cordewener, “Anti-Abuse Measures in the Area of Direct Taxation: Towards Converging Standards Under Treaty Freedoms and EU”, 26 EC Tax Review (2017), pp. 60-66.

<sup>172</sup> See ECJ, 7 September 2017, C-6/16, *Eqiom SAS*, EU:C:2017:641, and for detailed discussion, e.g. C. Brokelind, “Anti-Directive Shopping on Outbound Dividends in Light of the Pending Decision in Holcim France (Case C-6/16)”, 56 European Taxation (2016), pp. 394-399.

<sup>173</sup> ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009.

<sup>174</sup> For the (irrelevance) of the lack of the German language version of art. 1(2) PSD see ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, paras 54 et seq.

<sup>175</sup> ECJ (Grand Chamber), 12 September 2006, C-196/04, *Cadbury Schweppes*, EU:C:2006:544, para 55.

<sup>176</sup> ECJ, 5 July 2012, C-318/10, *SIAT*, EU:C:2012:415, para. 40.

<sup>177</sup> ECJ, 7 September 2017, C-6/16, *Eqiom SAS*, EU:C:2017:641, para. 30.

fraud and abuse, and noting that the mere fact that a company residing in the EU is directly or indirectly controlled by residents of third States does not imply a purely artificial arrangement, the Court eventually found that the French rule at issue in *Eqiom* was not in line with article 1(2) PSD.

- Likewise, in *Deister Holding and Juhler Holding*, the Court followed that reasoning with regard to the German denial of withholding tax exemption that was based on (foreign) ownership of the parent company and the failure to meet one of three objective tests, i.e. economic and substantial reasons for the involvement of that company, a 10 per cent gross-income threshold relating to own economic activity and partaking in general economic commerce. However, such a rule violated articles 1(2) and 5 PSD on the basis that, firstly, foreign ownership of the parent company does not indicate the existence of a wholly artificial arrangement, secondly, the objective tests amount to a general (and irrebuttable) presumption of fraud or abuse and, thirdly, the conditions of those tests (cumulatively and alternatively) cannot *per se* imply the existence of fraud or abuse.<sup>178</sup> The Court also clarified that the Directive does not establish any requirements with regard to the nature of the economic activities of qualified companies nor to the amount of turnover resulting from those companies' own economic activity. Moreover, “[t]he fact that the economic activity of a non-resident parent company consists in the management of its subsidiaries' assets or that the income of that company results only from such management cannot *per se* indicate the existence of a wholly artificial arrangement which does not reflect economic reality”.<sup>179</sup> Finally, German legislation also failed the directive's standard because it did not provide for an overall assessment, on a case-by-case basis, of the relevant situation based on factors that include the organisational, economic or other substantial features of the group of companies to which the parent company in question belongs, and the structures and strategies of that group.<sup>180</sup>

The judgments in *Eqiom* and *Deister Holding and Juhler Holding* have also demonstrated that domestic measures relying on that provision must not only comply with that provision, i.e. the abuse standard of the PSD, but they may also be assessed in the light of the fundamental freedoms (as it does not carry out exhaustive harmonisation<sup>181</sup>). Indeed, in the concrete cases, the French and German rules also violated the freedom of establishment, with the Court explicitly noting that “the objective of combating fraud and tax evasion, whether it is relied on under article 1(2) of the Parent-Subsidiary Directive or as justification for an exception to primary law, has the same scope. Therefore, the findings [with regard to article 1(2) PSD] also apply with regard to that freedom”.<sup>182</sup>

<sup>178</sup> ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, paras 64-71.

<sup>179</sup> ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, paras 72-73.

<sup>180</sup> ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, para. 74.

<sup>181</sup> According to settled case-law, any national measure in an area which has been the subject of exhaustive harmonisation at the level of the European Union must be assessed in the light of the provisions of that harmonising measure, and not in the light of the provisions of primary law (ECJ, 12 November 2015, C-198/14, *Visnapuu*, EU:C:2015:751, para. 40; ECJ, 8 March 2017, *Euro Park Service*, C-14/16, EU:C:2017:177, para. 19; ECJ, 7 September 2017, C-6/16, *Eqiom SAS*, EU:C:2017:641, paras. 15-18; ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, paras 45-46).

<sup>182</sup> ECJ, 7 September 2017, C-6/16, *Eqiom SAS*, EU:C:2017:641, para. 64; see also ECJ, 20 December 2017, C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, EU:C:2017:1009, para. 97.

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### 3.2.3 Merger Directive

Article 15(1)(a) MD allows member states to refuse to apply or withdraw the benefit of all or part of the provisions of that Directive only in such circumstances where the operation coming within its scope (e.g. a cross-border merger) has as its principal objective or one of its principal objectives tax evasion or tax avoidance.<sup>183</sup> That provision reads:

“1. A Member state may refuse to apply or withdraw the benefit of all or any part of the provisions of Articles 4 to 14 where it appears that one of the operations referred to in Article 1:

(a) has as its principal objective or as one of its principal objectives tax evasion or tax avoidance; the fact that the operation is not carried out for valid commercial reasons, such as the restructuring or rationalisation of the activities of the companies participating in the operation, may constitute a presumption that the operation has tax evasion or tax avoidance as its principal objective or as one of its principal objectives;”

In doing so, article 15(1)(a) MD permits member states to provide for a presumption of tax evasion or tax avoidance in cases where the “operation has the sole objective of obtaining a tax advantage and is thus not carried out for valid commercial reasons”,<sup>184</sup> the latter including “the restructuring or rationalisation of the activities of the companies participating in the operation”.<sup>185</sup> Conversely, the concept of “valid commercial reasons” as explicitly used in article 15(1)(a) MD “is a concept involving more than the attainment of a purely fiscal advantage” so that, for example, a “merger by way of exchange of shares, having only such an aim, cannot therefore constitute a valid commercial reason within the meaning of that article”.<sup>186</sup> However, “a merger operation based on several objectives, which may also include tax considerations, can constitute a valid commercial reason provided, however, that those considerations are not predominant in the context of the proposed transaction”.<sup>187</sup> Such an assessment may require weighing the magnitude of the anticipated tax benefit relative to the effect of valid commercial reasons (e.g. reduction of administrative and management costs), where the latter may not only be “marginal”.<sup>188</sup> To date, the Court has accepted the application of article 15(1)(a) MD, e.g. when a reorganisation took place for the sole purpose of loss utilisation;<sup>189</sup> in the case of a merger operation between two companies of the same group, when the acquired company does not carry out any activity, did not have any financial holdings and transfers to the acquiring company only substantial tax losses of undeter-

<sup>183</sup> See, e.g., ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369, para. 38; ECJ, 8 March 2017, C-14/16, *Euro Park Service*, EU:C:2017:177, para. 22.

<sup>184</sup> See ECJ, 8 March 2017, C-14/16, *Euro Park Service*, EU:C:2017:177, para. 23 and 53; see also ECJ, 10 November 2011, C-126/10, *Foggia*, EU:C:2011:718, para. 36 (“sole aim of obtaining a tax advantage”), and ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369, para. 45.

<sup>185</sup> See also, e.g., ECJ, 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408, para. 37.

<sup>186</sup> ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369, paras. 40 and 47. For a possibly different position with regard to the fundamental freedoms, see, e.g. the Commission’s Communication on “The application of anti-abuse measures in the area of direct taxation – within the EU and in relation to third countries”, COM(2007)785, p.3, where the Commission argues that minimising the tax burden is in itself a valid commercial consideration, as long as the arrangements entered into with a view to achieving it do not amount to artificial transfers of profits.

<sup>187</sup> ECJ, 10 November 2011, C-126/10, *Foggia*, EU:C:2011:718, para. 35.

<sup>188</sup> ECJ, 10 November 2011, C-126/10, *Foggia*, EU:C:2011:718, para. 47 (comparing an anticipated tax benefit of more than € 2 million with a “quite marginal” saving made by the group concerned in terms of cost structure).

<sup>189</sup> ECJ, 17 July 1997, C-28/95, *Leur-Bloem*, EU:C:1997:369.

mined origin;<sup>190</sup> and possibly when an exchange of shares was facilitated to enable a tax-exempt profit distribution.<sup>191</sup>

### 3.2.4 *Interest-Royalty Directive*

Article 5 IRD includes an anti-abuse provision that is quite similar to the ones found in the other company tax directives. Titled “Fraud and Abuse” it provides:

1. This Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud or abuse.
2. Member states may, in the case of transactions for which the principal motive or one of the principal motives is tax evasion, tax avoidance or abuse, withdraw the benefits of this Directive or refuse to apply this Directive.”

While there are currently no decisions of the ECJ on how to interpret that anti-avoidance provision, it is quite likely that the same standards that are applicable with regard to the PSD and the MD have to be applied, especially the exclusion of wholly artificial tax-avoidance arrangements used in order to benefit from the Directive’s withholding tax exemption. Indeed, article 5 IRD is focused on source State taxation, permitting member states to protect their withholding tax claim against abusive structures, especially in situations of “directive shopping” (e.g. the interposition of an EU company to gain benefits indirectly for third-country recipients, non-qualified EU recipients, or resident recipients). However, since the “beneficial owner” condition of article 1 “is specifically designed to tackle artificial conduit arrangements”, it may “be doubted whether a company that satisfied the ‘beneficial owner’ test could be considered an artificial conduit when applying article 5”.<sup>192</sup> A number of pending cases on the “beneficial ownership” requirement and the notion of “abuse” in article 5 IRD may bring clarity in this area.<sup>193</sup>

## 4. Conclusions and outlook

The questions surrounding the concept of tax avoidance, as well as the targeted efforts against it, are multiple and challenging to respond to, and this report has shown the levels and scope of anti-avoidance considerations in the EU tax area. From a policy perspective, a clear understanding of the meaning and scope of tax avoidance is necessary for the design

<sup>190</sup> ECJ, 10 November 2011, C-126/10, *Foggia*, EU:C:2011:718.

<sup>191</sup> ECJ, 5 July 2007, C-321/05, *Kofeoed*, EU:C:2007:408.

<sup>192</sup> See point 3.3.9 of the Report from the Commission to the Council in accordance with art. 8 of Council Directive 2003/49/EC on a common system of taxation applicable to interest and royalty payments made between associated companies of different member states, COM(2009)179, and for analysis G. Kofler and J. Lopez Rodriguez “Beneficial Ownership and EU Law”, in: M. Lang, P. Pistone, J. Schuch, C. Staringer and A. Storck (eds.), *Beneficial Ownership: Recent Trends* (IBFD Amsterdam, 2013), p. 215 (at pp. 229-230).

<sup>193</sup> Cases are pending before the ECJ as C-115/16, *N Luxembourg I*, C-118/16, *X Denmark*, C-119/16, *C Denmark I*, and C-299/16, *Z Denmark ApS*. In her opinions in those cases, AG Kokott argues, however, that the notion of “beneficial owner” in the IRD is to be interpreted autonomously and without recourse to the corresponding noting in tax treaties. See the Opinions of AG Kokott of 1 March 2018 in Cases C-115/16 (*N Luxembourg I*, EU:C:2018:143, paras 48-55), C-118/16 (*X Denmark*, EU:C:2018:146, paras 48-55), C-119/16 (*C Denmark I*, EU:C:2018:147, paras 48-55), and C-299/16 (*Z Denmark*, EU:C:2018:148, paras 48-55).

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of appropriate counter-measures, which are also relevant for the future of international taxation, economic growth and welfare. The OECD and the EU describe targeted tax avoidance or so-called “aggressive tax planning” as a conduct that (1) leads to minimisation/reduction of tax liability, (2) through an unreasonably broad interpretation of tax laws or exploitation of mismatches in the international tax framework, (3) without infringing (the letter of) the law.<sup>194</sup> Indeed, as evidenced in the national reports, national and international legislatures are employing a number of defences against this type of tax planning.

In addition to some more specific anti-abuse clauses in the company tax directives, the EU recently opted for a GAAR in its Anti-Tax-Avoidance Directive (ATAD), targeting arrangements whose main purpose is to obtain a tax advantage and that are not genuine as to economic substance and, moreover, that defeat the object or purpose of the applicable tax law. Similar concepts are found in the domestic laws of many member states, making reference to the broader concept of abuse of law.<sup>195</sup> Thus, where form does not reflect substance, an arrangement or transaction may be recharacterised or ignored. At the international level, the OECD Model Commentary now includes general rules to address treaty shopping, among them a “Principal Purposes Test” (PPT) and a “Limitation-on-Benefits” provision (LoB).<sup>196</sup> Specifically with regard to the PPT, however, the European Commission has recommended that the member states align the wording proposed by the OECD “with the case law of the Court of Justice of the European Union as regards the abuse of law” so that treaty benefits are also granted if the respective arrangement or transaction “reflects a genuine economic activity”.<sup>197</sup>

Notwithstanding their careful construction, the above measures raise concerns with regard to fundamental taxpayers’ rights, such as the right to legal certainty and the freedom to arrange one’s economic affairs. Indeed, there is an implied borderline between the letter of the law – that is followed – and what lies beyond such letter, the “spirit of the law” that is violated. This reliance on the spirit of the law seems, moreover, to be a more general trend. The OECD Guidelines for Multinational Enterprises, for example, contain a clear obligation for multinationals to comply with the spirit of tax law<sup>198</sup> and similar references can be found in national legal frameworks, e.g. the UK Code of Practice on Taxation for Banks.<sup>199</sup> This, of course, creates risks – commercial, reputational and others – for multinationals that fail to adhere to the call for incorporating compliance with the spirit of tax law in their public reports. Strong reliance on the evasive and oftentimes blurred “spirit of the law” (or its “object or purpose”), especially in light of different approaches used in various jurisdictions, might therefore put disproportionate burdens on taxpayers. In any case, proper safeguards should be put in place for taxpayers’ rights, e.g. through the fair allocation of the burden of proof and the implementation of drafting standards for tax legislation.

<sup>194</sup> OECD, “OECD: Work on Tax Avoidance and Evasion”, 8 *Intertax* (1980). pp. 9-16; European Commission, *Communication from the Commission to the European Parliament and the Council on tax transparency to fight tax evasion and avoidance*, COM (2015)136.

<sup>195</sup> See, e.g. C. Sallabank and N. André, *A Comparison Between the French Abuse of Law and the UK General Anti-Abuse Rule* (Mondaque, April 2014).

<sup>196</sup> See art. 29(1) to (7) and (9) of the OECD MC 2017 and art. 7 of the Multilateral Instrument (MLI), both based on OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances*, Action 6 – 2015 Final Report (2015).

<sup>197</sup> See point 2 of the Commission Recommendation (EU) 2016/136 of 28 January 2016 on the implementation of measures against tax treaty abuse, C(2016)271, [2016] OJ L 25, p. 67.

<sup>198</sup> OECD, *OECD Guidelines for Multinational Enterprises* (2017).

<sup>199</sup> UK HM Revenue and Customs, *Policy Paper Code of Practice on Taxation for Banks* (December 2013).



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