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EUROPEAN COURT OF JUSTICE

1.1

Reference for a preliminary ruling — Harmonisation of fiscal legislation — Common system of value added tax (VAT) — Directive 2006/112/EC — Deduction of VAT — Determination of the taxable person liable for VAT — Retroactive application of a derogating measure — Principle of legal certainty. Judgement dated 13 February 2019, Case C-434/17. ***Human Operator Zrt. Vs. Nemzeti Adó- és Vámhivatal Fellebbviteli Igazgatósága***

The European Union law objects to an Italian regulation prescribing the application of a derogating measure from article 193 of Council Directive no. 2006/112/EC of 28 November 2006 on the common system of value added tax, as amended by European Directive no. 2013/43/EE of 22 July 2013, before the European Union's deed authorizing such derogation has been notified to the Member State which has requested for it, if such deed makes no mention of its entry into force or initial date of application and even if that Member State has stated that it will apply the derogation retroactively.

The European Court of Justice has clarified the retroactive application of a measure derogating from article 193 of European Directive no. 2006/112/EC, with specific reference to Hungarian law.

It also held that, in order to comply with principles of legal certainty and the protection of legitimate expectations, the basic rules of EU law must, in principle, be interpreted as applying only to situations existing after their entry into force (see, to that effect, judgment *Falck* and *Acciaierie di Bolzano* vs. Commission). Thus, in general, the principle of legal certainty precludes an EU measure from taking effect from a point in time before its publication or its notification, as the case may be, since the Court has ruled that it may exceptionally be otherwise, where the purpose to be achieved so demands and where the legitimate expectations of those concerned are duly respected (see, to that effect, judgments *Amylum/ Council and Goed Wonen*).

With reference to the case at issue, the EC judges deem that the Hungarian Government was not in a position to introduce the reverse charge procedure for services which are not mentioned by Article 199(1)(a) of the VAT Directive before Hungary was notified of the Implementing Decision authorising that reverse charge procedure.

Moreover, whenever the provisions of a directive appear, so far as their subject matter is concerned, to be unconditional and sufficiently precise, they may be relied on before the national courts by individuals against the State where the State has failed to transpose the directive into national law within the time limit or has transposed it incorrectly (see judgements *E.ON Global Commodities and Almos Agrárkülkereskedelmi*).

1.2

Reference for a preliminary ruling — Approximation of laws — Common system of taxation applicable in the case of parent companies and subsidiaries of different Member States — Directive 90/435/EEC — Exemption of the profits distributed by companies of a Member State to companies of other Member States — Beneficial owner of the distributed profits — Abuse of rights — Company established in a Member State and paying to an associated company established in another Member State dividends all or almost all of which are then transferred outside the European Union — Subsidiary subject to an obligation to withhold tax on the profits at source. Judgment dated 26 February 2019, Joined cases C-116/16 and C-117/16, Skatteministeriet vs. T Danmark (C-116/16) and Y Denmark Aps (C-117/16)

Cases C-116/16 and C-117/16 are joined for the purposes of the judgment.
The general principle of EU law that EU law cannot be relied on for abusive or fraudulent ends must be interpreted as meaning that, where there is a fraudulent or abusive practice, the national authorities and courts are to refuse a taxpayer the exemption from withholding tax on profits distributed by a subsidiary to its parent company, provided for in Article 5 of Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, as amended by Council Directive 2003/123/EC of 22 December 2003, even if there are no domestic or agreement-based provisions providing for such a refusal.
Proof of an abusive practice requires, first, a combination of objective circumstances in which, despite formal observance of the conditions laid down by the EU rules, the purpose of those rules has not been achieved and, second, a subjective element consisting in the intention to obtain an advantage from the EU rules by artificially creating the conditions laid down for obtaining it. The presence of a certain number of indications may demonstrate that there is an abuse of rights, in so far as those indications are objective and consistent. Such indications can include, in particular, the existence of conduit companies which are without economic justification and the purely formal nature of the structure of the group of companies, the financial arrangements and the loans.
In order to refuse to accord a company the status of beneficial owner of dividends, or to establish the existence of an abuse of rights, a national authority is not required to identify the entity or entities which it regards as being the beneficial owner(s) of those dividends.

In a situation where the system, laid down by Directive 90/435, as amended by Directive 2003/123, of exemption from withholding tax on dividends paid by a company resident in a Member State to a company resident in another Member State is not applicable because there is found to be fraud or abuse, within the meaning of Article 1(2) of that directive, application of the freedoms enshrined in the FEU Treaty cannot be relied on in order to call into question the legislation of the first Member State governing the taxation of those dividends.

These requests for a preliminary ruling concern the interpretation of Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, as amended by Council Directive 2003/123/EC of 22 December 2003 ('Directive 90/435'), and of Articles 49, 54 and 63 TFEU.
The requests have been made in proceedings brought by the *Skatteministeriet* (Ministry of Taxation, Denmark) against T Danmark and Y Denmark Aps relating to the obligation imposed on those companies to pay withholding tax by reason of the payment by them of dividends to non-resident companies regarded by the tax authority as not being the beneficial owners of those dividends, which is a requirement commented in the above mentioned judgment.

In the case at issue, the questions referred by the national court concern the following three topics:
- the first topic relates to the existence of a legal basis enabling a Member State to refuse, on account of the commission of an abuse of rights, to grant the exemption provided for in Article 5 of Directive 90/435 to a company that has distributed profits to a company of another Member State, of which it is the subsidiary;
- the second topic addressed by the questions concerns the constituent elements of any abuse of rights and the conditions for proving it;
- the third topic of the questions concerns the interpretation of the provisions of the FEU Treaty relating to freedom of establishment and the free movement of capital.

It thus follows from that principle that a Member State must refuse to grant the benefit of the provisions of EU law where they are relied upon not with a view to achieving the objectives of those provisions but with the aim of benefiting from an advantage in EU law although the conditions for benefiting from that advantage are fulfilled only formally. According to the Court, that is so, for example, where the completion of customs formalities does not fall within the context of normal commercial transactions but is purely

formal and is designed solely to obtain wrongfully the grant of compensatory amounts (*see, to that effect, judgments dated 27 October 1981, Schumacher and others, 250/80, EU:C:1981:246, par. 16, and 3 March 1993, General Milk Products, C-8/92, EU:C:1993:82, par. 21)* or export refunds *(see, to that effect, judgment dated 14 December 2000, Emsland-Stärke, C-110/99, EU:C:2000:695, par. 59*)".

In particular, whilst the pursuit by a taxpayer of the tax regime most favourable for him cannot, as such, set up a general presumption of fraud or abuse, the fact remains that such a taxpayer cannot enjoy a right or advantage arising from EU law where the transaction at issue is purely artificial economically and is designed to circumvent the application of the legislation of the Member State concerned. And the absence of domestic or agreement-based anti-abuse provisions does not affect the national authorities' obligation to refuse to grant entitlement to rights provided for by Directive where they are invoked for fraudulent or abusive ends.

It ensues that the general principle of EU law that EU law cannot be relied on for abusive or fraudulent ends must be interpreted as meaning that, where there is a fraudulent or abusive practice, the national authorities and courts are to refuse a taxpayer the exemption from withholding tax on profits distributed by a subsidiary to its parent company, provided for in Article 5 of Directive 90/435, even if there are no domestic or agreement-based provisions providing for such a refusal.

As regards the constituent elements of an abuse of rights and the relevant evidence, it has been specified that Directive 90/435 does not contain provisions relating to the burden of proving that there is an abuse of rights. However, as the Danish and German Governments contend, it is in principle for the companies which seek entitlement to the exemption from withholding tax on dividends that is provided for in Article 5 of Directive 90/435 to establish that they fulfil the objective conditions imposed by the directive. Where a Tax Authority of the source Member State seeks, on a ground relating to the existence of an abusive practice, to refuse to grant the exemption provided for in Article 5 of Directive 90/435 to a company that has paid dividends to a company established in another Member State, it has the task of establishing the existence of elements constituting such an abusive practice while taking account of all the relevant factors, in particular the fact that the company to which the dividends have been paid is not their beneficial owner. Specifically, such an authority has the task not of identifying the beneficial owners of those dividends but of establishing that the supposed beneficial owner is merely a conduit company through which an abuse of rights has been committed.

For the sake of completeness, in its judgment the Court has explained that it is an indication of the existence of an arrangement intended to obtain improper entitlement to the exemption provided for in Article 5 of Directive 90/435 that all or almost all of the aforesaid dividends are, very soon after their receipt, passed on by the company that has received them to entities which do not fulfil the conditions for the application of Directive 90/435, either because they are not established in any Member State, or because they are not incorporated in one of the forms covered by the Directive, or because they are not subject to one of the taxes listed in Article 2(c) of the Directive, or because they do not have the status of 'parent company' and do not meet the conditions laid down in Article 3 of the Directive.

1.3

Reference for a preliminary ruling — Approximation of laws — Common system of taxation applicable to interest and royalty payments made between associated companies of different Member States — Directive 2003/49/EC — Beneficial owner of the interest and royalties — Article 5 — Abuse of rights — Company established in a Member State and paying to an associated company established in another Member State interest all or almost all of which is then transferred outside the European Union — Subsidiary subject to an obligation to withhold tax on the interest at source.

In Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16, referring to the requests for a preliminary ruling under Article 267 TFEU from the *Østre Landsret* (High Court of Eastern Denmark, Denmark) (C-115/16, C-118/16 and C-119/16), made by decisions of 19 February 2016, received at the Court on 25 February 2016, and from the *Vestre Landsret* (High Court of Eastern Denmark, Denmark) (C-299/16), made by decision of 24 May 2016, received at the Court on 26 May 2016, in the proceedings N Luxembourg 1 (C-115/16), X Denmark A/S (C-118/16), C Denmark I (C-119/16), Z Denmark ApS (C-299/16) against *Skatteministeriet.* Court judgment dated 26 February 2019

Cases C-115/16, C-118/16, C-119/16 and C-299/16 are joined for the purposes of the judgment.
Article 1(1) of 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, read in conjunction with Article 1(4) thereof, must be interpreted as meaning that the exemption of interest payments from any taxes that is provided for by it is restricted solely to the beneficial owners of such interest, that is to say, the entities which actually benefit from that interest economically and accordingly have the power freely to determine the use to which it is put.
The general principle of EU law that EU law cannot be relied on for abusive or fraudulent ends must be interpreted as meaning that, where there is a fraudulent or abusive practice, the national authorities and courts are to refuse a taxpayer the exemption of interest payments from any taxes that is provided for in

Article 1(1) of Directive 2003/49, even if there are no domestic or agreement-based provisions providing for such a refusal.

Proof of an abusive practice requires, first, a combination of objective circumstances in which, despite formal observance of the conditions laid down by the EU rules, the purpose of those rules has not been achieved and, second, a subjective element consisting in the intention to obtain an advantage from the EU rules by artificially creating the conditions laid down for obtaining it. The presence of a certain number of indications may demonstrate that there is an abuse of rights, in so far as those indications are objective and consistent. Such indications can include, in particular, the existence of conduit companies which are without economic justification and the purely formal nature of the structure of the group of companies, the financial arrangements and the loans. The fact that the Member State where the interest arises has concluded a convention with the third State in which the company that is the beneficial owner of the interest is resident has no bearing on any finding of an abuse of rights.

In order to refuse to accord a company the status of beneficial owner of interest, or to establish the existence of an abuse of rights, a national authority is not required to identify the entity or entities which it regards as being the beneficial owner(s) of that interest.

Article 3(a) of Directive 2003/49 must be interpreted as meaning that a société en commandite par actions (SCA) (limited partnership with share capital) authorised as a société d'investissement en capital à risque (SICAR) (risk capital investment company) governed by Luxembourg law cannot be classified as a company of a Member State, within the meaning of that directive, capable of being entitled to the exemption provided for in Article 1(1) of the directive if, a matter which is for the referring court to ascertain, the interest received by that SICAR, in a situation such as that at issue in the main proceedings, is exempt from impôt sur les revenus des collectivités (corporate income tax) in Luxembourg.

In a situation where the system, laid down by Directive 2003/49, of exemption from withholding tax on interest paid by a company resident in a Member State to a company resident in another Member State is not applicable because there is found to be fraud or abuse, within the meaning of Article 5 of that directive, application of the freedoms enshrined in the FEU Treaty cannot be relied on in order to call into question the legislation of the first Member State governing the taxation of that interest.

Outside such a situation, Article 63 TFEU must be interpreted as:

- *not precluding, in principle, national legislation under which a resident company which pays interest to a non-resident company is required to withhold tax on that interest at source whilst such an obligation is not owed by that resident company when the company which receives the interest is also a resident company, but as precluding national legislation that prescribes such withholding of tax at*

source if interest is paid by a resident company to a non-resident company whilst a resident company that receives interest from another resident company is not subject to the obligation to make an advance payment of corporation tax during the first two tax years and is therefore not required to pay corporation tax relating to that interest until a date appreciably later than the date for payment of the tax withheld at source;

- *precluding national legislation under which the resident company that owes the obligation to withhold tax at source on interest paid by it to a non-resident company is obliged, if the tax withheld is paid late, to pay default interest at a higher rate than the rate which is applicable in the event of late payment of corporation tax that is charged, inter alia, on interest received by a resident company from another resident company;*
- *precluding national legislation providing that, where a resident company is subject to an obligation to withhold tax at source on the interest which it pays to a non-resident company, account is not taken of the expenditure in the form of interest, directly related to the lending at issue, which the latter company has incurred whereas, under that national legislation, such expenditure may be deducted by a resident company which receives interest from another resident company for the purpose of establishing its taxable income.*

The requests for a preliminary ruling concern the interpretation of 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 and of Articles 49, 54 and 63 TFEU. In particular, the requests have been made in proceedings brought by N Luxembourg 1, X Denmark A/S, C Denmark I and Z Denmark ApS against the *Skatteministeriet* (Ministry of Taxation, Denmark) relating to the exemption from withholding tax as prescribed by the Directive if certain conditions are met.

First of all, please note that that under Article 3(a) of Directive 2003/49 three conditions must be met in order for a company to have the status of a ‘company of a Member State’:

- that company must have one of the forms listed in the annex to the directive;
- it must, in accordance with the tax laws of a Member State, be considered to be resident in that Member State and not be considered, within the meaning of a Double Tax Treaties to be resident for tax purposes outside the European Union;
- it must be subject to one of the taxes listed in Article 3(a)(iii) of Directive 2003/49 without being exempt, or to a tax which is identical or substantially similar and which is imposed after the date of entry into force of the Directive in addition to, or in place of, those existing taxes.

In the case at issue, the questions referred by the national courts concern the following topics:

- the concept of 'beneficial owner' and to the existence of a legal basis enabling a Member State to refuse, on account of the commission of an abuse of rights, to grant the exemption from any taxes that is provided for in Article 1(1) of the directive;
- the constituent elements of any abuse of rights and the conditions for proving it;
- the interpretation of the provisions of the FEU Treaty relating to freedom of establishment and the free movement of capital.

The Court underlined that the concept of 'beneficial owner of the interest' cannot refer to concepts of national law that vary in scope. Specifically, the concept of 'beneficial owner of the interest' must therefore be interpreted as designating an entity which actually benefits from the interest that is paid to it. Reference must therefore be made to economic reality by stating that a company of a Member State is to be treated as the beneficial owner of interest or royalties only if it receives those payments for its own benefit and not as an intermediary, such as an agent, trustee or authorised signatory, for some other person. Accordingly, the term 'beneficial owner' concerns not a formally identified recipient but rather the entity which benefits economically from the interest received and accordingly has the power freely to determine the use to which it is put. Only an entity established in the European Union can be a beneficial owner of interest, capable of being entitled to the exemption provided for in the Directive.

It has been specified that the Directive (reference is made to the proposal for a Council Directive, document COM (1998) 67) draws upon Article 11 of the OECD Model Tax Convention and pursues the same objective (i.e. avoiding international double taxation). It ensues that the concept of 'beneficial owner', which appears in the bilateral Conventions based on that Model, and the successive amendments of that Model and of the Commentaries relating thereto are, therefore, relevant when interpreting Directive 2003/49 (Ambulatory approach of treaties' interpretation). Moreover, it is clear from the development of the OECD Model Tax Convention and the Commentaries relating thereto that the concept of 'beneficial owner' excludes conduit companies and must be understood not in a narrow technical sense but as having a meaning that enables double taxation to be avoided and tax evasion and avoidance to be prevented.

With reference to abuse of law[1], when examining the structure of the group it is immaterial that some of the beneficial owners of the interest paid by the conduit company are resident for tax purposes in a third

1 The judgment included some statements of the joined cases C-116 and C-117, explained above.

State which has concluded a Double Tax Treaties with the source Member State; in fact, the existence of such a Double Tax Treaties cannot in itself rule out an abuse of rights. Whilst taxation must correspond to economic reality, the existence of a Double Tax Treaties is not, as such, capable of establishing that a payment was really made to recipients resident in the third State with which that convention has been concluded.

The judgment at issue included some examples of artificial constructions: such indications are capable of being constituted not only by a contractual or legal obligation of the company receiving interest to pass it on to a third party but also by the fact that, 'in substance', as the referring Court states in Cases C-115/16, C-118/16 and C-119/16, that company, without being bound by such a contractual or legal obligation, does not have the right to use and enjoy those sums (see on this regard Commentary to article 11 of OECD Model Tax Convention against double taxation and the OECD Report "*Clarification of the meaning of* "*beneficial owner*" in the OECD Model Tax Convention).

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EUROPEAN TAX NEWSLETTER | FEBRUARY 2019

LEGISLATION, MINISTERIAL GUIDANCE AND CASE LAW AT 28 FEBRUARY 2019.
THIS NEWSLETTER IS INTENDED AS A SUMMARY OF KEY DEVELOPMENTS AND HIGHLIGHTS MATTERS OF GENERAL INTEREST, AND THEREFORE SHOULD NOT BE USED AS A BASIS FOR DECISION-MAKING.
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