European Union

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Opinion Statement ECJ-TF 3/2022 on the EFTA Court Decision of 1 June 2022 in *PRA Group Europe* (Case E-3/21), on the Discriminatory Interaction between the "Interest Barrier" and Group Contributions

In this CFE Opinion Statement, the CFE ECJ Task Force comments on the EFTA Court decision of 1 June 2022 in *PRA Group Europe* (Case E-3/21), on the discriminatory interaction between the "interest barrier" and group contributions.

1. Introduction

This is an Opinion Statement prepared by the CFE ECJ Task Force on *PRA Group Europe* (Case E-3/21), in respect of which the EFTA Court delivered its decision on 1 June 2022.[1] At issue in *PRA Group Europe* was the interaction between the Norwegian "interest barrier rule" ("interest limitation rule"), which generally limits the deductibility of interest payments to affiliated resident and non-resident entities to 30% of EBITDA, and the group contribution rules, which permit tax effective transfers between group members, but are limited to Norwegian entities. As group contributions also increase the EBITDA of the recipient Norwegian entity (and decrease it at the level of the paying Norwegian entity), companies in the Norwegian tax group can achieve interest deductions under the interest barrier rules where profits ("tax EBITDA") and interest expenses are distributed unevenly between the companies in the group, while a similar opportunity to escape (or lessen the impact of) the interest barrier rules is not available to cross-border groups. The EFTA Court took a combined perspective on the interaction of these rules and found them to constitute an unjustified restriction of the freedom of establishment under articles 31 and 34 of the European Economic Area Agreement (1992).[2] The EFTA Court's decision is particularly interesting from an EU law perspective, as the interest barrier rule of article 4 of the EU Anti-Tax Avoidance Directive (2016/1164) (ATAD)[3] similarly foresees an option for Member States to introduce a domestically limited "interest barrier group" to permit a calculation of exceeding borrowing costs and the EBITDA at the local group level.

2. Background, Facts and Issues

OECD BEPS Action 4 addresses base erosion concerns relating to interest deductions and developed a best practice approach based on a fixed ratio rule,[4] capping interest deductions at a certain percentage of earnings before interest, taxes, depreciation and amortization (EBITDA). In the European Union, the ATAD built on the OECD's BEPS Project and introduced a (mandatory) "interest barrier rule" ("interest limitation rule") in its article 4, limiting the deduction of "exceeding borrowing costs" to 30% of EBITDA ("fixed-ratio rule"), generally focusing on each entity separately with certain escapes under the "group-ratio rules" that take into account how a local entity is leveraged in relation to the overall group (i.e. the

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1. NO: EFTA Court, 1 June 2022, Case E-3/21, *PRA Group Europe AS*. The decision and other documents pertaining to the case are available at https://eftacourt.int/cases/e-3-21/ (accessed 6 Jan. 2023).
2. Agreement on the European Economic Area, 2 May 1992, Primary Sources IBFD.
3. Council Directive 2016/1164 of 12 July 2016 Laying down Rules against Tax Avoidance Practices that Directly Affect the Functioning of the Internal Market, OJ L 193/1 (2016), Primary Sources IBFD [ATAD].
4. *See* OECD, *Limiting Base Erosion Involving Interest Deductions and Other Financial Payments – Action 4: 2015 Final Report* (5 Oct. 2015), Primary Sources IBFD [hereinafter *Action 4 Final Report*].

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"EBITDA escape" and the "equity escape"). The ATAD's interest barrier rule applies in "relation to a taxpayer's exceeding borrowing costs without distinction of whether the costs originate in debt taken out nationally, cross-border within the Union or with a third country, or whether they originate from third parties, associated enterprises or intra-group".[5]

The OECD has also addressed the question of whether a country should treat entities within a (tax) group as a single entity in applying the fixed and group ratio rules.[6] As the OECD notes in relation to multinational groups:[7]

> [w]here a group has more than one entity in a particular country, the country may apply the fixed ratio rule and group ratio rule to the position of each entity separately, or to the overall position of all group entities in the same country (i.e. the local group). Applying a rule to the overall position of the local group would avoid the scenario where a highly leveraged entity incurs an interest disallowance even though the interest expense of the local group as a whole falls within the limit permitted.

It is apparent that the OECD focuses on domestic groups ("the local group"), as, from a policy perspective, treating all group entities in a single state as one taxpayer does not give rise to profit shifting concerns, whereas extending that group perspective across the border would. Building on the OECD's recommendations, the ATAD gives the Member States the option ("may") to treat a group entity as the "taxpayer" for purposes of the interest barrier, whether or not the group results are otherwise consolidated. This means that the Member States can either newly define a "group" for purposes of the interest barrier rules (article 4(1)(a)) or defer to an existing group taxation regime (article 4(1)(b)). Where a group is treated as a taxpayer, "exceeding borrowing costs and the EBITDA may be calculated at the level of the group and comprise the results of all its members" (article 4(1) last sentence). While article 4(1) of the ATAD might not be entirely clear as to whether it is limited to domestic or also cross-border groups, the wording at least suggests that only group entities in the same country are being addressed (i.e. groups "as defined according to national tax law", which are typically limited to domestic entities), and the ATAD's Preamble makes it perfectly clear that this "interest barrier group" approach is limited to domestic entities in a single Member State:[8,9]

> Where a group includes more than one entity in a Member State, the Member State may consider the overall position of all group entities in the same State, including a separate entity taxation system to allow the transfer of profits or interest capacity between entities within a group, when applying rules that limit the deductibility of interest.

Treating a whole (domestic) group as a single taxpayer for purposes of the interest barrier and the corresponding calculation of exceeding borrowing costs and the EBITDA at the group level can offer several advantages for taxpayers (that can also go beyond the benefits of a group ratio rule): First, interest income and interest expenses of all group members are combined, which results in the neutralization of interest payments between group members for purposes of the interest barrier rule. Second, the EBITDAs of all group members are combined, which might increase the amount of deductible interest in a group-wide perspective in a given year (if, for example, a group member has excess EBITDA that can be used to create interest capacity for another group member in a given year). Conversely, however, the *de minimis* amount of EUR 3 million is then applied only once at the group level (article 4(3)).

Indeed, many Member States have implemented the ATAD's framework by treating a group as the "taxpayer" and consolidating EBITDAs, as well as interest income and expenses at the level of, for example, the group parent company under the domestic group taxation regime.[10,11] This approach is, however, generally limited to domestic group members and does not include foreign entities either because the domestic group taxation regime is limited to domestic groups in the first place (e.g. in Germany) or because the domestic interest barrier rules explicitly limit that approach to the domestic sphere, i.e. to group entities and domestic permanent establishments (PEs) of foreign group entities (e.g. in Austria). Needless to say, the focus of the "interest barrier group" on domestic situations has raised an intense debate concerning its compatibility with the freedom of establishment under article 49 of the TFEU,[12] especially in light of *X BV and X NV* (Case C-398/16)[13] and *Lexel* (484/19).[14]

5. *See* Recital 7 of the Preamble to the ATAD.
6. *Action 4 Final Report*, *supra* n. 4, at para. 196 et seq.
7. Id., at para. 47.
8. It might be noted in passing that, similarly, the interest barrier rule in the Commission's proposal for a common tax base (Proposal for a Council Directive on a Common Corporate Tax Base,COM(2016) 685 final, art. 13 (26 Oct. 2016), Primary Sources IBFD) similarly refers to the "national group taxation system", while the Commission's proposal for a common consolidated corporate tax base (CCCTB) would treat the whole cross-border CCCTB group as a single taxpayer for purposes of the interest barrier (Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB), COM(2016) 683 final, art. 69 (26 Oct. 2016), Primary Sources IBFD).
9. Recital 7 of the Preamble to the ATAD.
10. *See*, e.g. AT: Corporate Income Tax Act (Körperschaftsteuergesetz), § 12a(7) and DE: Corporate Income Tax Act, § 15.
11. The same effect may arise if a Member State applies a group taxation regime with respect to, e.g., a resident parent company or a non-resident parent company with a PE established in the Member State concerned and subsidiaries resident in that Member State and considering the respective parent companies to be the "single taxpayer" *as a consequence of this group taxation regime*. *See*, e.g., the optional fiscal unity regime in the Netherlands (*see* NL: Corporate Income Tax Act 1969 (Wet op de vennootschapsbelasting 1969, art. 15 [hereinafter Vpb]). In such a situation, the calculation of the exceeding borrowing costs and the EBITDA takes place automatically at the group level, i.e. the "single taxpayer", based on art. 4(1), first sentence ATAD without the necessity of relying on the option of art. 4(1), second and third sentences ATAD. The Netherlands has explicitly refrained from including the option of the ((inter)) national) group ratios in its domestic interest barrier rule (*see* art. 15b Vpb and, e.g., Parliamentary Papers (*Kamerstukken*) II 2018/19, 35030, no. 3, pp. 11 and 21; and Letter of State Secretary of Finance of 28 Oct. 2021, Parliamentary Papers II 2021/22, 35927, no. 32, p. 46). Therefore, according to the Netherlands legislator, the Netherlands fiscal unity is covered by art. 4(1), first sentence ATAD.
12. *See* sec. 4.
13. NL: ECJ, 22 Feb. 2018, Case C-398/16, *X BV, X NV v. Staatssecretaris van Financiën* and C-399/16, *X BV and X NV*, EU:C:2018:110, paras 34 and 49, Case Law IBFD.
14. SE: ECJ, 20 Jan. 2021, Case C-484/19, *Lexel AB v. Skatteverket*, paras. 40, 41 and 78, Case Law IBFD and, for analysis, CFE ECJ Task Force, *Opinion Statement ECJ-TF 1/2021 on the ECJ Decision of 20 January 2021 in Lexel AB (Case C-484/19) Concerning the Application of the Swedish*

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PRA Group Europe AS is particularly interesting, as it addresses a similar issue in the context of the Norwegian interest barrier rules and in light of the freedom of establishment under articles 31 and 34 of the EEA Agreement (1992) (and outside the ATAD's scope of application). Norway employs both *prima facie* non-discriminatory interest barrier rules (limiting the deductibility of interest paid to resident and non-resident affiliated parties to 30% of an entity's EBITDA) and a group contribution system (under which profits can be transferred, e.g. from a profitable to a loss-making group member), the latter, however, being confined to *domestic* group members. While Norway does not have a system of tax consolidation at the group level, group contributions achieve a similar result as regards the intra-group transfer of profits and losses: In a purely Norwegian situation, a group contribution is tax deductible at the level of the payer and taxable income at the level of the recipient; it likewise increases the EBITDA and the interest deduction for the recipient (and equivalently decreases the EBITDA of the payer). This was also considered in the Norwegian legislative process, where it was noted that since the group contribution forms part of the basis for the calculation and while the maximum deduction for the group as a whole will remain unchanged, companies in the tax group will be able, to a certain extent, to coordinate to achieve interest deductions where there are profits ("tax EBITDA") and where interest expenses are distributed unevenly between the companies in the group.[15] A similar opportunity is not available in cross-border situations: "[A] Norwegian tax-resident company in a group of companies liable to taxation in other EEA States, will not be able to similarly escape (or lessen the impact of) the limited interest deduction rules by providing a group contribution to a group company liable to taxation in another EEA State".[16]

It should be noted that these Norwegian rules have been subject to a reasoned opinion by the EFTA Surveillance Authority (ESA), which affirmed a violation of articles 31 and 34 of the EEA Agreement because the Norwegian interest barrier rules, while not providing for any difference in treatment between cross-border and domestic situations, nevertheless allows only Norwegian companies to benefit from the use of group contribution rules to create tax consolidations under Norwegian law.[17] The proceedings have, however, been closed due to amendments to the Norwegian rules: As of 1 January 2019, Norway has extended the interest barrier rules to interest paid to independent parties ("external interest") and introduced an "equity escape clause", under which a group company can claim a full deduction of interest if it can demonstrate that its equity/total assets ratio is equal to or higher than the global group ratio. An assessment of the amended legislation by the ESA is currently ongoing.[18]

The facts of *PRA Group Europe AS* are straightforward and may be simplified: PRA Group Europe Holding S.à.r.l. ("PRA Holding"), a Luxembourg company, has financed its Norwegian subsidiary, PRA Group Europe Subholding AS ("PRA Subholding"), with a mix of equity and debt. PRA Subholding's interest expense in 2014 and 2015 related to that debt. The deduction of claimed interest expense was, however, subsequently disallowed based on Norway's interest barrier rules, as calculated for PRA Subholding separately (irrespective of whether it was part of a group). PRA argued that this violates the freedom of establishment under articles 31 and 34 of the EEA Agreement, as in a domestic setting, the maximum deduction (30% of EBITDA) and hence the impact of the interest barrier can be lessened or removed by group contributions received, whereas such group contributions are not possible in cross-border situations (and none was in fact made to PRA Subholding due to its futility).

Faced with competing arguments from the taxpayer, as well as the tax administration, the Oslo District Court (Oslo tingrett) decided to refer a number of questions to the EFTA Court:[19]

> 1) Is there a restriction within the meaning of Article 31 EEA, read in conjunction with Article 34, when group contributions from Norwegian companies increase the maximum deduction for interest and thus the entitlement to deduction of interests [sic] on debt to affiliated parties under the limited interest deduction rule, a possibility which, under Norwegian tax rules, is not available for investments by or in EEA companies?
>
> 2) Is an EEA company that is in a group with a Norwegian company in a comparable situation to that of a Norwegian company that is in a group with another Norwegian company, and what significance does it have for the comparability assessment that no actual group contribution has been made from the EEA company to the Norwegian company, but rather a loan?
>
> 3) In the event that there is a restriction: Which reasons in the public interest may justify such a restriction?

3. The Decision of the EFTA Court

The Oslo District Court's first two questions inquire as to the existence of a restriction of the freedom of establishment and the comparability of situations, which is the foundation for the finding of prohibited discrimination. In essence, therefore, the EFTA Court had to deal with a situation in which the interaction between two sets of rules – the interest barrier rules and the group contribution rules – place Norwegian-based companies, which form part of a group with companies of other EEA states, at a disadvantage vis-à-vis companies in entirely Norwegian-based groups, as only the latter are able to lessen or

Interest Deductibility Rules, 61 Eur. Taxn. 6, pp. 264-268 (2021), Journal Articles & Opinion Pieces IBFD.

15. *See* NO: Prop. 1 LS (2013–2014) Part 4.7.1, p. 111, available at https://www.regjeringen.no/no/dokumenter/prop-1-ls-20132014/id740943/ (accessed 6 Jan. 2023): "*Ved at konsernbidrag inkluderes I beregningsgrunnlaget, vil selskap i skattekonsern ha en viss mulighet til å samordne seg med hensyn til rentefradrag i tilfeller der overskudd ("skattemessig EBITDA") og rentekostnader er ujevnt fordelt mellom konsernselskapene*".
16. *PRA Group Europe AS* (E-3/21), para. 26.
17. *See*, for a description of these proceedings and the closing of the EFTA Surveillance Authority, the Decision of 3 July 2019 in Case No. 76153, Decision No. 050/19/COL, available at https://www.eftasurv.int/esa-at-a-glance/publications/public-access-to-documents/public-documents (accessed 6 Jan. 2023).
18. *See* NO: ESA, Case No. 82998.
19. The reference and other documents pertaining to the case are available at https://eftacourt.int/cases/e-3-21/ (accessed 6 Jan. 2023).

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remove the impact of the limited interest deduction rules through the application of group contribution rules.

The EFTA Court first held that this combination of the limited interest deduction and the group contribution rules constitutes an obstacle to the freedom of establishment under articles 31 and 34 of the EEA Agreement, as "[a] difference in treatment may stem from a combination of different rules or circumstances".[20]

Moreover, the EFTA Court considered the internal and cross-border situations as objectively comparable in light of the purpose and content of the national legislative provisions in question, viewed again in their combination:[21] A situation in which a company established in one EEA state makes interest payments on a loan taken out from a company established in another EEA state and these two companies belong to the same group is no different from a situation in which the recipient of the interest payments is a company belonging to the group and is established in the same EEA state (i.e. Norway), and that comparability is not impacted by the fact that companies established in Norway "are able to lessen or remove the impact of limited interest deduction rules through the application of group contribution rules, whilst companies established in different EEA States are not".[22]

Finally, the fact that no actual group contribution has been made from the Luxembourg-based PRA Holding to the Norwegian-based PRA Subholding is, in the view of the EFTA Court, immaterial for this comparability assessment.[23] Interestingly, the EFTA Court did not directly address the contention of the Norwegian government, which tried to demonstrate that, from the perspective of a tax incentive, the non-deductibility of group contributions in Luxembourg is the decisive criterion.[24]

The EFTA Court hence held:[25]

> Consequently, the answer to Questions 1 and 2 must be that, in the context of the national legislation at issue in the main proceedings, a foreign EEA-based company in a group with a Norwegian-based company is in a comparable situation to that of a Norwegian-based company in a group with another Norwegian-based company. It is immaterial for the comparability assessment that no actual group contribution has been made from the company based in another EEA State to the Norwegian-based company. Article 31 EEA, read in conjunction with Article 34 EEA, must be interpreted as meaning that national legislation, such as that at issue in the main proceedings, constitutes a restriction on the freedom of establishment where a company liable to taxation in Norway may, by using group contribution rules, lessen or remove the impact of rules limiting interest deductions in respect of loans taken out with affiliated companies, provided it is in a group with other companies liable to taxation in Norway, whereas this is not possible if it is in a group with companies liable to taxation in other EEA States.

What remained to be addressed was the Oslo District Court's last question relating to a potential justification. The EFTA Court rejected both a justification based on the need to preserve the balanced allocation of taxing powers[26] and on the fight against tax avoidance and evasion.[27]

First, the EFTA Court acknowledged that, in isolation, group contribution rules had been justified by the need to preserve the balanced allocation of taxing powers between EEA states, i.e. it was considered "legitimate to limit certain tax advantages to domestic groups of companies, to the exclusion of non-resident EEA companies".[28] *PRA Group Europe AS*, however, was about the combination of the limited interest deduction and the group contribution rules, rather than the group contribution rules assessed alone:[29] Referring to *Lexel*,[30] the EFTA Court held that in cases:[31]

> in which combinations of tax rules function such that cross-border situations are treated less favourably than domestic situations, although one rule alone (in this instance, the group taxation rule) could itself be justified by the balanced allocation of taxing powers, this, in itself is insufficient to justify the overall fiscal situation, including the effect on the limited interest deduction rules.

In that context, considerations regarding the balanced allocation of taxing rights, which relate to preserving states' taxing rights over activities carried out on their territory:[32]

> are not capable of justifying a restriction such as that arising in circumstances in which a tax deduction has been granted in a national but not a cross-border situation. Rather, and in particular, if an EEA State grants such a benefit in a domestic situation (and renounces part of its taxation rights), that EEA State cannot

20. *See PRA Group Europe AS* (E-3/21), paras. 29-30, referring to *X BV and X NV* (C-399/16), paras. 34 and 49 and *Lexel* (C-484/19), paras. 40, 41 and 78.
21. *See PRA Group Europe AS* (E-3/21), paras. 31-33.
22. Id., para. 33.
23. Id., paras. 34-36, where the EFTA Court also added "that it is sufficient for legislation to be regarded as a restriction on the freedom of establishment if it is capable of restricting the exercise of that freedom without there being any need to establish that the legislation in question has actually had the effect of leading some of the companies established in another EEA State to refrain from acquiring, creating or maintaining a subsidiary in the EEA State in question".
24. *See* the discussion by the Oslo District Court in NO: Oslo District Court, 1 July 2021, 20-126483TVI-TOSL/06, i.e. its reference in *PRA Group Europe AS*, wherein the argument of the Norwegian government is summarized as follows: "It is the rules on entitlement to deductions in the country where the parent company is domiciled for tax purposes (in this case Luxembourg) that determine whether it has incentives to make other value transfers to subsidiaries in addition to the loan. That Luxembourg does not have rules on group contributions is a consequence of the fact that the tax rules are not harmonized within the EEA, with the result that the individual EEA State[s] determine themselves whether they wish to have rules on matters such as group contributions. That the parent company may not claim deductions for group contributions is a matter that possibly must be taken up with the authorities in Luxembourg, not the tax authorities in Norway. […] Since it is the tax rules in Luxembourg that determine whether the parent company has incentives to undertake other transfers to the plaintiff in addition to the loan, the rules on group contributions […] are irrelevant for the question whether there is a restriction".
25. *PRA Group Europe AS* (E-3/21), para. 37.
26. Id., paras. 41-48.
27. Id., paras. 49-56.
28. Id., para. 41, referring to NO: EFTA Court, 13 Sept. 2017, Case E-15/16, *Yara International*, [2017] EFTA Ct. Rep. 434, para. 55; FI: ECJ, 18 July 2007, Case C-231/05, *Oy AA*, para. 67, Case Law IBFD; NL: ECJ, 25 Feb. 2010, Case C-337/08, *X Holding BV v. Staatssecretaris van Financiën*, paras. 42-43, Case Law IBFD and *X BV and X NV* (C-398/16 and C-399/16), para. 23.
29. *PRA Group Europe AS* (E-3/21), paras. 43-48.
30. *Lexel* (C-484/19), para. 78.
31. *PRA Group Europe AS* (E-3/21), para. 46.
32. Id., para. 48, referring to NL: ECJ, 29 Mar. 2007, Case 120/78, *Rewe Zentralfinanz eG v. Finanzamt Köln-Mitte*, para. 43, Case Law IBFD.

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argue the same taxing right is important in the cross-border situation in an attempt to limit equal treatment.

Second, a national measure restricting the right of establishment for the purposes of preventing tax avoidance may be justified, "provided it specifically targets wholly artificial arrangements which do not reflect economic reality, and it is appropriate to secure the attainment of this objective and does not go beyond what is necessary to attain it".[33] However, established case law on discriminatory limitations of the deductibility of interest shows that such rules are only permitted "to the extent that they do not have any underlying commercial justification based on an assessment at arm's length" and must be limited to the arm's length amount.[34] Moreover, justification requires a case-specific examination and the opportunity for the taxpayer to provide evidence of any commercial justification that there may be for that arrangement.[35] These requirements are not met by the Norwegian rules, as they "do not provide for the opportunity for taxpayers to show that the transaction is commercially justified", there is "no possibility to demonstrate that a transaction is genuine and on arm's length terms", and the "deduction refused may not necessarily be limited to the proportion of interest which exceeds what would have been agreed had the relationship between the parties been one at arm's length".[36] These requirements are not altered by the fact that, in the European Union, under the ATAD's interest barrier rules, it is not "necessary to combine the interest limitation rule with the opportunity for taxpayers to show that the transaction is commercially justified". Conversely, the EFTA Court notes that this understanding is not undisputed and that "this directive has neither been incorporated into the EEA Agreement nor was it in force in the EU at the material time".[37]

The EFTA Court hence concluded:[38]

> Accordingly, the answer to the third question must be that a restriction arising from national legislation such as that at issue in the main proceedings may be justified where it serves the legitimate objective of preventing wholly artificial arrangements leading to tax avoidance. However, if national law, which is for the referring court to determine, does not provide the taxpayer with the opportunity to demonstrate that the transaction took place on terms corresponding to what would have been agreed had the relationship between the parties been one at arm's length, it goes beyond what is necessary to pursue that objective.

4. Comments

The EFTA Court makes it abundantly clear that, for purposes of identifying a restriction and for establishing comparability, a combined perspective on the interaction of two sets of rules – here the interest barrier, on the one hand, and the group contribution regime, on the other – is necessary.[39] This approach finds clear support in the ECJ's decisions in *X BV and X NV*[40] and in *Lexel*,[41] both of which dealt with the interaction of domestic rules on interest deductibility with the respective group taxation regimes. In *X BV and X NV*, for example, the Court noted that while the interest deductibility rules did not draw any distinction according to whether or not a group is cross-border, it was the impact of tax consolidation, which was limited to domestic entities, that caused the discrimination. More generally, such a combined approach was also taken in *Groupe Steria* regarding the treatment of dividends inside and outside of a group taxation regime.[42]

This combined perspective is also to be taken at the level of justification: Just because the limitation of group taxation regimes to domestic entities can be justified by the need to preserve the balanced allocation of taxing powers (apart from, perhaps, the issue of "final losses" on the level of proportionality),[43] this does not mean that the collateral impact on other rules (e.g. the interest barrier rules) is automatically justified as well. Quite to the contrary, as the EFTA Court highlighted, it is about whether the difference in treatment under the group contribution regime "in relation to the limited interest deduction rules can be justified by the need to safeguard the allocation of the power to impose taxes between EEA States",[44] which was not the case in *PRA Group Europe AS*. Put differently, the balanced allocation of taxing powers that justifies domestic group taxation regimes does not likewise justify the effect of a discriminatory denial of interest deductions.

Interestingly, the referring Norwegian court asked, as the third referral question, which "reasons in the public interest may justify such a restriction" instead of invoking a specific one. It is hence quite remarkable that the Court, in answering this question, has not discussed the applicability of the coherence argument. Had it been considered, the Court might have reached the conclusion that, in a purely domestic situation, there was indeed a direct link between: (i) on the one hand, the increase in the EBITDA at the level of the entity that receives a group contribution for purposes of the interest barrier (as an advantage) and (ii) on the other hand, the increase of taxable profit at the level

33. *PRA Group Europe AS* (E-3/21), para. 49, referring to NO: EFTA Court, 9 July 2014, Cases E-3/13 and E-20/13, *Fred. Olsen and Others*, [2014] EFTA Ct. Rep. 400, para. 166 and *Yara International* (E-15/16), para. 37).
34. *PRA Group Europe AS* (E-3/21), para. 52. Compare the decisions in UK: ECJ, 13 Mar. 2007, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v. Commissioners of Inland Revenue*, Case Law IBFD, para. 83 and *Lexel* (C-484/19), paras. 50-51.
35. *PRA Group Europe AS* (E-3/21), para. 53, referring to *Lexel* (C-484/19), para. 50 and *Yara International* (E-15/16), para. 51.
36. *PRA Group Europe AS* (E-3/21), para. 54.
37. Id., para. 56.
38. Id., para. 57.
39. Id., paras. 29-30.
40. *X BV and X NV* (C-398/16 and C-399/16), paras. 34 and 49.
41. *Lexel* (C-484/19), paras. 40, 41 and 78 and, for analysis, CFE ECJ Task Force, *supra* n. 14.
42. FR: ECJ, 2 Sept. 2015, Case C-386/14, *Groupe Steria SCA v. Ministry of Finance and Public Account*, Case Law IBFD, and CFE ECJ Task Force, *Opinion Statement ECJ-TF 4/2015 on the Decision of the European Court of Justice in Groupe Steria SCA (Case C-386/14), on the French Intégration Fiscale*, 56 Eur. Taxn. 5 (2016), Journal Articles & Opinion Pieces IBFD.
43. *See* for that "final loss exception" for systems of group relief: UK: ECJ, 13 Dec. 2005, Case C-446/03, *Marks & Spencer plc v. Halsey (Her Majesty's Inspector of Taxes)*, Case Law IBFD and UK: ECJ, 3 Feb. 2015, Case C-172/13, *European Commission v. United Kingdom of Great Britain and Northern Ireland, (Marks & Spencer II)*, Case Law IBFD; for group contributions: SE: ECJ, 19 June 2019, Case C-608/17, *Skatteverket v. Holmen AB*, Case Law IBFD and *Yara International* (E-15/16); and for tax consolidation regimes: *X Holding* (C-337/08).
44. *PRA Group Europe AS* (E-3/21), para. 46.

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of the same entity (as a disadvantage). Arguably, therefore, the required direct link and the identity of the taxpayer and applicable tax would exist in such a situation.[45] Conversely, in the cross-border scenario, the taxpayer *PRA Group Europe AS* had obviously claimed to receive only the advantage (in the form of a higher EBITDA for the purposes of the interest barrier, based on a "hypothetical" group contribution) without bearing the corresponding disadvantage of an increased tax base. One could even expand that argument: Indeed, the Court did not address a potential "double advantage"[46] that would only emerge in the cross-border scenario: Domestically, the group contribution would be neutral in terms of the EBITDA of the group from an overall perspective (as the increase would be matched by a corresponding decrease in Norway). In the cross-border scenario, the recognition of a group contribution in Norway for purposes (only) of the interest barrier rules would not be matched by a corresponding decrease in Luxembourg (which does not have group contribution rules). In effect, the EBITDA at the group level at the state of the (hypothetical) contributor would remain unchanged, while the EBITDA in the state of the company receiving the group contribution would increase, essentially artificially increasing the overall interest deductibility potential.

The broader question is, of course, what *PRA Group Europe AS* means for the group perspective on interest barrier rules in the European Union based on article 4 of the ATAD. There are at least two variations of the theme: First, Norway's system at issue in *PRA Group Europe AS* does not concern an "interest barrier group" as foreseen in article 4(1) of the ATAD, but rather the impact of a group taxation regime on the interest barrier rules. Such potentially discriminatory impact is also present, e.g. in Sweden, where the group contribution system is likewise limited to domestic group entities, and so are the effects of group contributions on the Swedish implementation of the ATAD's interest barrier rule.[47] Second, as for "interest barrier groups" under article 4(1) of the ATAD, where a group is treated as a single taxpayer, one focus of this debate is whether an isolated or a combined perspective should be taken: while some have pointed out that the ECJ has indeed accepted a limitation of various group taxation regimes to domestic situations (apart from, perhaps, the issue of "final losses"), others have stressed that it is the combined effect of such group taxation regimes and interest barrier rules that leads to a discriminatory effect. The EFTA Court has clearly sided with the latter perspective ("combined effect"), which argues that the freedom of establishment under article 49 of the TFEU prohibits the limitation of an "interest barrier group" to domestic members of a group.

If one accepts this proposition, however, the tension with article 4(1) of the ATAD becomes obvious, as it is the latter that arguably[48] limits the group perspective to domestic settings. Indeed, the Norwegian government in *PRA Group Europe AS* tried to argue that the rules on the domestic "interest barrier group" in article 4(1) of the ATAD, in conjunction with Recital 7 of the Preamble, are in line with the fundamental freedoms,[49] which would then imply that the Norwegian rules are also in compliance with articles 31 and 34 EEA Agreement (before and after the ATAD was in force). The EFTA Court has skillfully avoided the issue. It merely pointed out that the ATAD "has neither been incorporated into the EEA Agreement nor was it in force in the EU at the material time".[50] Still, the issue is complex:

Since the treatment of an "interest barrier group" as a single taxpayer under article 4(1) second and third sentence of the ATAD is optional for Member States ("may also treat as a taxpayer"), this implies that no "exhaustive harmonization"[51] has taken place, as the creation of an "interest barrier group" is – in the words of Advocate General Kokott – "no duty" for the Member States, "but only an entitlement".[52] Consequently, this would result in a requirement of non-discriminatory implementation of an option foreseen in a Directive, i.e. such a "possibility may be exercised only in compliance with the fundamental provisions of the Treaty".[53] In essence, and in light of

45. *See* BE: ECJ, 28 Jan. 1992, Case C-204/90, *Hanns-Martin Bachmann v. Belgian State*, Case Law IBFD; FR: ECJ, 27 Nov. 2008, Case C-418/07, *Société Papillon v. Ministère du budget, des comptes publics et de la fonction publique*, Case Law IBFD; FI: ECJ, 7 Sept. 2004, Case C-319/02, *Petri Manninen*, Case Law IBFD and NL: ECJ, 29 Nov. 2011, Case C-371/10, *National Grid Indus BV v. Inspecteur van de Belastingdienst Rijnmond/kantoor Rotterdam*, Case Law IBFD.
46. *See*, for that concept and its prevention, *Marks & Spencer* (C-446/03), paras. 43 and 47.
47. It should be noted that during the implementation of art. 4 ATAD in Sweden, concerns about the EU compatibility were addressed but, in light of *Oy AA* (C-231/05), it was concluded that the effect of group contributions on the interest barrier was in accordance with EU law. *See* SE: Gov. Bill No. 2017/18:245, p. 108 (*I och med att företag som kan lämna koncernbidrag till varandra i viss utsträckning kan fördela avdragsunderlagen inom koncernen, uppstår frågan om förslaget står i överensstämmelse med EU-rätten. Det kan inte uteslutas att en sådan utjämningsmöjlighet skulle kunna betraktas som en inskränkning av etableringsfriheten i fördraget om Europeiska unionens funktionssätt (FEUF). Anledningen till att lämnade och mottagna koncernbidrag ingår i avdragsunderlaget är emellertid att avdragsunderlaget motsvarar skattemässigt EBITDA. Koncernbidrag utgör således en del av beräkningen av det skattemässiga resultatet av näringsverksamheten. En prövning bör göras av den generella ränteavdragsbegränsningsregeln inklusive koncernbidragsreglerna. Det kan därvid konstateras att de svenska reglerna om koncernbidrag är förenliga med etableringsfriheten i FEUF, sedda tillsammans med de svenska reglerna om koncernavdrag (se t.ex. mål C-231/05 Oy AA, RÅ 2009 ref. 13–15 och RÅ 2009 not. 35–37). Mot den bakgrunden bör även det nu aktuella förslaget anses stå i överensstämmelse med EU-rätten*).
48. *See* sec. 2.
49. *See* the discussion of NO: 1 July 2021, Oslo District Court, 20-126483TVI-TOSL/06, referenced in *PRA Group Europe AS*, wherein it argued that "[t]he EU legislature must necessarily have taken the view that ATAD is compatible with primary EU law, including the freedom of establishment. Had it not, the Directive would have been invalid under EU law".
50. *PRA Group Europe AS* (E-3/21), para. 56.
51. Once "exhaustive harmonization" is achieved, national tax law will only be tested against the secondary EU law it seeks to implement, but not against primary EU law. *See*, e.g., FR: ECJ, 8 Mar. 2017, Case C-14/16, *Euro Park Service*, para. 19, Case Law IBFD; DE: ECJ, 20 Dec. 2017, Case C-504/16 and C-613/16, *Deister Holding and Juhler Holding*, para. 45, Case Law IBFD.
52. FI: Opinion of Advocate General Kokott, 13 July 2017, Case C-292/16, *A Oy v. Veronsaajien oikeudenvalvontayksikkö*, para. 22, Case Law IBFD.
53. This requirement was established by the Court, e.g., in NL: ECJ, 18 Sept. 2003, Case C-168/01, *Bosal Holding BV v. Staatssecretaris van Financiën*, paras. 21-28, Case Law IBFD; UK: ECJ, 12 Dec. 2006, Case C-446/04, *Test Claimants in the Franked Investment Income Group Litigation v. Commissioners of Inland Revenue*, para. 46, Case Law IBFD; DE: ECJ, 23 Feb. 2006, Case C-471/04, *Keller Holding v. Finanzamt Offenbach*

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PRA Group Europe AS, Member States would then only have the choice between extending the "interest barrier group" to non-resident group members in the EU/EEA (which would undermine the policy objective of article 4 of the ATAD) or not exercising the option of an "interest barrier group" at all (which would make the interest barrier apply to situations wholly outside profit shifting concerns).

Conversely, if one were to accept that article 4(1) of the ATAD – either its basic rule in the first sentence or even the option in the second and third sentence – has brought about "exhaustive harmonization", a national measure "must be assessed in the light of the provisions of the harmonising measure and not those of the Treaty",[54] and the compatibility with the fundamental freedoms then becomes one of the validity of secondary EU law (articles 263 and 267 of the TFEU), i.e. the focus would shift to the question of whether or not article 4(1) of the ATAD complies with primary EU law. However, and while the fundamental freedoms are also binding on the EU legislature,[55] it undoubtedly enjoys a much broader discretion than domestic legislatures with regard to the shaping of the Internal Market[56] and faces only a "review as to manifest error".[57] It seems to be against that background that the ATAD's Preamble notes that "national implementing measures which follow a common line across the Union would provide taxpayers with legal certainty in that those measures would be compatible with Union law".[58]

It remains to be seen how the Court will approach a potential challenge to the ATAD's interest barrier rules[59] and if the mere existence of the ATAD and the value judgments made by the EU legislature therein could lead to a different protection of taxpayers in the European Union vis-à-vis the European Economic Area. (To add an additional layer of complexity, it might be noted in passing that the different treatment between domestic and cross-border groups might also raise State aid questions.[60])

One final point should be highlighted: The EFTA Court mentioned an even more fundamental position of the ESA, according to which "the limitation rules must comply with fundamental freedoms and an assessment on proportionality, allowing the taxpayer the opportunity to provide commercial justification for excess interest expenses".[61] Arguably, therefore, the ESA views the prevention of tax avoidance as the only acceptable ground of justification for discriminatory effects of an interest barrier, which would, inter alia, require the opportunity for taxpayers to show that the transaction is commercially justified to be proportionate. Clearly, this is not the case, e.g. in article 4 of the ATAD, which applies irrespective of any tax avoidance or artificiality. It is hence no surprise that the EU Commission in *PRA Group Europe AS* disagreed with the ESA and argued that the Norwegian rules should not be precluded by articles 31 and 34 of the EEA Agreement.[62]

5. The Statement

The CFE ECJ Task Force welcomes the EFTA Court's progressive impetus on fundamental freedoms doctrine: PRA Group Europe AS makes it clear that, for purposes of identifying a restriction, for establishing comparability and for justification, a combined perspective on the interaction of two sets of rules – here the interest barrier, on the one hand, and the group contribution regime, on the

am Main-Land, para. 45, Case Law IBFD; and *Groupe Steria* (C-386/14), paras. 37-39.

54. FR: ECJ, 12 Oct. 1993, Case C-37/92, *Vanacker and Lesage*, EU:C:1993:836, para. 9; DE: ECJ, 11 Dec. 2003, Case C-322/01, *DocMorris*, EU:C:2003:664, paras. 63-65; BE: ECJ, 16 Dec. 2008, Case C-205/07, *Lodewijk Gysbrechts*, EU:C:2008:730, para. 33, Case Law IBFD; BE: ECJ, 18 July 2013, Case C-265/12, *Citroën Belux*, EU:C:2013:498, para. 31; and HU: ECJ, 30 Apr. 2014, Case C-475/12, *UPC DTH Sàrl*, EU:C:2014:285, para. 63.
55. *See*, e.g., DE: ECJ, 1 Oct. 2009, Case C-247/08, *Gaz de France – Berliner Investissement SA v. Bundeszentralamt für Steuern*, para. 53, Case Law IBFD and AT: ECJ, 26 Oct. 2010, Case C-97/09, *Ingrid Schmelz v. Finanzamt Waldviertel*, para. 50, Case Law IBFD.
56. *See*, e.g., SE: ECJ, 17 Oct. 2013, Case C-203/12, *Billerud Karlsborg AB and Billerud Skärblacka AB v Naturvårdsverket*, EU:C:2013:664, paras 34-37; PL: ECJ, 7 Mar. 2017, Case C-390/15, *Rzecznik Praw Obywatelskich (RPO)*, paras. 37-72, Case Law IBFD; HU: ECJ, 8 Dec. 2020, Case C-620/18, *Hungary v. Parliament and Council*, EU:C:2020:1001, paras 104-117; and PL: ECJ, 8 Dec. 2020, Case C-626/18, *Poland v. Parliament and Council*, EU:C:2020:1000, paras. 87-100.
57. *See*, e.g., UK: ECJ, 10 Dec. 2002, Case C-491/01, *British American Tobacco (Investments) and Imperial Tobacco*, EU:C:2002:741, para. 123; *Billerud* (C-203/12), para. 35; and *RPO* (C-390/15), para. 54.
58. *See* Recital 2 of the Preamble to the ATAD.
59. As noted in *supra* n. 11, the result of the optional fiscal unity regime in the Netherlands is that the calculation of the exceeding borrowing costs and the EBITDA automatically takes place at the group level, i.e. the "single taxpayer", based on art. 4(1), first sentence ATAD without the necessity of relying on the option of art. 4(1), second and third sentences ATAD. Therefore, according to the Netherlands legislature, the Netherlands fiscal unity is covered by art. 4(1), first sentence ATAD. This rule is a minimum standard. *See* Recitals 2, 3, 6, 16 of the Preamble to the ATAD and art. 11(6) ATAD. Member States may be stricter according to art. 3 ATAD. As held, art. 4(1), first sentence ATAD, being a minimum standard, could be considered as "exhaustive harmonization", but the second and third sentences cannot. A consequence of this distinction may be that, depending on the various group taxation systems, different results may arise: art. 4(1) second and third sentences ATAD, being options, can be tested against the fundamental freedoms, whereas the first sentence cannot. From the perspective of realizing one internal market, this outcome may not be desirable. A possible different approach could be that the ECJ will interpret art. 4(1) ATAD in such a way that also systems like the Netherlands fiscal unity will be covered by art. 4(1) second and third sentences and not by the first sentence because the fiscal unity may have similar results as other systems of group taxation. To the extent that Member States include rules in their domestic tax systems that are stricter than art. 4(1), first sentence ATAD, it could be argued that these rules, to the extent that they go beyond the minimum standard, can be tested against the fundamental freedoms.
60. As art. 107 TFEU only refers to "aid granted by a Member State or through State resources", the decisive question becomes whether potential aid is even imputable to a Member State. A "measure is not imputable to a Member State if the Member State is under an obligation to implement it under Union law without any discretion", as "[i]n that case, the measure stems from an act of the Union legislature and is not imputable to the State" (*see* para. 44 of the Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, OJ C 262, p. 1 (2016)). As for options granted by secondary law, the Commission seems to assume imputability to a Member State "where Union law simply allows for certain national measures and the Member State enjoys discretion (i) as to whether to adopt the measures in question or (ii) in establishing the characteristics of the concrete measure which are relevant from a State aid perspective" (id., at para. 45). The Court, however, seemed to have taken a different perspective on imputability when it held that a restriction caused by the exercise of the option to exempt only domestic small enterprises from VAT "cannot be attributed to the Member States", "as the directives in question allow them to offer a VAT exemption only to small undertakings established in their respective territories" (*Ingrid Schmelz* (C-97/09)).
61. *PRA Group Europe AS* (E-3/21), para. 56.
62. *See* the Report for the Hearing in Case E-3/21, para. 28.

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other – is necessary. From that perspective, the interaction of the Norwegian rules on the "interest barrier" and on group contributions leads to unjustified discrimination in cross-border situations.

If asked to decide on a similar case, however, the ECJ might take a different approach. First, the ECJ could take a different perspective on the available grounds of justifications and, e.g., accept the coherence of the tax system as such a ground. Second, article 4 of the ATAD gives the Member States the option to treat an "interest barrier group" as a single taxpayer and to limit the group perspective to domestic settings. Even if such an option in the ATAD is not viewed as "exhaustive harmonization", one could wonder if the mere existence of the ATAD and the value judgments made by the EU legislature therein could lead to a different outcome in the European Union (ECJ) vis-à-vis the European Economic Area (EFTA Court).

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