The General Anti-Abuse Rule of the Parent-Subsidiary Directive - Interpretation and Effects

Author: Antti Vanhanen University of Helsinki Faculty of Law Master's thesis Financial law March 2016 Supervisor: Marjaana Helminen



HELSINGIN YLIOPISTO

HELSINGFORS UNIVERSITET

Tiedekunta/Osasto Fakultet/Sektion - Faculty Laitos/Institution- Department Faculty of Law Tekijä/Författare – Author Antti Samuli Vanhanen Tvön nimi / Arbetets titel – Title The General Anti-Abuse Rule of the Parent-Subsidiary Directive - Interpretation and Effects Oppiaine /Läroämne – Subject Financial law Työn laji/Arbetets art – Level Aika/Datum - Month and year Sivumäärä/ Sidoantal - Number of pages Master's thesis March 2016 xxii + 76 Tiivistelmä/Referat – Abstract The past few years have seen a surge of new political initiatives with the aim of combating tax evasion and tax avoidance. As a part of these initiatives on the level of the European Union, the Council enacted in January 2015 a new general anti-abuse provision to the Parent-Subsidiary Directive. The Parent-Subsidiary Directive regulates tax benefits to cross-border distributions in the EU with the purpose of eliminating obstacles to formation of corporate groups across the Member State borders. The Directive contained previously a provision that authorized the Member States to apply their national anti-abuse provisions within the scope of the Directive although the application of these provisions was voluntary, and the content and scope of the national provisions was not regulated by the Directive. In the words of the Commission, the purpose of the change was to prevent misuse of the Directive and to create consistency, and these aims were to be achieved by introduction of a common anti-abuse rule in all the Member States. The new general anti-abuse rule in the Parent-Subsidiary Directive represents an approach without precedents in the field of European direct tax law since it creates a detailed anti-abuse provision with the objective of harmonizing the national anti-abuse rules applicable to the benefits of the Directive. Most of all, the Member States are, from now on, obliged to combat abuse within the scope of the Directive since the new provision has to be implemented and applied nationally. The provision raises, however, several guestions regarding its application and its effects as a part of European tax legislation. The wording of the provision, which contains several conditions with the aim of defining abuse in the context of the Directive, reflects the varying formulations the ECJ has used in its case law on anti-abuse measures. It may appear prima facie that the provision marks a departure from the consistent case law and creates a new concept of abuse in the field of European tax law. The purpose of the research is to discuss the possible interpretations and the impact of the new provision. The different conditions of the provision are evaluated in the light of the ECJ case law in order to clarify their scope and meaning. The effects of the provision are discussed with respect to the immediate effects of its application, the effects on the Member States and their national anti-abuse rules, and the possible conflicts with the primary law of the EU. The ECJ direct tax case law contains a line of case law where the Court has examined abuse of tax law and the possibility to enact measures in order to combat abusive transactions. The concept of abuse within the field of European direct tax law has been developed especially in relation to such Member State anti-abuse measures which have had restrictive effects on the fundamental freedoms. In this case law, the ECJ has required that these anti-abuse provisions must combat only "wholly artificial arrangements", and the Court has developed specific tests which the national rules must respect when establishing the abusive nature of a transaction. This case law is discussed extensively in order to establish the possible interpretations for the new provision. Regarding the interpretation of the new anti-abuse provision, most questions arise in relation to the relevance of tax purposes and the genuine-nature of the arrangement. Given the variance in the ECJ case law, several ways to interpret the provision are compared in order to establish the most reasonable interpretation. In addition, the discussion reveals different points of uncertainty with regard to the way how the benefits of the Directive are meant to be denied and how the implementation of the provision affects national anti-abuse clauses and the freedom of movement. The research establishes that the new anti-abuse provision can be interpreted in accordance with the established ECJ case law although the wide latitudes of the provision mean that it can be subjected to various interpretations. The most important effects of the provision reside in its compulsory application and the impact on national legislation. The provision can, effectively, prevent the national legislators from adopting different solutions in its scope of application. The actual consequences for the companies that fall within the ambit of the provision contain several questions that cannot be given an unequivocal answer based on the wording of the provision alone. Most of all, the provision is set to cause uncertainty before its scope has been definitely scrutinized by the ECJ. Avainsanat – Nyckelord – Keywords European Tax Law, the Parent-Subsidiary Directive, Anti-Abuse Provision, General Anti-Abuse Rule, Tax Abuse, Tax Avoidance, Tax Evasion Säilytyspaikka – Förvaringställe – Where deposited Muita tietoja – Övriga uppgifter – Additional information

Index

Indexii	i
Sources	V
Literature	V
EU Legislationxiv	V
Other EU Sources	V
Case Law of the European Court of Justicexv	i
Other International Sources	K
National Legislationxx	K
National Preparatory Materialsxx	i
Abbreviationsxx	i
1 Introduction and the Research Questions	1
1.1 Introduction	1
1.2 Research Questions and Limitations	2
1.3 Research Methods	3
1.4 Outline of the Research	1
	1
2 European Direct Taxation, Prevention of Tax Abuse and the PSD	
 2 European Direct Taxation, Prevention of Tax Abuse and the PSD	1
	_
2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination	7
 2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination 2.2 Rule of Reason and Abuse of Tax Law	7 7
 2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination 2.2 Rule of Reason and Abuse of Tax Law	7 7 8
 2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination 2.2 Rule of Reason and Abuse of Tax Law	7 7 8
 2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination	7 7 8 1
 2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination	7 7 8 1 2
 2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination	7 7 8 1 2 3

2.5 General Features of the New Anti-Abuse Provision	16
3 Interpretation of the Anti-Abuse Provision	19
3.1 An Arrangement or a Series of Arrangements	19
3.1.1 Which Arrangement are Caught by the Provision	19
3.1.2 Part of an Arrangement	21
3.2 Main Purpose of Obtaining a Tax Advantage	
3.2.1 General Remarks	
3.2.2 Main Purpose or One of the Main Purposes	24
3.2.3 Further Questions Related to the Purpose Test	31
3.2.4 Obtainment of a Tax Advantage	
3.3 How the Purpose of the Directive is Defeated	
3.4 Non-Genuine Transactions	39
3.4.1 General Notions on the Concept	39
3.4.2 Valid Commercial Reasons	40
3.4.3 Economic Reality	43
3.4.4 The Level of Required Artificiality	47
3.5 Conclusions on the Interpretation of the PSD Anti-Abuse Rule	49
4 Effects of the Provision as a Part of European Direct Tax Legislation	51
4.1 How the Provision is Applied	51
4.1.1 What Benefits are Denied and How Double Taxation is Relieved?	51
4.1.2 Can Similar Benefits be Obtained from Other Bases?	54
4.1.3 Which Taxpayers are Denied the Benefits?	55
4.1.4 The Obligation to Combat Abuse	57
4.2 National Implementation of the Anti-Abuse Provision	60
4.2.1 The Way of Implementation	60
4.2.2 Legislative Choices in the Member States	62
4.3 Application of Other Anti-Abuse Provisions	64

4.4 The PSD Anti-Abuse Provision and the EU Primary Law	67
4.4.1 Does the Provision Create a Restriction on the Fundamental Freedoms?	67
4.4.2 Is the Provision Consistent with the Principle of Subsidiarity?	71
4.4.3 Does Application of the Provision in the Member States Create a Restriction?	72
5 Conclusions	73

Sources

Literature

Aarnio Aulis, Laintulkinnan Teoria: yleisen oikeustieteen oppikirja, 1989 WSOY (Aarnio 1989)

Allevi Laura - Celesti Chiara, 10th GREIT Annual Conference on *EU BEPS; Fiscal Transparency, Protection of Taxpayer Rights and State Aid* and 7th GREIT Summer Course on *Tax Evasion, Tax Avoidance & Aggressive Tax Planning*, Intertax 1/2016 p. 70-96 (Allevi - Celesti 2016)

Almendral Violeta Ruiz, Tax Avoidance and the European Court of Justice: What is at Stake for European General Anti-Avoidance Rules? Intertax 12/2005 p. 562-583 (Almendral 2005)

Brokelind Cécile, Une interpretation de la directive sociétés mères et filiales du 23 juillet 1990, 2000 Studentlitteratur (Brokelind 2000)

Brokelind Cécile, Ten years of application of the Parent-Subsidiary Directive, EC Tax Review 3/2003 p. 158-167 (Brokelind 2003)

Brokelind Cécile, Legal Issues in Respect of the Changes to the Parent-Subsidiary Directive as a Follow-Up of the BEPS Project, Intertax 12/2015 p. 816-824 (Brokelind 2015)

Cerioni Luca, The "Abuse of Rights" in EU Company Law and EU Tax Law: A Rereading of the ECJ Case Law and the Quest for a Unitary Notion, European Business Law Review 6/2010 p. 783-813 (Cerioni 2010) Cordewener Axel, Free Movement of Capital between EU Member States and Third-Countries: How Far Has the Door Been Closed? EC Tax Review 6/2009 p. 260-263 (Cordewener 2009)

Dahlberg Mattias, Direct Taxation in Relation to the Freedom of Establishment and the Free Movement of Capital, 2005 Kluwer Law International (Dahlberg 2005)

Debelva Filip - Luts Joris, The General Anti-Abuse Rule of the Parent-Subsidiary Directive, European taxation 6/2015 p. 223-234 (Debelva - Luts 2015)

de Broe Luc, International Tax Planning and Prevention of Abuse, 2008 IBFD (de Broe 2008)

de Broe Luc, Some observations on the 2007 communication from the Commission: "The application of anti-abuse measures in the area of direct taxation within the EU and in relation to third countries", EC Tax Review 3/2008 p. 142-148 (de Broe 2008a)

de la Feria Rita, Prohibition of Abuse of (Community) Law: the Creation of a New General Principle of EC Law Through Tax, Common Market Law Review 2/2008 p. 395-441 (de la Feria 2008)

Dougan Michael, Minimum Harmonization and the Internal Market, Common Market Law Review 4/2000 p. 853-885 (Dougan 2000)

Englisch Joachim, Taxation of Cross-Border Dividends and EC Fundamental Freedoms, Intertax 4/2010 p. 197-221 (Englisch 2010)

Evers Maike - de Graaf Arnaud, Limiting Benefit Shopping: Use and Abuse of EC Law, EC Tax Review 6/2009 p. 279-298 (Evers - de Graaf 2009)

Evers Maike - de Graaf Arnaud, Limiting Benefit Shopping: Outline of a Measure to Counter Erosion of the Dividend Tax Base in the EU, EC Tax Review 6/2010 p. 238-246 (Evers - de Graaf 2010)

Freedman Judith, The Anatomy of Tax Avoidance Counteraction: Abuse of Law in a Tax Context at Member State and European Union Level, in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria - Stefan Vogenauer, 2011 Hart Publishing p. 365-380 (Freedman 2011) Grau Amparo - Herrera Pedro M., The link between tax coordination and tax harmonization: limits and alternatives, EC tax review 1/2003 p. 28-36 (Grau - Herrera 2003)

Helminen Marjaana, EU Tax Law - Direct Taxation, Third edition 2013 IBFD (Helminen 2013)

Helminen Marjaana, The Principle of Elimination of Double Taxation under EU Law -Does it Exist? in Principles of Law: Function, Status and Impact in EU Tax Law, ed. Cécile Brokelind, 2014 IBFD p. 391-412 (Helminen 2014)

Hilling Maria, Justifications and Proportionality: An Analysis of the ECJ's Assessment of National Rules for the Prevention of Tax Avoidance, Intertax 5/2013 p. 294-307 (Hilling 2013)

Hrehorovska Lucia, Tax Harmonization in the European Union, Intertax 3/2006 p. 158-166 (Hrehorovska 2006)

Isenbaert Mathieu, The Contemporary Meaning of 'Sovereignty' in the Supranational Context of the EC as Applied to the Income Tax Case Law of the ECJ, EC Tax Review 6/2009 p. 264-278. (Isenbaert 2009)

Jimenez Adolfo Martin, Towards a Homogeneous Theory of Abuse in EU (Direct) Tax Law, Bulletin For International Taxation 4/5/2012 p. 270-292 (Jimenez 2012)

Kiekebeld Ben, Anti-Abuse in the Field of Taxation: Is There One Overall Concept? EC Tax Review 4/2009 p. 144-145 (Kiekebeld 2009)

Kingston Suzanne, A Light in the Darkness: Recent Developments in the ECJ's Direct Tax Jurisprudence, Common Market Law Review 5/2007 p. 1321-1359 (Kingston 2007)

Knobbe-Keuk Brigitte, The EC Corporate tax directives – anti-abuse provisions, direct effect, German implementation law, Intertax 8/9/1992 p. 485-494 (Knobbe-Keuk 1992)

Kofler Georg - Tumpel Michael, "Abuse" in Direct and Indirect Community Tax Law: A Convergence of Standards? in Value Added Tax and Direct Taxation - Similarities and Differences, ed. Michael Lang - Peter Melz - Eleonor Kristoffersson, 2009 IBFD p. 471-481 (Kofler - Tumpel 2009)

Kofler Georg - Tenore Mario, Fundamental Freedoms and Directives in the Area of Direct Taxation, in Traditional and Alternative Routes to European Tax Integration, ed. Dennis Weber, 2010 IBFD p. 311-360 (Kofler - Tenore 2010)

Lang Michael, *Cadbury Schweppes*' Line of Case Law from the Member States' Perspective, in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria - Stefan Vogenauer, 2011 Hart Publishing p. 435-458 (Lang 2011)

Lyal Richard, *Cadbury Schweppes* and Abuse: Comments in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria - Stefan Vogenauer, 2011 Hart Publishing p. 427-434 (Lyal 2011)

Melbi Ingrid, Förslag till ändring i EUs moder-dotterbolagsdirektiv, Skattenytt 3/2014 p. 134-139 (Melbi 2014)

Merks Paulus, Tax Evasion, Tax Avoidance and Tax Planning, Intertax 5/2006 p. 272-281 (Merks 2006)

Mortelmans Kamiel, The Relationship between the Treaty Rules and Community Measures for the Establishment and the Functioning of the Internal Market - Towards a Concordance Rule, Common Market Law Review 6/2002 p. 1303-1346 (Mortelmans 2002)

Panayi Christiana, Treaty Shopping and Other Tax Arbitrage Opportunities in the European Union: A Reassessment – Part 2, European Taxation 4/2006 p. 139-155 (Panayi 2006)

Peteva Jenia, Abuse Under EC Tax Law and the Standard of Review of the European Court of Justice, in Value Added Tax and Direct Taxation - Similarities and Differences, ed. Michael Lang - Peter Melz - Eleonor Kristoffersson, 2009 IBFD p. 483-499 (Peteva 2009)

Petrosovich Katrina, Abuse under the Merger Directive, European Taxation 12/2010 p. 558-567 (Petrosovich 2010)

Piantavigna Paolo, Prohibition of Abuse of Law: A New General Principle of EU Law? 3-4 October 2008, Oxford (UK), Intertax 3/2009 p. 166-175 (Piantavigna 2009) Piantavigna Paolo, Tax Abuse in European Union Law: A Theory, EC Tax Review 3/2011 p. 134-147 (Piantavigna 2011)

Picq Emmanuel, "Abuse" of EU Holding Companies: Fundamental Freedoms, EC Parent-Subsidiary Directive and the French Constitution - Part 1, European Taxation 10/2009 p. 471-478 (Picq 2009)

Picq Emmanuel, "Abuse" of EU Holding Companies: Fundamental Freedoms, EC Parent-Subsidiary Directive and the French Constitution - Part 2, European Taxation 11/2009 p. 534-541 (Picq 2009a)

Pistone Pasquale, The Need for Tax Clarity and the Application of the *Acte Clair* Doctrine for Direct Taxes, Intertax 10/2007 p. 534-536 (Pistone 2007)

Poulsen Martin, Freedom of Establishment and the Balanced Allocation of Tax Jurisdiction, Intertax 3/2012 p. 200-211 (Poulsen 2012)

Poulsen Martin, Directive/Treaty Shopping and Abuse of EU Law, Intertax 4/2013 p. 230-251 (Poulsen 2013)

Raby Nick, National Implementation of the Parent-Subsidiary Directive: Some Problems and Opportunities Identified, EC Tax Review 4/1992 p. 216-223 (Raby 1992)

Richardson Mirurgia, Fighting Tax Fraud and Tax Evasion in the EU: The 2012 Action Plan, EC Tax Review 4/2015 p. 220-231 (Richardson 2015)

Robert Eric - Tof Driss, The Substance Requirement and the Future of Domestic Anti-Abuse Rules within the Internal Market, European Taxation 11/2011 p. 436-444 (Robert - Tof 2011)

Rousselle Olivier - Liebman Howard M., The Doctrine of the Abuse of Community Law: The Sword of Damocles Hanging over the Head of EC Corporate Tax Law? European Taxation 12/2006 p. 559-564 (Rousselle - Liebman 2006)

Rädler Albert J. - Lausterer Martin - Blumenberg Jens, Tax abuse and EC law, EC Tax Review 2/1997 p. 86-101 (Rädler - Lausterer - Blumenberg 1997)

Schaper Marcel, The Structure and Organization of EU Law in the Field of Direct Taxes, 2013 IBFD (Schaper 2013)

Schelpe Dirk, The Denkavit-Vitic-Voormeer Case, EC Tax Review 1/1997 p. 17-22 (Schelpe 1997)

Schrauwen Annette, Sources of EU Law for Integration in Taxation, in Traditional and Alternative Routes to European Tax Integration, ed. Dennis Weber, 2010 IBFD p. 15-28 (Schrauwen 2010)

Snell Jukka, The Notion of and a General Test for Abuse of Rights: Some Normative Reflections, in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria - Stefan Vogenauer, 2011 Hart Publishing p. 219-231 (Snell 2011)

Sørensen Karsten Engsig, Abuse of Rights in Community Law: a Principle of Substance or Merely Rhetoric? Common Market Law Review 2/2006 p. 423-459 (Sørensen 2006)

Sørensen Karsten Engsig, What is a General Principle of EU Law? A Response, in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria -Stefan Vogenauer, 2011 Hart Publishing p. 25-32 (Sørensen 2011)

Sørensen Karsten Engsig, Reconciling Secondary Legislation and the Treaty Rights of Free Movement, European Law Review 3/2011 p. 339-361 (Sørensen 2011a)

Sørensen Karsten Engsig, The Fight Against Letterbox Companies in the Internal Market, Common Market Law Review 1/2015 p. 85-117 (Sørensen 2015)

Ståhl Kristina - Persson Österman Roger, EG Skatterätt, Upplaga 2 2006 Iustus Förlag (Ståhl - Persson Österman 2006)

Ståhl Kristina, National Courts' Treatment of Tax Rules that Conflict with the EC Treaty, Intertax 12/2008 p. 548-553 (Ståhl 2008)

Syrpis Phil, The Relationship between Primary and Secondary Law in the EU, Common Market Law Review 2/2015 p. 461-487 (Syrpis 2015)

Szudoczky Rita, The Influence of Primary Law on the Interpretation of Secondary Law in the Field of EU Citizenship and Direct Taxation: "Whatever works"..., in Traditional and Alternative Routes to European Tax Integration, ed. Dennis Weber, 2010 IBFD p. 191-227 (Szudoczky 2010)

Tavares J.S. Romero - Bogenschneider Bret N., The New *De Minimis* Anti-abuse Rule in the Parent-Subsidiary Directive: Validating EU Tax Competition and Corporate Tax Avoidance? Intertax 8/9/2015 p. 484-494 (Tavares - Bogenschneider 2015)

Tenore Mario, The Scope for "Consistent Interpretation" in the Area of Dividend Taxation, in Legal Remedies in European Tax Law, ed. Pasquale Pistone, 2009 IBFD p. 27-44 (Tenore 2009)

Tenore Mario, Taxation of Cross-Border Dividends in the European Union from Past to Future, EC Tax Review 2/2010 p. 74-84 (Tenore 2010)

Tenore Mario, Taxation of Dividends: A Comparison of Selected Issues under Article 10 OECD MC and the Parent-Subsidiary Directive, Intertax 4/2010 p. 222-238 (Tenore 2010a)

Terra Ben J.M. - Wattel Peter J., European Tax Law, 2012 Kluwer Law International (Terra - Wattel 2012)

van den Hurk Hans, Proposed Amended Parent-Subsidiary Directive Reveals the European Commission's Lack of Vision, Bulletin for International Taxation 9/2014 p. 488-497 (van den Hurk 2014)

Vanistendael Frans, The compatibility of the basic economic freedoms with the sovereign national tax systems of the Member States, EC Tax Review 3/2003 p. 136-143 (Vanistendael 2003)

Vanistendael Frans, *Halifax* and *Cadbury Schweppes*: one single European theory of abuse in tax law? EC Tax Review 4/2006 p. 192-195 (Vanistendael 2006)

Vanistendael Frans, *Cadbury Schweppes* and Abuse from an EU Law Perspective, in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria - Stefan Vogenauer, 2011 Hart Publishing p. 407-425 (Vanistendael 2011)

van Thiel Servaas, Justifications in Community Law for Income Tax Restrictions on Free Movement: *Acte Clair* Rule That Can Be Readily Applied by National Courts – Part 1, European Taxation 7/2008 p. 279-290 (van Thiel 2008) van Thiel Servaas, Refund of Taxes and Charges Collected Contrary to Community Law, in Legal Remedies in European Tax Law, ed. Pasquale Pistone, 2009 IBFD p. 287-322 (van Thiel 2009)

Vinther Nikolaj - Werlauff Erik, Tax Motives are Legal Motives – The Borderline between the Use and Abuse of the Freedom of Establishment with Reference to the *Cadbury Schweppes* Case, European Taxation 8/2006 p. 383-387 (Vinther - Werlauff 2006)

Vogenauer Stefan, The Prohibition of Abuse of Law: An Emerging General Principle of EU Law, in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria - Stefan Vogenauer, 2011 Hart Publishing p. 521-571 (Vogenauer 2011)

Wattel Peter, Non-Discrimination à *la Cour*: The ECJ's (Lack of) Comparability Analysis in Direct Tax Cases, European Taxation 12/2015 p. 542-553 (Wattel 2015)

Weber Dennis, A closer look at the general anti-abuse clause in the Parent-Subsidiary Directive and the Merger Directive, EC Tax Review 2/1996 p. 63-69 (Weber 1996)

Weber Dennis, The first steps of the ECJ concerning an abuse-doctrine in the field of harmonized direct taxes, EC Tax Review 1/1997 p. 22-31 (Weber 1997)

Weber Dennis, Tax Avoidance and the EC Treaty Freedoms, 2005 Kluwer Law International (Weber 2005)

Weber Dennis, In Search of a (New) Equilibrium Between Tax Sovereignty and the Freedom of Movement Within the EC, Intertax 12/2006 p. 585-615 (Weber 2006)

Weber Dennis, Some Remarks on the Application of Community Law, Its Legal Effects and the Relationship between These Concepts, in Legal Remedies in European Tax Law, ed. Pasquale Pistone, 2009 IBFD p. 45-67 (Weber 2009)

Weber Dennis, Abuse of Law in the Context of Indirect Taxation: Why We Need the Subjective Intention Test, When is Combating Abuse an Obligation and Other Comments, in Prohibition of Abuse of Law – A New General Principle of EU Law, ed. Rita de la Feria - Stefan Vogenauer, 2011 Hart Publishing p. 395-406 (Weber 2011)

Weber Dennis, Abuse of Law in European Tax Law: An Overview and Some Recent Trends in the Direct and Indirect Tax Case Law of the ECJ - Part 1, European Taxation 6/2013 p. 251-264 (Weber 2013) Weber Dennis, Abuse of Law in European Tax Law: An Overview and Some Recent Trends in the Direct and Indirect Tax Case Law of the ECJ - Part 2, European Taxation 7/2013 p. 313-328 (Weber 2013a)

Weber Dennis, The New Common Minimum Anti-Abuse Rule in the EU Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect, Intertax 2/2016 p. 98-129 (Weber 2016)

Wittock Nathalie, The Influence of the Principle of Union Loyalty in Tax Matters, EC Tax Review 4/2014 p. 171-188 (Wittock 2014)

Zalasinski Adam, Proportionality of Anti-Avoidance and Anti-Abuse Measures in the ECJ's Direct Tax Case Law, Intertax 5/2007 p. 310-321 (Zalasinski 2007)

Zalasinski Adam, Case-Law-Based Anti-Avoidance Measures in Conflict with Proportionality Test – Comment on the ECJ Decision in Kofoed, European Taxation 12/2007 p. 571-576 (Zalasinski 2007a)

Zalasinski Adam, Some Basic Aspects of the Concept of Abuse in the Tax Case Law of the European Court of Justice, Intertax 4/2008 p. 156-167 (Zalasinski 2008)

Zalasinski Adam, The Limits of the EC Concept of 'Direct Tax Restriction on Free Movement Rights', the Principles of Equality and Ability to Pay, and the Interstate Fiscal Equity', Intertax 5/2009 p. 282-297 (Zalasinski 2009)

Zalasinski Adam, The Principle of Prevention of (Direct Tax) Abuse: Scope and Legal Nature - Remarks on the *3M Italia* Case, European Taxation 9/2012 p. 446-454 (Zalasinski 2012)

Zalasinski Adam, The Principle of Proportionality and (European) Tax Law, in Principles of Law: Function, Status and Impact in EU Tax Law, ed. Cécile Brokelind, 2014 IBDF p. 303-317 (Zalasinski 2014)

Äimä Kristiina, EY-oikeudellisista periaatteista ja tulkinnasta erityisesti vero-oikeuden alalla, Verotus /1999 p. 494-504 (Äimä 1999)

EU Legislation

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

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

Council Directive 2003/123/EC of 22 December 2003 amending Directive 90/435/EEC on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States

Council Directive 2009/133/EU 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

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

Council Directive 2014/86/EU of 8 July 2014 amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States

Council Directive (EU) 2015/121 of 27 January 2015 amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States

Other EU Sources

Opinion of Mr Advocate General Alber delivered on 24 September 2002, Bosal Holding BV v Staatssecretaris van Financiën

Joined opinion of Mr Advocate General Poiares Maduro delivered on 7 April 2005, Halifax plc, Leeds Permanent Development Services Ltd and County Wide Property Investments Ltd v Commissioners of Customs & Excise

Opinion of Mr Advocate General Léger delivered on 2 May 2006, Cadbury Schweppes plc and Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue Opinion of Mr Advocate General Geelhoed delivered on 29 June 2006, Test Claimants in the Thin Cap Group Litigation v Commissioners of Inland Revenue

Opinion of Advocate General Kokott delivered on 8 February 2007, Hans Markus Kofoed v Skatteministeriet

Opinion of Advocate General Mengozzi delivered on 29 March 2007, Columbus Container Services BVBA & Co. v Finanzamt Bielefeld-Innenstadt

Opinion of Advocate General Kokott delivered on 16 July 2009, Modehuis A. Zwijnenburg BV v Staatssecretaris van Financiën.

COM(2006) 254 Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee, concerning the need to develop a coordinated strategy to improve the fight against fiscal fraud

COM(2007) 785 Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee, The application of antiabuse measures in the area of direct taxation – within the EU and in relation to third countries

COM(2012) 722 Communication from the Commission to the European Parliament and the Council, An Action Plan to strengthen the fight against tax fraud and tax evasion

C(2012) 8806 Commission recommendation of 6.12.2012 on aggressive tax planning

COM(2013) 814 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

SWD(2013) 474 Commission Staff Working Document Impact Assessment, Accompanying the document, 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

MEMO/13/1040 European Commission Memo, Brussels, 25 November 2013, Questions and Answers on the Parent Subsidiary Directive

Political agreement, Brussels, 5 December 2014, no. 16435/14, 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(2015) 302 Communication from the Commission to the European Parliament and the Council, A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action

COM(2016) 26 Proposal for a Council Directive laying down rules against tax avoidance practices that directly affect the functioning of the internal market

Case Law of the European Court of Justice

C-33/74 Van Binsbergen

C-106/77 Simmenthal

C-115/78 Knoors

C-14/83 Von Colson

C-229/83 Leclerc

C-270/83 Avoir fiscal

C-79/85 Segers

C-14/86 Pretore di Salò

C-39/86 Lair

C-80/86 Kolpinghuis Nijmegen

C-175/88 Biehl

C-106/89 Marleasing

C-221/89 Factortame

C-279/93 Schumacker

C-55/94 Gebhard

Joined Cases C-283/94, C-291/94 and C-292/94 Denkavit-VITIC-Voormeer

C-28/95 Leur-Bloem

C-264/96 ICI

C-367/96 Kefalas

C-212/97 Centros

C-294/97 Eurowings

C-311/97 Royal Bank of Scotland

C-35/98 Verkooijen

C-251/98 Baars

C-375/98 Epson

C-376/98 Tobacco Advertising

C-476/98 Open Skies

C-110/99 Emsland-Stärke

C-141/99 AMID

C-294/99 Athinaïki

C-62/00 Marks & Spencer

C-136/00 Danner

C-324/00 Lankhorst-Hohorst

C-436/00 X and Y

C-58/01 Océ Van der Grinten

C-167/01 Inspire Art

C-168/01 Bosal Holding

C-422/01 Skandia and Ramstedt

C-9/02 De Laysterie du Saillant

C-255/02 Halifax

C-315/02 Lenz

C-319/02 Manninen

C-446/03 Marks & Spencer

C-456/03 Commission v Italy

C-196/04 Cadbury Schweppes

C-374/04 ACT Group Litigation

C-386/04 Stauffer

C-428/04 Commission v Austria

C-446/04 FII Group Litigation

C-471/04 Keller Holding

C-513/04 Kerckhaert-Morres

C-524/04 Thin Cap Group Litigation

C-157/05 Holböck

C-170/05 Denkavit

C-231/05 Oy AA

C-298/05 Columbus Container Services

C-321/05 Kofoed

C-379/05 Amurta

C-451/05 ELISA

C-284/06 Burda

C-425/06 Part Service

C-27/07 Banque Fédérative du Crédit Mutuel C-48/07 Les Vergers du Vieux Tauves C-105/07 Lammers & Van Cleeff C-138/07 Cobelfret C-162/07 Ampliscientifica C-303/07 Aberdeen C-330/07 Jobra Joined Cases C-22/08 and C-23/08 Vatsouras-Koupatantze C-67/08 Block C-96/08 CIBA C-128/08 Damseaux C-182/08 Glaxo Wellcome C-248/08 Gaz de France C-311/08 SGI C-352/08 Zwijnenburg Joined Cases C-436/08 and C-437/08 Haribo-Salinen C-103/09 Weald Leasing C-277/09 RBS Deutschland C-126/10 Foggia C-318/10 SIAT C-371/10 National Grid Indus C-417/10 3M Italia C-504/10 Tanoarch

C-322/11 K

C-387/11 Commission v Belgium

C-653/11 Newey

C-80/12 Felixstowe

C-282/12 Itelcar

Joined cases C-39/13, C-40/13 and C-41/13 SCA Group Holding BV-X AG and Others-MSA International Holdings BV and MSA Nederland BV

Other International Sources

OECD, Action Plan on Base Erosion and Profit Shifting, 19.7.2013

National Legislation

Lov nr 540 af 29/04/2015 Lov om ændring af ligningsloven, boafgiftsloven, fondsbeskatningsloven, skatteforvaltningsloven og forskellige andre love (Denmark)

Laki elinkeinotulon verottamisesta 24.6.1968/360 (Finland)

Loi nº 2015 - 1786 du 29 décembre 2015 de finances rectificative pour 2015, publiée au Journal Officiel du 30 décembre 2015 (France)

Wet van 23 december 2015 tot wijziging van de Wet op de vennootschapsbelasting 1969 en de Wet op de dividendbelasting 1965 in verband met de implementatie van aanpassingen in de Moeder-dochterrichtlijn (Wet implementatie wijzigingen Moederdochterrichtlijn 2015) (Netherlands)

Decreto N.º 10/XIII Altera o Código do Imposto sobre o Rendimento das Pessoas Coletivas, aprovado pelo Decreto-Lei n.º 442-B/88, de 30 de novembro, transpondo a Diretiva 2015/121/UE, do Conselho, de 27 de janeiro de 2015 (Portugal)

Kupongskattelag 1970:624 (Sweden)

National Preparatory Materials

Hallituksen esitys HE 59/2015 vp Hallituksen esitys eduskunnalle laiksi elinkeinotulon verottamisesta annetun lain 6 a §:n muuttamisesta (Finland)

Valiokunnan mietintö VaVM 13/2015 vp - HE 59/2015 vp Hallituksen esitys eduskunnalle laiksi elinkeinotulon verottamisesta annetun lain 6 a §:n muuttamisesta (Finland)

Eduskunnan vastaus EV 81/2015 vp - HE 59/2015 vp Hallituksen esitys eduskunnalle laiksi elinkeinotulon verottamisesta annetun lain 6 a §:n muuttamisesta (Finland)

Elinkeinoelämän keskusliitto, Muistio Hallituksen esitys eduskunnalle laiksi elinkeinotulon verottamisesta annetun lain 6 a §:n muuttamisesta 12.11.2015 (Finland)

Suomen Yrittäjät, Lausunto hallituksen esityksestä laiksi elinkeinotulon verottamisesta annetun lain 6 a §:n muuttamisesta 12.11.2015 (Finland)

Wijziging van de Wet op de vennootschapsbelasting 1969 en de Wet op de dividendbelasting 1965 in verband met de implementatie van aanpassingen in de Moederdochterrichtlijn (Wet implementatie wijzigingen Moeder-dochterrichtlijn 2015) (Netherlands)

34306 Nr. 3 Memorie van toelichting, 15 September 2015 (Netherlands)

34306 Nr. 4 Advies Afdeling advisering Raad van State en Nader rapport, 15 September 2015 (Netherlands)

Skatteutskottets utlåtande 2013/14:SkU23 Subsidiaritetsprövningen av kommissionens förslag om ändring av direktiv 2011/96/EU om ett gemensamt beskattningssystem för moderbolag och dotterbolag hemmahörande i olika medlemstater (Sweden)

Finansdepartementet, Skatte- och tullavdelningen April 2015 Begränsad skattefrihet för utdelning och nya bestämmelser mot skatteflykt i fråga om kupongskatt (Sweden)

Regeringens proposition 2015/16:14 Begränsad skattefrihet för utdelning och nya bestämmelser mot skatteflykt i fråga om kupongskatt (Sweden)

Abbreviations

EU European Union

xxi

ECJ	European Court of Justice
PE	Permanent establishment
PSD	Parent-Subsidiary Directive
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
VAT	Value-added tax

1 Introduction and the Research Questions

1.1 Introduction

Preventing tax abuse and tax evasion has been high on the political agenda of many governments in the past few years. The most important example of the initiatives to combat this phenomenon has been the BEPS-project launched by OECD and the G20-countries which aims to develop solutions to prevent misuse of differences in national tax legislations.¹ Equally in the EU, addressing these problems has received increasing attention, and the Commission published in 2012 an Action Plan to combat tax evasion and tax fraud where several initiatives to control these issues were presented.²

The Action Plan proposed, among other things, the revision of direct tax directives in a way that mitigates the problems related to their misuse. In January 2015, the Council enacted the Directive 2015/121/EU amending the Parent-Subsidiary Directive (Directive 2011/96/EU hereinafter "PSD") which introduced a new, general anti-abuse provision aiming to prevent abuse of the benefits of the Directive. The former Article 1(2) of the PSD included only an authorization enabling the Member States to apply their domestic anti-abuse provisions which did not include, however, any specifications on these provisions. By enacting a general, common anti-abuse rule which the Member States must implement in their legislation, the EU tries to lessen the disparities in the Member State anti-abuse measures and create consistency.³ If the situation is found to be abusive by the criteria of the provision, the Member States have to deny the benefits of the Directive.

The approach of enacting an obligatory general anti-abuse provision is new to the European tax law. The approach is in line with the EU recommendation on aggressive tax planning where a general anti-abuse rule was proposed to be taken to Member States legislations.⁴ Besides the anti-abuse rules in direct tax directives, the ECJ has created an expanding field of case law on abuse of law. In the field of tax law, this approach has taken various forms but, most relevantly, the ECJ has required the national anti-abuse rules to target only "wholly artificial arrangements."⁵

¹ See the BEPS 15-step Action Plan which was accepted in July 2013.

² See COM(2012) 722.

³ See recitals 2-5 of the Directive 2015/121/EU and COM(2013) 814 p. 2-5.

⁴ See Directives 2009/133/EU Art. 15 (Merger Directive) and 2003/49/EC Art. 5 (Interest-royalty Directive). See also recommendation C(2012) 8806.

⁵ See e.g. C-446/03 *Marks & Spencer* para. 57 and C-196/04 *Cadbury Schweppes* para. 55.

The new anti-abuse rule raises several questions on its application since the conditions laid down in the provision are relatively broadly formulated. An important issue is, therefore, how the provision should actually be applied and which situations fall within its scope. In other words, how the new PSD anti-abuse provision situates itself within the field of European tax law with regard to the various strains of the ECJ case law. As the PSD applies only to cross-border distributions, the provision may create an additional burden on cross-border transactions. Given the established ECJ case law on national anti-abuse measures, it may be questioned whether this approach is suitable and whether its leads to the detriment of the objectives of PSD. On the other hand, there are legitimate reasons to counter tax-abuse, and the effectiveness the provision should be examined in the context of these objectives.

1.2 Research Questions and Limitations

The focus of this research is the new, general anti-abuse provision of the PSD and its interpretation. The research aims to answer the following questions. First, how can the provision be interpreted in the light of the ECJ case law and the ECJ doctrine on the prevention of abuse within the field of taxation? Second, what are the effects of its inclusion in the European direct tax legislation? The effects signify legal effects not e.g. economical or political effects. This question is examined with respect to effects caused by application of the provision, its implementation, relation with the legislation of the Member States, and the EU primary law. By answering these questions, the purpose is to form an understanding of the real significance of the new provision.

The research discusses the ECJ anti-abuse doctrine with the aim of interpreting the PSD anti-abuse provision. The research is limited to the assessment of tax law on the European level, but an exception to this is formed by the observation of national legislative solutions that the Member States have adopted in implementing the new anti-abuse provision. The research does not intend to discuss, however, more in-depth the effects of the provision on existing Member State anti-abuse measures, and this relation is examined only on a general level without considering the specifics of individual domestic anti-abuse doctrines. The research is limited, by the virtue of its topic, to the field of direct taxation but, given the development of the concept of abuse within the ECJ case law, relevant cases from other fields of Union law are given consideration when necessary. Furthermore, the research does not attempt to discuss different ways to combat the abuse of the PSD or to propose and evaluate approaches that could achieve this aim more effectively.

1.3 Research Methods

Jurisprudence consists of different methodological currents. The methodology of this research is based on the methods of legal dogmatism. Legal dogmatism is a field of jurisprudence that concentrates on the research of legal rules currently in force. Its two main aims are interpretation, with the purpose of establishing the content of legal rules, and systemization, with the aim of organizing the legal rules in question.⁶ This research strives to form through the interpretation of the new anti-abuse provision a picture of its place and significance within the field of European tax law. Although the implementing legislation of the Member States is examined, the research does not purport to resort to the methodology of comparative law.

The research situates itself within the field of European tax law and, more broadly, the European law and international tax law. European law forms a supranational legal order which possesses its specific characteristics regarding the interpretation of legal rules and the significance legal sources. Of special importance for the research is the evaluation of the ECJ case law. The European law can be interpreted, *inter alia*, historically, literally, contextually, and teleologically. Especially the teleological interpretation, which signifies interpretation based on the purpose of the provision, has played an important role in the jurisprudence of the ECJ.⁷ Within the Internal Market, this interpretation means, essentially, an interpretation that is compatible with the objectives of the EU itself.

Furthermore, national legislation implementing EU secondary legislation must be interpreted in conformance with the objectives of this legislation.⁸ This has been stated also with regard to the direct tax directives, and their interpretation is based, besides the wording, on the purpose and objectives of these directives.⁹ Of further importance is that the directives itself, as secondary legislation, must be interpreted according to the EU primary law. This technique is used to clarify the scope of the secondary legislation and to find an interpretation that conforms best to the primary law and avoids collisions with it.¹⁰ This means that, besides the text of the new provision, also considerations related to the purpose of the PSD and the EU primary law must influence its interpretation.

⁶ On legal dogmatism, see Aarnio 1989 p. 48.

⁷ On different methods of interpretation in EU law, see Äimä 1999 p. 502-504.

⁸ On consistent interpretation, see Tenore 2009 p. 28-31. See also cases C-14/83 *Von Colson* para. 26, C-80/86 *Kolpinghuis Nijmegen* para. 12, and C-106/89 *Marleasing* para. 8.

⁹ See C-27/07 *Banque Fédérative du Crédit Mutuel* para. 22 and C-247/08 *Gaz de France* para. 26.

¹⁰ On the interpretation of secondary law, see Szudoczky 2010 p. 191-193.

1.4 Outline of the Research

The first part of the research concerns general questions related to European tax law relevant to the topic of the research. In this context, the main content of the ECJ doctrine on abuse of tax law is discussed as well as the relevant issues related to the freedom of movement. Furthermore, the PSD, its purpose, and the general features of the new antiabuse rule are examined in order to create foundations for further research.

The third chapter, which contains the second part of the research, examines the questions related to the interpretation of the new anti-abuse provision. The research advances based on the conditions which can be discerned from the wording of the provision and which are analyzed in the light of the ECJ case law. The objective of this section is to discuss possible interpretations that can be given to the new provision and the issues that these interpretations could create.

The fourth chapter deals with the effects that the application of the new provision may have in different contexts. First, it is examined which are the consequences of the provision on taxpayers that come within its scope of application. Second, questions related to the implementation of the provision in the Member States and its effects on national anti-abuse provisions are discussed. Third, the provision is contrasted with the fundamental freedoms in order to discuss the impact the provision has on the functioning of the freedom of movement and how the fundamental freedoms could affect the application of the provision.

2 European Direct Taxation, Prevention of Tax Abuse and the PSD

2.1 Tax Sovereignty, Freedom of Movement and the Prohibition of Discrimination

Despite the profound integration of many policy sectors, direct taxation has long remained within the competence of the Member States, and the EU does not have own taxation rights. The situation is called Member State tax sovereignty.¹¹ Since the primary law of the EU does not deal with direct taxation, the Member States can independently decide whether they are willing to collect taxes, at what rate, and in which circumstances although this tax sovereignty must not hinder the application of fundamental freedoms.¹² Most visibly, tax sovereignty means that the EU has as many different tax systems as there are Member

 ¹¹ See Isenbaert 2009 p. 266-267.
 ¹² On tax sovereignty, see Weber 2006 p. 586.

States, and the content of these systems is defined by the political decisions of the Member State in question which enables a Union-wide tax competition.¹³

Even though the Member States can, consequently, decide quite freely on the composition of their tax systems, this does not imply that taxation would not be relevant for the Internal Market. Differences between the tax systems of the Member States may create barriers to the free movement within the Union and cause disturbances since the taxpayers have to conform to several tax systems.¹⁴ The positive integration of direct taxation has been, however, relatively restricted. This is related to the limits of the harmonization options. The lack of explicit Treaty articles requires, in conformance with the principle of subsidiarity, that harmonization is necessary compared to actions of the Member States. A further, crucial obstacle is the unanimity requirement of the Article 115 TFEU which functions as an efficient brake to harmonization of tax legislation.¹⁵Achieving unanimity in the Council is challenging which means that removing the obstacles caused by national tax systems is not generally possible through harmonization.

On the other hand, negative integration and the case law of the ECJ have played an important role in the field of direct taxation. In spite of the fact that the Member States are free to decide the essential characteristics of their tax systems, taxation must not lead to restriction of the fundamental freedoms guaranteed by the TFEU. Although the Union does not have competence in the field of direct taxation, the ECJ has consistently stated that the national tax systems must be applied in accordance with the Union law.¹⁶ The TFEU forbids discrimination based on nationality (Article 18) and guarantees the free movement goods (Article 28), persons (Articles 21, 45 and 49), services (Article 56), and capital (Article 63) the application of which can be provoked in national courts. Union citizens come within the scope of the Treaty freedoms if they have exercised their freedom of movement which means that purely internal situations are not relevant.¹⁷

The ECJ has created an extensive case law on the application of the Treaty freedoms which has expanded from other sectors to direct taxation. The principal ideas of this case law are briefly established. The Treaty freedoms as such prohibit discrimination of cross-border

¹³ See Hrehorovska 2006 p. 158, 163.

¹⁴ See Terra - Wattel 2012 p. 198-199.

¹⁵ On the limits of harmonization, see Grau - Herrera 2003 p. 30-31. On the principle of subsidiarity, see Hrehorovska 2006 p. 163.

¹⁶ See, inter alia, C-279/93 Schumacker para. 21, C-311/97 Royal Bank of Scotland para. 19, C-196/04

Cadbury Schweppes para. 40, and C-374/04 *ACT Group Litigation* para. 36.

¹⁷ See Ståhl - Persson Österman 2006 p. 66-68 on the fundamental freedoms.

situations when compared with domestic equivalents. Companies and individuals which are judged to be in a similar situation should not face less advantageous tax treatment because of their nationality.¹⁸ Both direct and indirect discrimination is prohibited.¹⁹ The residents and non-residents may be judged to be in a comparable situation which prohibits diverging tax treatment.²⁰ Mere disparities that are caused by the existence of several national tax systems are not, however, discriminatory.²¹

In its case law, the ECJ has, nevertheless, expanded the scope of this approach to encompass also Member state legislation that forms "a restriction" to the freedom of movement while not explicitly discriminating between foreign and domestic operators. Originally developed elsewhere in the Union law, this doctrine has been later brought to the field of direct taxation.²² Obstacles to the freedom of movement, although not discriminatory, may constitute an illegal restriction if they're liable to prevent inter-state movement. Therefore, when national rules create such obstacles to cross-border situations which are not present in domestic ones, their application constitutes a breach of the Treaty. This approach is seen to have been modified or diluted in the more recent ECJ case law since it creates delicate problems with regard to national tax sovereignty.²³

As an illustration near the topic of this research, the influence of the fundamental freedoms on cross-border dividend taxation is given further observations. Taxation of dividends in the Member States comes within the scope of the freedom of establishment and the free movement of capital although a "definite influence test" has been used to distinguish between these two freedoms.²⁴ A Member State is not allowed to subject foreign-sourced dividends to less favorable tax treatment than to which domestically sourced dividends are subjected if the situations are deemed to be comparable.²⁵ For example, granting exemption from the income tax only in cases where the dividends are domestically-sourced is not in accordance with the freedom of movement.²⁶ Equally, outbound dividends should not be taxed in the source state less favorably than domestic dividends. In Denkavit, for

¹⁸ On the concept of discrimination, see Zalasinski 2009 p. 283-284.

¹⁹ On the definitions, see Dahlberg 2005 p. 67.

²⁰ See Vanistendael 2003 p. 136-137 and C-279/93 Schumacker paras. 36-38.

²¹ See Weber 2006 p. 588-594. See also Terra - Wattel 2012 p. 93-94.

 ²² See Zalasinski 2009 p. 285-288 and e.g. C-168/01 *Bosal Holding* para. 27.
 ²³ See Kingston 2007 p. 1335-1341 and Terra - Wattel 2012 p. 83-92.

²⁴ On the applicable freedoms, see English 2010 p. 199-201.

²⁵ See English 2010 p. 201-206. Further on the case law on inbound dividend taxation, see Tenore 2010 p. 78-81.

²⁶ See case C-35/98 Verkooijen para. 36. From other cases see C-315/02 Lenz paras. 20-22 and C-319/02 Manninen para. 55.

instance, a tax system which taxed cross-border dividends but exempted domestic dividends was deemed to be contrary to the freedom of movement.²⁷ All in all, the fundamental freedoms have had a profound impact on the way the dividends are taxed within the EU.

From this discussion, it is evident that the ECJ case law has widespread repercussions for direct taxation within the EU. Its main influence lies in the fact that even non-harmonized national legislation must conform to the Treaty freedoms and, consequently, to the ECJ case law. Because of these effects of the freedom of movement, there has been a need to develop justifications which can be revoked to justify restrictions to the freedoms.

2.2 Rule of Reason and Abuse of Tax Law

2.2.1 Treaty Justifications and Rule of Reason

Although the Member States must respect the fundamental freedoms when applying their national tax rules, they may, in some occasions, apply those rules in a way that would *prima facie* mean a breach these freedoms. In general, the Treaty justifications have only a narrow relevance as justification for direct tax measures.²⁸ The ECJ has, however, created the so called "rule of reason" doctrine according to which even such justifications that are not mentioned in the Treaties can be used to justify restrictive national measures. These exemptions must be applied in a non-discriminatory manner in order to secure a public interest. In addition, the measures must be proportionate and suitable to achieve these objectives.²⁹ There have been, however, some inconsistencies in whether only non-discriminatory measures can be justified.³⁰ In tax matters, the ECJ has been seen to have moved to a three-step justification where the measures must be justified by a legitimate aim, and must not restrict the fundamental freedoms more than necessary.³¹

The list of public interest justifications that have been rejected by the Court includes such justifications as loss of budget revenue and administrative difficulties. Justifications that the Court has accepted in its tax case law are, among others, effectiveness of fiscal

²⁷ See case C-170/05 *Denkavit* para. 41. On the case law on outbound dividends, see Tenore 2010 p. 75-78. From other cases see C-379/05 *Amurta* para. 61.

²⁸ See van Thiel 2008 p. 279, where the narrow scope of Treaty justifications is mentioned as the main obstacle to their application in direct tax matters.

²⁹ See Ståhl - Persson Österman 2006 p. 144-146. See also case C-55/94 *Gebhard* para. 37 for the definition of the conditions.

³⁰ See Weber 2005 p. 163.

³¹ See Terra - Wattel 2012 p. 63-64.

supervision, balanced allocation of taxation powers, prevention of abuse, coherence of tax system and the principle of territoriality even though fiscal coherence has been applied only in extremely rare occasions, and fiscal supervision has found equally restricted application.³² Although several justifications are usually revoked by the Member States at the same time, prevention of abuse is given further attention. This justification confers the Member States a right to apply their national anti-abuse rules if certain conditions, developed in the ECJ case law, are met.

2.2.2 Prevention of Abuse as Justification and the Prohibition of Abuse of Rights

Before discussing prevention of abuse as a justification, certain definitions are established. First, tax avoidance has been seen to signify reduction of tax burden trough legal means which may, however, be countered by national legislation. Tax abuse has been described as misuse of differences in the rights of the taxpayers through artificial arrangements, and it is situated near tax avoidance. Tax evasion, on the contrary, means illegal means to reduce the tax burden through withholding of information or giving false data.³³

Both within and outside the field of tax law, there has been a strain of ECJ case law where an independent, European principle prohibiting the abuse of rights has been developed.³⁴ The roots of this doctrine stem from the *Van Binsbergen* case in 1974 which has been followed by several cases in different fields of EU law.³⁵ In direct taxation, it was stated in *Kofoed* that there is a general principle of Community law which prohibits the abuse of rights.³⁶ In some cases, it is possible that the principle itself could be applied by the Member States to combat abuse.³⁷ It appears that in the field of harmonized indirect tax law (VAT), the principle of abuse of rights may find independent relevance in authorizing Member States to deny tax benefits in abusive situations without needing to recourse to national law. In the case of the Treaty freedoms, the application of the principle is possible only as a justification for national measures.³⁸ What is more, the application of anti-abuse

³² See van Thiel 2008 p. 280-282.

³³ On different definitions, see Zalasinski 2008 p. 158-161.

³⁴ On the existence of the principle, see de la Feria 2008 p. 436-441.

³⁵ See, *inter alia*, cases C-33/74 *Van Binsbergen* para. 13, C-115/78 *Knoors* para. 25, C-229/83 *Leclerc* para. 27, C-39/86 *Lair* para. 43, C-367/96 *Kefalas* para. 20 and C-212/97 *Centros* paras. 24-25. Comments on the development see Cerioni 2010 p. 784-787. See also Schaper 2013 p. 368-370.

³⁶ See C-312/05 *Kofoed* para. 38.

³⁷ See Sørensen 2006 p. 439-440.

³⁸ On different effects of the principle, see Zalasinski 2012 p. 452-453, Weber 2013 p. 262-264, and case C-417/10 *3M Italia* para. 32.

rules in direct tax directives seems to require the existence of national provisions since these rules in the directives cannot have direct effect.³⁹

In the course of years, the ECJ has explored in several cases the concept of abuse and prevention of tax avoidance as a legitimate justification to apply national tax rules. Initially, however, the Court did not accept the legitimacy of this justification. In the case *Avoir Fiscal*, the lack of authorization from the Treaty prevented the application of national tax avoidance measures restricting the freedom of establishment.⁴⁰ This outright rejection was lessened in later cases although the justification was applied in a restricted manner. In *ICI*, for instance, the ECJ did not disregard completely the possibility to apply national anti-abuse rules even though rejecting their application in the case at hand since they did not, "have the specific purpose of preventing wholly artificial arrangements."⁴¹

In the light of its later case law, it is, nevertheless, clear that the ECJ has accepted prevention of abuse as a justification. In the case *Marks & Spencer*, for example, the Court accepted in principle the legitimacy of Member State legislation the aim of which was prevention of tax avoidance by disallowing the transfer of losses from foreign subsidiaries although the justification was analyzed in combination with other justifications.⁴² The concept of "wholly artificial arrangements" is central to the ECJ case law on anti-abuse measures. The concept which was present in cases such as *ICI, Lankhorst-Hohorst* and *Marks & Spencer*, was further refined in *Cadbury Schweppes*. In that case, the Court established, in line with its earlier case law, that national rules anti-abuse rules may be justified when they target the use of, "wholly artificial arrangements which do not reflect economic reality," and which aim to circumvent national tax law through the abuse of Community law. If the transaction, on the contrary, reflects economic reality alongside tax motives, it cannot be considered to be abusive.⁴³ In *Cadbury Schweppes*, the ECJ created a definition of abuse for the field of European direct taxation. The concept has been repeated in several cases following *Cadbury Schweppes*.⁴⁴

³⁹ See Cerioni 2010 p. 807-809, Sørensen 2011 p. 29-32, and case C-321/05 *Kofoed* paras. 42-44. See also Rousselle - Liebman 2006 p. 562.

⁴⁰ See case C-270/83 Avoir fiscal para. 25.

⁴¹ See case C-264/96 *ICI* para. 26. On the development of the justification, see van Thiel 2008 p. 285-287. See also cases C-175/88 *Biehl* paras. 15-16, C-324/00 *Lankhorst -Hohorst* para. 37, C-436/00 *X and Y* paras. 43, 61, and C-9/02 *De Laysterie du Saillant* para. 50. See also Poulsen 2012 p. 205-206.

⁴² See case C-446/03 Marks & Spencer paras. 49-51.

⁴³ See case C-196/04 *Cadbury Schweppes* paras. 51-56, 65. On the case, see Vanistendael 2006 p. 193-195.

⁴⁴ See, e.g., C-105/07 *Lammers & van Cleeff* para. 26, C-303/07 *Aberdeen* para. 63, C-330/07 *Jobra* para. 35, C-182/08 *Glaxo Wellcome* para. 89, and C-80/12 *Felixstowe* para. 31.

In order to establish whether there is abuse of Union law, the ECJ has developed a two-part test consisting of objective and subjective elements. The test was initially developed outside the field of tax law, but it is currently used also in tax matters. In *Emsland-Stärke*, the Court required that, first, the circumstances show that the objectives of the legislation in question were not attained despite their formal observance and, second, that there was an intent to obtain advantages from EU rules through artificial conditions. ⁴⁵ This test has been introduces to the field of taxation both in indirect taxation (*Halifax*) and in direct taxation (*Cadbury Scweppes*).⁴⁶

In spite of this case law, which authorizes the application of national anti-abuse provisions in certain cases, the ECJ recognizes the legality of tax motives. Due to divergences in tax systems between the Member States and the absence of harmonization, the taxpayers have an opportunity to exploit these differences by establishing themselves in other Member States. Although taxation in that Member State would be more beneficial and this factor would play a role in the decision to establish there, the tax motives do not in itself turn the transaction abusive.⁴⁷ Similar situation was accepted in cases on company law such as *Centros* and *Inspire Art* where companies that availed themselves of more beneficial company law requirements in other Member States were not deemed to be abusive.⁴⁸ This is also evident from several cases within the field of direct taxation which have demonstrated the legality of tax motives.⁴⁹ Nevertheless, the establishment may be disregarded if it is wholly artificial i.e., it fills the requirement of the ECJ case law on tax avoidance.⁵⁰

Furthermore, the national anti-abuse measures must conform to certain additional requirements. In *Thin Cap Group Litigation*, the ECJ established that national courts must be able to ascertain the abusive nature of the transaction based on objective elements and that the taxpayer must be allowed to provide evidence to rebut the assumption of abuse. If abuse is detected, the response must be limited, in line with the principle of proportionality,

⁴⁵ See Cerioni 2010 p. 787-789 and case C-110/99 *Emsland-Stärke* paras. 52-53.

⁴⁶ See C-255/02 *Halifax* paras. 74-75 and C-196/04 *Cadbury Schweppes* para. 64.

⁴⁷ See Vinther - Werlauff 2006 p. 384 where the legitimacy of tax motives is discussed.

⁴⁸ See cases C-212/97 *Centros* para. 27 and C-167/01 *Inspire Art* paras. 137-138. See also de la Feria 2008 p. 428-429 where it is considered that the ECJ narrowed this concept in *Cadbury Schweppes*.

⁴⁹ See cases C-294/97 *Eurowings* para. 44, C-136/00 *Danner* para. 56, C-422/01 *Skandia and Ramstedt* para. 52, and C-196/04 *Cadbury Schweppes* para. 49.

⁵⁰ See Vinther - Werlauff 2006 p. 384-386.

to the advantage gained by the abuse.⁵¹ In *SIAT*, the Court discussed also legal certainty as a part of the proportionality analysis.⁵²

In conclusion, the Member States have certain leeway to apply national anti-abuse measures if they apply only to "wholly artificial arrangements" and conform to other limitations which the ECJ has established in its case law. Nevertheless, the proportionality and suitability of these provisions have been questioned on many occasions. On the other hand, the Court has allowed the Member States to apply in certain cases, where there have been also other justifications in addition to tax abuse and which have concerned loss border transfer of losses or profits, more restrictive provisions which have not targeted exclusively wholly artificial arrangements.⁵³ The PSD provision is, of course, different in this respect since it is a common measure enacted by the EU and not unilaterally by a Member State but, given its similarities with the concepts discussed, the case law on the rule of reason doctrine has a great relevance for its interpretation.

2.3 Preventing Tax Fraud and Tax Evasion in the EU

Concomitant with the OECD BEPS-project and international political actions on tax avoidance, combating tax fraud and tax evasion is high also on the European political agenda. In 2006, the Commission presented a communication where it invited different parties to discuss the problem of tax fraud and a coordinated European response to the issue. In 2012, the Commission introduced a concrete step in this project by presenting the Action Plan on tax fraud and tax evasion. Furthermore, in June 2015, the Commission presented the Action Plan on corporate taxation and, in early 2016, a proposal for a Council Directive on rules against tax avoidance.⁵⁴

The 2012 Action Plan is divided into three sections which are: improvements to current instruments, new Commission initiatives, and future initiatives. Within this framework, the Commission presented several new actions with the aim of aiding the Member States in their work against tax fraud and tax evasion.⁵⁵ Actions 14 and 15 proposed changes to the PSD by planning to introduce new provisions on hybrid structures and discussing the possibility of anti-abuse provisions in EU direct tax directives. Consequently, the Council

⁵¹ On the analysis of the conditions, see Weber 2013a p. 315-316 and case C-524/04 *Thin Cap Group Litigation* paras. 81-83. See also C-28/95 *Leur-Bloem* para. 48.

⁵² See C-318/10 *SIAT* paras. 57-59. See also Hilling 2013 p. 303-304.

⁵³ See Weber 2013a p. 320-322 and Hilling 2013 p. 300-301. See also cases C-446/03 *Marks & Spencer* para. 51 and C-231/05 *Oy AA* para. 60.

⁵⁴ See COM(2006) 254, COM(2012) 722, COM(2015) 302, and COM(2016) 26.

⁵⁵ See Richardson 2015 p. 220-223 for comments on the plan.

adopted the amendments in the Directive 2014/86/EU on hybrid instruments and in the Directive 2015/121/EU on the general anti-abuse provision.

2.4 The Parent-Subsidiary Directive

2.4.1 General Remarks on the Directive

The PSD was initially enacted in 1990 as the Council Directive on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (Directive 90/435/EEC). The Directive has been subsequently amended in 2003 (Directive 2003/123/EEC) and most recently in 2011 (Directive 2011/96/EU). The objective of the Directive is to alleviate the problems caused by double taxation within the Union and facilitate the operations of companies across the Member State borders. This aim is achieved by exempting from withholding taxes the distributions paid by a subsidiary to its parent company, and by eliminating the double taxation in the country of residence of the latter.⁵⁶

The application of the Directive is depended on several conditions. The Directive applies both to distributions between Member State subsidiaries and their Member State parents and to distributions between these subsidiaries and permanent establishments (PE) situated in different Member States. A company qualifies for the benefits of the Directive if it has one of company types listed in the Directive, it is tax resident in one of the Member States, and it is liable to pay, without the possibility of exemption, one of the taxes listed in the Directive. Furthermore, the benefits can be conferred only to companies or PEs that hold at least 10 % of the capital of the subsidiary.⁵⁷

Certain comments with regard to application of these conditions are necessary. First, only the companies listed in the annex of the Directive qualify for benefits if the Member State does not use an open-ended list.⁵⁸ A company can qualify for the benefits of the Directive although the three conditions would be fulfilled in different Member States.⁵⁹ The companies having tax residence outside the EU are not entitled to the benefits of the Directive. In dual residence situations with non-EU countries, the companies may qualify if there either is no tax treaty that limits the taxing competence of the Member State, or if

 $^{^{56}}$ See recitals 3-4 of the preamble to the Directive 2011/96/EU.

⁵⁷ See Art. 1-3 of the Directive 2011/96/EU. Comments on the articles, see Helminen 2013 p. 157-165.

⁵⁸ See case C-247/08 *Gaz de France* paras. 43-44.

⁵⁹ See Tenore 2010a p. 235-236.

the company is a tax resident of an EU country under the tax treaty.⁶⁰ This implies, effectively, that companies with a form not recognized by Member State legislation or which are established outside the Union are not entitled to the PSD benefits.

If the conditions are satisfied, the Member State of the parent company (or that of the PE) has to either exempt the distributions received or grant a credit on the underlying taxes. The Member State of the subsidiary shall not levy a withholding tax on the outgoing distributions.⁶¹ Although the Member States retain more freedom in defining the taxation of distributions outside the scope of the Directive, even this taxation must be in conformance with the Treaty freedoms.⁶² This applies also to the interpretation of the Directive itself since it forms part of secondary legislation.⁶³

2.4.2 Objectives of the Directive

The objectives of the PSD, which are relevant for later interpretation, are discussed further. First, it is stated that the objective of the Directive is to exempt distributions from withholding taxes in the state of the subsidiary and to eliminate double taxation in the state of the parent.⁶⁴ This can be, however, considered to be the way to achieve the more fundamental objective of the Directive which is to improve grouping of companies by alleviating the tax hindrances these companies face and which may be needed to create, "conditions analogous to those of an internal market." This lessens the taxation differences that exist in cross-border groups when compared with corporate groups in one Member State and enhances the neutrality of competition, productivity, and competitive strength.⁶⁵ Furthermore, the ECJ has stated in several judgments that the purpose of the Directive is to remove "any disadvantage" to cross-border cooperation.⁶⁶ Therefore, the main purpose of the PSD is to further the formation of the Internal Market, which correspond to the objectives of the Union as a whole, by supporting the grouping of companies, and this cooperation is supported by the removal of tax obstacles.⁶⁷ It has been

⁶⁰ On the significance of tax treaties on the application, see Terra - Wattel 2012 p. 607.

⁶¹ For the definition of withholding tax, see C-375/98 *Epson* para. 23, C-294/99 *Athinaïki* paras. 28-29, C-58/01 *Océ Van der Grinten* para. 47, and C-284/06 *Burda* para. 52.

⁶² See cases C-374/04 ACT Group Litigation para. 54 and C-379/05 Amurta para. 24.

⁶³ On the application of other EU law on tax directives, see Englisch 2010 p. 201 and Szudoczky 2010 p.

^{191-193.} See also C-138/07 Cobelfret para. 55.

⁶⁴ See recital 3 of the preamble to the Directive 2011/96/EU.

⁶⁵ See recitals 4-6 of the Directive 2011/96/EU. See also C-48/07 *Les Vergers du Vieux Tauves* para. 37.

⁶⁶ See e.g. cases C-294/99 Athinaïki para. 25, C-446/04 FII Group Litigation para. 103, and C-284/06 Burda para. 51.

⁶⁷ For the objectives of the EU, see Art. 26 TFEU and Art. 3(3) TEU.

interpreted from the ECJ judgment Denkavit-VITIC-Voormeer that the Directive is intended to foster lasting cooperation instead of short-term advantages.⁶⁸

Supporting the formation of company groups is based on the political will to further the creation of the Internal Market in a specific sector which entails that the purpose of the PSD is aimed at a defined group of situations. The purpose is, therefore, not to alleviate the tax treatment of individual companies but only the tax disadvantages of those companies that form a part of an international group. These activities must cross the Member State borders in order to have relevance in the Internal Market context. These companies have to be, furthermore, companies of the Member States which is a concept that is more closely defined in the Article 2 of the Directive.

In addition, it is stated in the PSD that the Directive has a purpose of enacting tax rules that are neutral from the point of view of competition and that achieve fiscal neutrality.⁶⁹ Fiscal neutrality is an economic concept that concerns the creation of tax rules that do not have effects on the behavior of the taxpayers which in the case of the PSD means the neutrality of cross-border distributions.⁷⁰ It has been, however, considered that these efficiency arguments could not play a decisive role in the ECJ in the interpretation of the PSD although they are comparable to the aim of alleviating the tax disadvantages in general.⁷¹ As a consequence, fiscal neutrality can be considered to represent the same objective as established above: mitigating tax hindrances for cross-border distributions.

2.4.3 The Former General Anti-Abuse Rule in the Parent-Subsidiary Directive

Before 2015, the PSD did not contain a specific, general anti-abuse provision. The Article 1(2) of the Directive contained, however, a provision that authorized the Member States to apply their domestic or agreement-based anti-abuse and anti-fraud measures. This meant that the Member States had an option, not an obligation, to apply their national anti-abuse rules in cases where the benefits of the Directive were abused, but there were no specific limits placed on these provisions. The provision was not, apparently, subject to ECJ judgments which would have more clearly established its limits.⁷²

⁶⁸ See Weber 1997 p. 26 and joined cases C-283/94, C-291/94 and C-292/94 Denkavit-VITIC-Voormeer para. ⁶⁹ See recitals 4, 6 of the preamble to the Directive 2011/96/EU.
⁷⁰ See Brokelind 2000 p. 28-29.

⁷¹ Ibid. p. 30-33.

⁷² See Tavares - Bogenschneider 2015 p. 491 where it is, however, stated that minimum economic substance was required under the rulings on the other direct tax directives.

Nevertheless, directive-based anti-abuse provisions do not allow, without national implementation, the Member States to deny the rights granted to the taxpayers. This is based on the lack of direct effect of such directive provisions that restrict private rights and was seen in the case *Kofoed* where the anti-abuse provision of the Merger Directive did not allow the restriction of the rights of the taxpayers when it was not included in national legislation although the implementation was defined broadly.⁷³ The PSD authorization was, therefore, essentially depended on the existence of national rules. What is more, the ECJ found in its *Denkavit-VITIC-Voormeer* case that the general anti-abuse authorization cannot be used to combat abuse which is countered by other provisions of the Directive.⁷⁴

Given the lack of guidance on the scope of the provisions authorized by the PSD, opinions were divided on the true extent of discretion that the Member States had in enacting them. Some concluded that the old authorization could have been used to counter only wholly artificial arrangements.⁷⁵ It was even stated that only such anti-abuse provisions that were supported by other provisions of the PSD could have been justified.⁷⁶ In some older contributions, it was deemed that abuse could exist only in situations with a third-country connection.⁷⁷ Furthermore, in *Leur-Bloem*, the ECJ declared that general, automatic anti-abuse rules constituted a disproportional way to apply the anti-abuse provisions in the directives.⁷⁸ Due to rule of reason requirements, the absence of specific provisions does not mean that the Member States would not be restricted to combat abusive situations.

In conclusion, the scope of the anti-abuse authorization in the PSD was unclear with regard to question how far-reaching measures the Member States could actually enact. The new provision takes a step in another direction since it establishes more definite, although vague, criteria to determine which arrangements can be seen to constitute abuse of the PSD.

2.4.4 Abuse of the Parent-Subsidiary Directive

Abuse has been examined in the ECJ case law both with regard to circumvention of rules and abusive attainment of advantages attached to rules.⁷⁹ The PSD can, such as other legal instruments, be misused in order to obtain its benefits improperly. A specific concern is the

⁷³ See Zalasinski 2007a p. 573-574 and case C-321/05 *Kofoed* paras. 42-46.

⁷⁴ See joined cases C-283/94, C-291/94 and C-292/94 *Denkavit-VITIC-Voormeer* para. 31 and Weber 1997 p. 25.

⁷⁵ See Tenore 2010a p. 233-235.

⁷⁶ See Brokelind 2003 p. 162. See also de Broe 2008 p. 1001 where the discretion was seen to be limited.

⁷⁷ See Knobbe-Keuk 1992 p. 489 and Rädler - Lausterer - Blumenberg 1997 p. 98.

⁷⁸ See Zalasinski 2007 p. 315-319 for proportionality of anti-abuse provisions and case C-28/95 *Leur-Bloem* para. 48.

⁷⁹ On this classification, see Vogenauer 2011 p. 525-530.

problem of "directive-shopping" which is mentioned also by the Commission as one of the reasons to enact the new anti-abuse provision.⁸⁰ In this form of abuse, those that are not entitled to the benefits of the Directive when receiving distributions directly, such as third-country residents, may attempt to access these benefits through abusive constructions, but it is possible that a more lenient implementation of the PSD in some Member States could be source of such actions also in situations involving only Member States.⁸¹

Directive-shopping is made possible by disparities between Member State tax systems since certain Member States may subject distributions to beneficial treatment such as no or low withholding tax. Tax treaty benefits combined with the PSD may allow the repatriation of distributed profits with low or inexistent tax burden.⁸² By interposing a company in a Member State, non-residents can gain access to these benefits although this would not be directly possible due to nationality requirements of the PSD. Interestingly, this problem was envisaged already in the early stages of application of the PSD.⁸³ Companies established according to Member State legislation are protected by the freedom of establishment even though their owners would reside outside the Union and, consequently, the Member State response is limited by the rule of reason doctrine.⁸⁴

For instance, a holding company can be established in an EU Member State with a beneficial tax treaty network. Due to the PSD benefits, the subsidiaries in other Member States are able to channel their profits to the holding company free of withholding taxes. The holding company can, on its turn, distribute its profits to a non-EU parent company with a low tax burden by utilizing tax treaties.⁸⁵ Another example is the circumvention of participation exemption rules of a Member State through a Member State conduit company.⁸⁶ In addition, there are naturally also other ways to abuse the PSD, but some of these situations are dealt with specific provisions of the Directive.

2.5 General Features of the New Anti-Abuse Provision

The Council Directive 2015/121/EU introduced a new general anti-abuse provision to the PSD based on the proposal in the Commission 2012 Action Plan to revise the directive-

⁸⁰ See COM(2013) 814 p. 4-5.

⁸¹ For definition of directive-shopping, see de Broe 2008 p. 22-24.

⁸² Generally on the problem, see Poulsen 2013 p. 230-231 and Sørensen 2015 p. 106.

⁸³ See Raby 1992 p. 221.

⁸⁴ See Evers - de Graaf 2009 p. 279-281 and Poulsen 2013 p. 233-236.

⁸⁵ This structure in presented in Tavares - Bogenschneider 2015 p. 486-488. Similarly Panayi 2006 p. 154-156.

⁸⁶ See de Broe 2008 p. 23-24. See also Weber 1996 p. 66 and Weber 2016 p. 116.

based anti-abuse provisions.⁸⁷ The Member States had to implement the provision before the end of the year 2015. In its recommendation on aggressive tax planning, the Commission had already recommended that the Member States should adopt a general anti-abuse rule corresponding to the one presented in the recommendation.⁸⁸ The proposed PSD anti-abuse provision was developed in accordance with this recommendation although the enacted provision differs in several aspects from the proposal of the Commission.

The state of Union legislation contained several alleged challenges that prompted the Commission to propose the new provision. First, the Member State response to abusive situations was found to be limited by the ECJ case law, and the variance in Member State provisions was seen to create opportunities for directive-shopping and other forms of abuse. Moreover, the prevention of abusive practices was considered to be jeopardized by the fact that some Member States did not have any specific anti-abuse provisions in their legislation. The national anti-abuse provisions were deemed to lack the effectiveness of an EU-level response and, in the worst case, they could be seen to contribute to misuse of the Directive.⁸⁹

In order to address these concerns, the Commission proposed an obligatory anti-abuse provision that would prevent the misuse of the PSD and achieve uniformity on the level of Member State legislations. The amending provision states that: "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."90 Transactions are not genuine, "to the extent that they are not put into place for valid commercial reasons which reflect economic reality." Furthermore, the Article 1(4) of the provision authorizes the Member States to apply their national or agreement-based provisions.

At the first sight, several conditions can be derived from the provision. First, there must be an arrangement or a series of arrangements. Second, the main purpose or one of the main purposes of this arrangement must be the obtainment of a tax advantage. Third, this advantage must be contrary to the objectives of the Directive. And finally, the arrangement

⁸⁷ See COM(2012) 722 p. 9 action 15.

⁸⁸ See C(2012) 8806 p. 4-5.

 ⁸⁹ See SWD(2013) 474 p. 12-13. See also COM(2013) 814 and recital 4 of the Directive 2015/121/EU.
 ⁹⁰ See Article 1(2) of the Directive 2015/121/EU. The Article contains also further definitions.

must be non-genuine which is the case when there are no valid commercial reasons that reflect economic reality. Further research is based on this classification.⁹¹ Since both the provision and the amending Directive lack any further notions on its application, it may be concluded that all the conditions must be fulfilled at the same time. This may be assumed from the way in which the conditions are presented in connection with each other.⁹² As a consequence, if the transaction in question leaves even one of the conditions unfulfilled, it falls outside the scope of the provision.

Equally relevant is the way of harmonization. The provision intends to achieve minimum harmonization i.e., it forms the baseline which the Member States must implement, but they are, nevertheless, free to enact stricter provisions as long as these provisions comply with the primary law.⁹³ Therefore, all the Member States have to take and apply the PSD provision as a part of their national tax legislation. This is one of the salient features of the provision since it implies that the Member States are obliged to deny the benefits of the Directive although this was earlier only an opportunity whose exercise had to comply with the ECJ case law.⁹⁴ There have been, however, opinions that the anti-abuse rule leads in fact to total harmonization which prevents both stricter and more lenient provisions.⁹⁵

Before moving on to the analysis of the conditions, few remarks on directives and their interpretation deserve to be observed. The EU Directives do not form part of the national legal order and, consequently, what binds and obliges the Member States is the purpose of the directive. A directive needs to be implemented in the form of national legislation although the Member States can decide on the details of implementation.⁹⁶ Since anti-abuse clauses restrict the rights of the taxpayer, the application of directive-based anti-abuse measures is precluded in absence of national legislation although even a general principle in national law may be sufficient.⁹⁷ The national legislation must be interpreted in the light of the purpose of the directive and, more generally, in the light of the purposes of the EU Treaties.⁹⁸

⁹¹ This classification of conditions is made also by Debelva - Luts 2015 p. 224.

⁹² See Tavares - Bogenschneider 2015 p. 486, Debelva - Luts 2015 p. 224 and Brokelind 2015 p. 819.

 ⁹³ See recital 5 of the preamble to the Directive 2015/12/EU. On minimum harmonization, see Dougan 2000 p. 854-855.
 ⁹⁴ When the Directive 2015/12/EU. On minimum harmonization, see Dougan 2000 p. 854-855.

⁶⁴ When the Member States have not been forced to adopt the anti-abuse concept, see Lang 2011 p. 455-457. ⁹⁵ See van den Hurk 2014 p. 494.

⁹⁶ Generally on the directives and their effect, see Helminen 2013 p. 22-23 and Art. 288 TFEU.

⁹⁷ See case C-321/05 *Kofoed* paras. 45-46 and Zalasinski 2007a p. 573-574. Generally on the direct effect, see e.g. C-14/86 *Pretore di Salò* paras. 19-20 and C-80/86 *Kolpinghuis Nijmegen* paras. 9-10.

⁹⁸ On consistent interpretation, see Tenore 2009 p. 27-29.

In this case, there is, on the one hand, the purpose of the PSD which is alleviation of obstacles to cross-border business in the EU and, on the other hand, the purpose of the new provision with the aim of preventing abusive practices by creating an exemption to the application of the Directive and which may lead to restriction of cross-border movement since the PSD applies only to these situations.⁹⁹ These aims must be taken into account when the new provision is interpreted. Anti-abuse rules in direct tax directives have been seen, additionally, to reflect the general principle of the prohibition of abuse although the direct application of the principle in this case has been discarded.¹⁰⁰ The national legislation should, however, be evaluated in the light of the provision in the Directive.¹⁰¹

3 Interpretation of the Anti-Abuse Provision

3.1 An Arrangement or a Series of Arrangements

3.1.1 Which Arrangement are Caught by the Provision

The first condition to be analyzed is the existence of an arrangement or a series of arrangements. It appears that this condition can limit the application of the provision in two situations. First, if there are some factors that restrict the scope of the arrangement to only certain specific situations and, second, if a certain minimum limit to the existence of an arrangement could be defined under which there would be no arrangement and, therefore, no abuse.

The provision itself does not define the concept of arrangement or how wide its application should be. The Commission proposal contained, however, a substantially different provision than the one enacted and which included a list of different situations that could constitute an "artificial arrangement" and be subject to the anti-abuse provision. The situations listed where: transaction, scheme, action, operation, agreement, understanding, promise or undertaking.¹⁰² The definition is comparable to the one used in the Commission recommendation on aggressive tax planning.¹⁰³

⁹⁹ See recitals 3-4 of the preamble to the Directive 2011/96/EU and Art. 1 on the scope of application as well as recital 2 of the preamble to the Directive 2015/121/EU.

¹⁰⁰ See Piantavigna 2011 p. 140 and Jimenez 2012 p. 288. See also Sørensen 2011 p. 29-32.

¹⁰¹ See Freedman 2011 p. 369-370.

¹⁰² See COM(2013) 814 p. 9 where the listed situations formed an artificial arrangements when they did not reflect economic reality.

¹⁰³ See C(2012) 8806 p. 4. The list contained also "grant" and "event" and concerned "any" of the situations.

Despite the fact that the list may give some ideas on the scope of the definition, the terms in itself are generally formulated, and no delimitation of the condition can be deducted from them. Nevertheless, it appears that at least the original definition was meant to be wide in scope since the situations cover virtually all relevant transactions conceivable.¹⁰⁴ The listing was, however, not included in the enacted provision which means that no further conclusions can be made on the basis of its wording. On the other hand, this may have been only to technical reasons since such a listing may not have any greater relevance in the application of the provision.

As the provision itself does not limit the concept of arrangement, it should be examined whether the concept has found any separate significance in other direct tax directives or in the ECJ case law. Regarding the directives, the benefits may be withdrawn if one of principal purposes of a "transaction" (Interest-royalty Directive) or an "operation" (Merger Directive) is tax evasion, avoidance or abuse, while in the case of the latter, the operation finds its content in the transactions regulated by the Directive (mergers, divisions etc.).¹⁰⁵ When it has interpreted the provision of the Merger Directive, the ECJ has not attached any specific significance to the concept of operation. The Court has connected the abuse with "transactions not carried out in the context of normal commercial operations."¹⁰⁶ Normal commercial restructurings do not fall within the scope of the anti-abuse provision if they do not reflect artificiality.¹⁰⁷ What is, therefore, significant is not the existence of a transaction or an operation but the lack of its commercial validity.

Similar conclusions may be drawn from the ECJ case law on anti-abuse measures in nonharmonized direct taxation. In *Cadbury Schweppes*, the national tax measures were justified when they concerned wholly artificial arrangements.¹⁰⁸ The case, however, remains silent on the concept of an arrangement itself. Equally in the later cases, where the Court has referred to wholly artificial arrangements, the notion has concentrated on the factors which can indicate the real economic motives and, consequently, the nonartificiality of the arrangement.¹⁰⁹ In conclusion, the arrangements are not considered

¹⁰⁴ See also Debelva - Luts 2015 p. 224, where it is concluded that the concept should be interpreted broadly.

¹⁰⁵ See Art. 6 of the Directive 49/2003/EC and Art. 15 of the Directive 2009/133/EC.

¹⁰⁶ See cases C-321/05 *Kofoed* para. 38 and C-126/10 *Foggia* para. 50.

¹⁰⁷ For interpretation of the cases, see Jimenez 2012 p. 280-284.

¹⁰⁸ See case C-196/04 *Cadbury Schweppes* paras. 50-55 and 67-69.

¹⁰⁹ See, for example, cases C-524/04 *Thin Cap Group Litigation* paras. 72-74, C-105/07 *Lammers & Van Cleeff* paras. 26-28, C-303/07 *Aberdeen* paras. 64-65, and C-282/12 *Itelcar* para. 34.

separately but only in connection with the artificiality evaluation in the context of "wholly artificial arrangements."

Some interesting remarks can be, however, derived from the recitals of the amending Directive where it is stated that the provision can apply to non-genuine elements of the arrangement when, for example, the entity in question would be genuine but the elements of a distribution would not.¹¹⁰ Since the PSD applies only to distributions between companies, it is reasonable to conclude that a company is involved in all arrangements, but the arrangements can, as stated in the preamble, include also other elements. If the provision would be limited only to certain arrangements, such as specific transactions, this restriction would likely be visible in the wording. Since abuse does not limit itself to specific structures, it is in accordance with the purpose of the provision that the term "arrangement" covers all transactions that fulfill the other conditions of the provision.

In conclusion, since the concept of arrangement does not seem to have been limited in the provision itself or, on general level, in the ECJ case law, it should include all arrangements, whatever their closer composition, which contain abusive elements. An arrangement can be considered to be rather an essential prerequisite to the application of the provision since misuse of the Directive benefits does not happen all by itself, but this concept alone does not affect the threshold of finding abuse. It should be relevant only if a lower limit to the existence of an arrangement could be defined. This is, however, hardly necessary since in these cases there would not most probably be abuse either. Series of arrangement or a part of it can be found individually abusive, it is only logical that also several arrangements in a row can be accorded the same treatment.

3.1.2 Part of an Arrangement

In addition to arrangements and series of arrangements, which are in their entirety abusive, the provision can also apply to parts or steps of these arrangements.¹¹¹ At the first sight, if the arrangement is given the interpretation discussed above, this should not imply much since a part or a step of an arrangement can, arguably, be defined as an arrangement itself. Since arrangement cannot be given a more precise definition, it encompasses also structures where only a certain element is individually abusive. It has been seen that this

¹¹⁰ See recital 8 to the Directive 2015/121/EU. See also Poulsen 2013 p. 239 for a similar situation.

¹¹¹ See recital 8 of preamble to the Directive 2015/121/EU and Art. 1(2) where it is stated that : "An arrangement may comprise more than one step or part."

means evaluation of abusive intent for the part of the arrangement separately which seems to be only in accordance with the provision since otherwise these parts could hardly be found abusive if the more widely-defined arrangement as a whole would not be.¹¹²

What may be more relevant is that, according to the recital, this approach permits the application of the provision only to non-genuine parts of the arrangement leaving the rest of the arrangement intact. This refers to the principle of proportionality which limits the application of all legal rules beyond what can be judged to be necessary.¹¹³ First, the anti-abuse rules should apply only to arrangements that can be considered to be artificial and not to all transactions of certain types.¹¹⁴ Furthermore, if an arrangement is found to be artificial, the benefits can be withdrawn only to the extent they remove the advantage gained by this conduct.¹¹⁵ Therefore, if a part or a step of the arrangement is found to non-genuine, it is in line with the principle of proportionality that only those parts are subjected to the anti-abuse provision. Stating this in the provision does not, however, seem to bring anything new since these requirements have already been present in the ECJ case law on anti-abuse measures.¹¹⁶

It is, however, probable that the application of the provision would also affect the rest of the arrangement. If, for example, a company was genuinely established but a certain distribution would be non-genuine, the non-application of the benefits on the distribution would leave also the company without these benefits. If the arrangement consists of steps and one of these steps is caught by the provision, it could, even without explicit application of the provision, affect the genuine parts of the arrangement. It can be, moreover questioned which taxpayers are caught by the provision, but since this issue is more related to the chapter on the effects of the provision, it is examined at a later stage.

3.2 Main Purpose of Obtaining a Tax Advantage

3.2.1 General Remarks

The second criterion to be examined is the requirement that the arrangement has been enacted, "for the main purpose or one of the main purposes of obtaining a tax advantage." This condition refers to the subjective element of ECJ anti-abuse case law first established

¹¹² See Weber 2016 p. 110.

¹¹³ On the principle of proportionality, see Zalasinski 2007 p. 310-312.

¹¹⁴ See cases C-28/95 *Leur-Bloem* para. 44 and C-196/04 *Cadbury Schweppes* para. 55.

¹¹⁵ See case C-524/04 *Thin Cap Group Litigation* para. 83.

¹¹⁶ See Weber 2013a p. 313-316.

in the agricultural case *Emsland Stärke* where it was required that there is, "a subjective element consisting in the intention to obtain an advantage from the Community rules by creating artificially conditions laid down for obtaining it."¹¹⁷ The test has found application also in others areas of EU law including taxation where it has been adopted both in direct taxation and in indirect taxation.¹¹⁸ The condition has been, however, subject to diverging interpretations and some controversy which requires that it is examined further.¹¹⁹

The case law contains different interpretations of the threshold when tax purposes become abusive. For example in *Halifax*, it was required that the "essential aim" of the transaction was the obtainment of a tax advantage.¹²⁰ This is where the new provision goes further, while stating that it is possible to apply the provision when one of the main purposes is the obtainment of a tax advantage. The formulation may appear very broad since taxpayers have usually several purposes when conducting their transactions, and it is equally normal to take tax considerations into account.¹²¹ If the provision is applied according to its letter, it may make possible the denial of the PSD benefits in cases where tax considerations feature as a relevant, but not as an exclusive, reason alongside other valid commercial reasons.¹²²

The wording is problematic also with regard to the generally accepted principle in direct tax cases according to which the taxpayers have a right to choose the Member State of establishment based on tax-criteria.¹²³ It is completely acceptable to take tax factors into account as long as the establishment is otherwise non-artificial i.e., it is not wholly artificial.¹²⁴ The new provision seems to, however, adopt an approach where non-exclusive tax reasons, even in the existence of other, more important reasons, can fulfill the test and fall within the scope of the provision which would imply a lower standard to find abuse. This is also in contrast with the initial proposal where "essential purpose" was required.¹²⁵ Furthermore, since the purpose of the PSD itself is to offer tax benefits by lessening the

¹¹⁷ See de la Feria 2008 p. 409-411 and case C-110/99 *Emsland Stärke* paras. 52-54.

¹¹⁸ See cases C-255/02 *Halifax* para. 75 and C-196/04 *Cadbury Schweppes* para. 64.

¹¹⁹ See, *inter alia*, Kiekebeld 2009 p. 144, Piantavigna 2011 p. 144-145, and Weber 2013 p. 255, 257.

¹²⁰ See case C-255/02 *Halifax* para. 75.

¹²¹ Similarly Lyal 2011 p. 430-433 who criticizes the reliance on subjective tax saving motives.

¹²² See also Picq 2009 p. 474 where a similar test in French law is criticized.

¹²³ See Vinther - Werflauff 2006 p. 384 and Weber 2013a p. 322-324.

¹²⁴ See cases C-294/97 *Eurowings* para. 44, C-136/00 *Danner* para. 56, C-422/01 *Skandia and Ramstedt* para. 52, and C-196/04 *Cadbury Schweppes* paras. 49-50 and 65-66.

¹²⁵ See COM(2013) 814 p. 9.

double taxation of distributions, the recourse to the Directive implies a will to attain a tax advantage in the first place.¹²⁶

Given the apparently broad formulation of the provision, it should be examined how the it could be interpreted in the light of the ECJ case law. It is examined, first, how the subjective test has been interpreted previously and, second, whether the PSD provision can be situated under one of the expressions that the Court has already used.

3.2.2 Main Purpose or One of the Main Purposes

First, a look is given to direct tax case law on the fundamental freedoms since the PSD provision, while requiring subjective and objective elements, resembles the formulation of the anti-abuse test which the ECJ has used in this case law. The subjective element was explicitly mentioned in *Cadbury Schweppes* where it was formulated as an, "intention to obtain tax advantage." This is connected with wholly artificial arrangements which are, "with a view to escaping tax normally due."¹²⁷ Tax motives are not, however, relevant if the transaction, "reflects economic reality."¹²⁸ This implies that if the transaction is nonartificial, the intention of the taxpayer to have a tax advantage does not play a further role in the evaluation of abuse but, on the contrary, if there is a wholly artificial arrangement, the reduction of tax burden must be considered as a part of this evaluation.¹²⁹ This means that in order to find abuse, there must be avoidance of tax burden as well as artificiality.¹³⁰ A difference between the PSD provision and this formulation is, essentially, that abuse in the case of the PSD does not attempt to circumvent national law but to gain a certain advantage granted by a tax directive.

Cadbury Schweppes has been interpreted to mean that there is no abuse although tax would be the principal reason for the transaction.¹³¹ The case included the concept of wholly artificial arrangements which have the sole intend of evading taxation and "wholly" has been interpreted that no other reasons in addition to tax ones can exist.¹³² The more recent case law on wholly artificial arrangements contains an amount of lexical ambiguity in this matter. In Thin Cap Group Litigation and in Lammers & Van Cleeff, reference was made

¹²⁶ See Debelva - Luts 2015 p. 225.

¹²⁷ See case C-196/04 *Cadbury Schweppes* paras. 55, 64.

¹²⁸ Ibid para. 65.

¹²⁹ See Piantavigna 2011 p. 144-145 where a contrast is made between VAT cases and direct tax cases. See also Vanistendael 2006 p. 195 and Cerioni 2010 p. 795.

¹³⁰ See Weber 2013 p. 254-255.
¹³¹ See Vanistendael 2011 p. 413.

¹³² See C-196/04 *Cadbury Schweppes* paras. 61, 63. See also Piantavigna 2011 p. 145.

to, "purely artificial arrangements, the essential purpose of which is to circumvent the tax legislation of that Member State."¹³³ Furthermore, the purpose to obtain a tax advantage had to be the "only purpose" in *Jobra* and *Glaxo Wellcome* and "sole purpose" in *Aberdeen, SIAT*, and *Itelcar*.¹³⁴ In yet other cases, such as *K*, *Felixstowe*, and *SCA Group Holding*, there was no specific reference to the importance of tax purposes but references to *Cadbury Schweppes*.¹³⁵ Sole purpose was also required in *Denkavit-VITIC-Voormeer* on the former PSD anti-abuse provision although the case predates *Cadbury Schweppes*.¹³⁶

There have been, nonetheless, opinions that this "sole purpose test", as inferred from *Cadbury Schweppes* and from several subsequent cases, could be interpreted to be, in essence, close to the "essential purpose test" present in other, especially VAT, case law noting the explicit reference to *Halifax* in *Cadbury Schweppes*.¹³⁷ One argument has been that if genuine economic activity is required in order to establish the non-artificiality of the arrangement, this implies that there are also other motives in addition to tax motives.¹³⁸ Applying the lower essential aim-threshold would mean that transactions which are not solely tax motivated but represent clearly artificiality could be caught by anti-abuse rules.¹³⁹ This interpretation seems to be, most of all, practical since requiring that the sole or unique purpose of the transaction is avoidance of taxation could imply that transactions where the tax motives would play a crucial, but not an exclusive, role could not be prevented by anti-abuse measures.¹⁴⁰

Second, the case law on the Merger Directive is examined since the anti-abuse provision in the Article 15 of the Directive 2009/133/EC contains language similar to the PSD in requiring that an operation, "has as its principal objective or as one of its principal objectives tax evasion or tax avoidance." There have been comments that the PSD provision should be interpreted, by virtue of this case law, to require that "sole" or at

¹³³ See cases C-524/04 *Thin Cap Group Litigation* para. 81, and C-150/07 *Lammers & Van Cleeff* para. 30.

¹³⁴ See cases C-303/07 *Aberdeen* para. 65, C-330/07 *Jobra* para. 35, C-182/08 *Glaxo Wellcome* para. 89, C-318/10 *SIAT* para. 50, and C-282/12 *Itelcar* paras. 34, 37.

¹³⁵ See cases C-322/11 K paras. 61-62, C-80/12 *Felixstowe* para. 33, and joined cases C-39/13, C-40/13, C-41/13 SCA Group Holding/ X AG/ MSA International Holdings para. 42.

¹³⁶ See joined cases C-283/94, C-291/94 and C-292/94 Denkavit-VITIC-Voormeer para. 31.

¹³⁷ See C-196/04 *Cadbury Schweppes* para. 64.

¹³⁸ See Vanistendael 2006 p. 195 and Cerioni 2010 p. 805. See also Jimenez 2012 p. 278.

¹³⁹ See Weber 2013 p. 256-257 where application of the VAT standard in direct tax cases is supported. See also Pistone 2007 p. 535.

¹⁴⁰ See Piantavigna 2009 p. 173, Freedman 2011 p. 375, and Vogenauer 2011 p. 540 where a similar position is presented.

least "predominant" purpose of the arrangement is the obtainment of a tax advantage.¹⁴¹ There appears to be a slight difference in the wording since the PSD provision requires that the purpose is the obtainment of a tax advantage that defeats the purpose of the Directive while the Merger Directive requires that the purpose is tax evasion or avoidance although the latter situations include, inherently, the obtainment of a tax advantage.¹⁴² In cases *Leur-Bloem, Kofoed, Zwijnenburg* and *Foggia*, it was first established, in accordance with the Directive, that the provision applies to an operation which has, "tax evasion or avoidance as its principal objective or as one of its principal objectives," and this can be presumed if there are no valid commercial reasons.¹⁴³ In *Kofoed* and *Foggia*, however, it was stated that EU legislation cannot be applied to, "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," with references to both *Halifax* and *Cadbury Schweppes*.¹⁴⁴ Equally in *Foggia*, the Court states that valid commercial reasons, "involves more than the attainment of a purely fiscal advantage," and when this is the only aim of transaction, valid commercial reasons are not present.¹⁴⁵

At the first sight, it appears that *Kofoed* and *Foggia* attached the label of abuse under the provision of the Merger Directive to transactions whose only aim is the obtainment of an advantage. This interpretation has been defended despite the wording of the provision.¹⁴⁶ *Foggia*, nevertheless, seems to refer also to another threshold while establishing that an operation can entail the existence of valid commercial reasons even if there were tax considerations if, "those considerations are not predominant."¹⁴⁷ What is more, it was established that if the only aim of the transaction is the obtainment of a tax advantage, "such a finding may constitute a presumption that the operation has tax evasion or avoidance as one of its principal objectives."¹⁴⁸ This implies that a transaction with no other reasons in addition to tax reasons can be presumed to have a principally abusive objective, but it cannot be derived from *Foggia* that only such transactions which leaves

¹⁴¹ See Debelva - Luts 2015 p. 225, who justify the interpretation with reference to the Merger Directive.

¹⁴² On the different concepts of avoidance, see Zalasinski 2008 p. 158-160.

¹⁴³ See cases C-28/95 *Leur-Bloem* paras. 38-39, C-321/05 *Kofoed* para. 37, C-352/08 *Zwijnenburg* para. 43, and C-126/10 *Foggia* para. 33.

¹⁴⁴ See cases C-321/05 *Kofoed* para. 38 and C-126/10 *Foggia* para. 50.

¹⁴⁵ See case C-126/10 *Foggia* para. 34. See also C-28/95 *Leur-Bloem* para. 47.

¹⁴⁶ See Petrosovich 2010 p. 562 where the wording is seen to potentially conflict with the purpose of the Directive.

¹⁴⁷ See C-126/10 *Foggia* para. 35.

¹⁴⁸ Ibid. para. 36.

room also to other purposes. The interpretation of the Merger Directive is interesting with regard to the PSD provision since it means that under a similarly-worded provision the tax saving purpose does not have to be either sole purpose or one of the main purposes for the transaction, but that the predominance of these purposes suffices.

Despite comments that abuse differs in different fields of tax law, a brief look is given to the certain judgments of VAT case law where the essential aim threshold has been given further attention.¹⁴⁹ In *Halifax*, it was established 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," which is not the case if, "the economic activity carried out may have some explanation other than the mere attainment of tax advantages."¹⁵⁰ In Part Service, on the other hand, it was established that there is abuse of the VAT directives if the "principal aim" of the transaction is the obtainment of a tax advantage.¹⁵¹ The mention on the sole purpose test in Halifax was, according to the ECJ, only meant indicate that the threshold for finding abuse, when the tax avoidance was the only purpose, had already been surpassed, and if the principal purpose was the obtainment of a tax advantage, the other non-tax purposes were not relevant.¹⁵² This was confirmed also in subsequent cases such as Weald Leasing, RBS Deutschland and Tanoarch, although in the latter two there was a somewhat unclear mention that, "the essential aim of the transactions concerned is solely to obtain that tax advantage."153 However, in the French, Spanish, Swedish and Finnish versions of the judgment, this has been translated as essential aim. Somewhat contradictorily, the same cases referred also to sole purpose test separately which implies some confusion with regard to the terminology.¹⁵⁴

After discussing the case law, it must be considered if one of these formulations could apply to the PSD provision. First, it would appear that the concept of wholly artificial arrangements with the sole purpose of tax avoidance is not expressed in the provision although it requires, similarly to *Cadbury Schweppes*, that the arrangement must be "nongenuine". Nevertheless, it has been considered that the main purpose test can be actually

¹⁴⁹ See Freedman 2011 p. 370 and Vanistendael 2011 p. 422-425.

¹⁵⁰ See C-255/02 *Halifax* para. 75.

¹⁵¹ See C-425/06 *Part Service* para. 45.

¹⁵² Ibid. paras. 44 and 62. See also Kiekebeld 2009 p. 144.

¹⁵³ See cases C-103/09 *Weald Leasing* para. 30, C-277/09 *RBS Deutschland* para. 49, and C-504/10 *Tanoarch* para. 52.

¹⁵⁴ See cases C-103/09 Weald Leasing para. 26, C-277/09 RBS Deutschland para.51, and C-504/10 Tanoarch para. 51.

reconciliated with wholly artificial arrangements if business reasons in one part of the arrangement do not displace the artificiality in another part.¹⁵⁵ The question is whether the anti-abuse measures in the cases on wholly artificial arrangements differ from those in the secondary legislation.¹⁵⁶ Essentially, does the creation of an explicitly formulated antiabuse provision lead to a new concept of abuse that should be regarded separately from the case law on the fundamental freedoms which concerns the justification of national measures? Wholly artificial arrangements have been seen to be justified in the case of the freedoms since the Member State measures could compromise the freedom of movement.¹⁵⁷ On the other hand, it has been considered that anti-abuse rules based on the former anti-abuse authorization in the PSD should have fulfilled the wholly artificial arrangement test, but in this case the concept of abuse was not formulated more closely in the provision itself which brought the situation closer to *Cadbury Schweppes* case law.¹⁵⁸ It has been derived from the case of the Merger Directive, which contains a specific although non-mandatory anti-abuse provision, that the national measures should be interpreted in the light of the ECJ case law on this specific anti-abuse clause when such a clause exists.¹⁵⁹

Accordingly, the conceptually closer situation of the Merger Directive could support another conclusion. Given the quite close formulation of this provision and the fact that both directives concern secondary legislation and have a similar purpose i.e., creation conditions similar to Internal Market by removing tax obstacles, the case law could support the conclusion that tax purposes must be predominant due to the fact that this was the content given to principal purposes in *Foggia*.¹⁶⁰ What remains, nevertheless, uncertain is the significance of the reference in *Kofoed* and *Foggia* to abusive practices whose sole purpose is to obtain advantages, as there is a direct reference to *Cadbury Schweppes*.¹⁶¹ In some contributions, even the Merger Directive has been seen to require wholly artificial arrangements.¹⁶² In Kofoed, the ECJ referred to the principle of abuse law which the provision of the Merger Directive reflects, but the Court established in the same judgment

¹⁵⁵ See Weber 2016 p. 110.

¹⁵⁶ See Weber 2011 p. 400-401 where abuse on EU and national level are considered to be distinct in formulation, but at the same they are seen to represent a common concept.

¹⁵⁷ See Vanistendael 2011 p. 423 and Lyal 2011 p. 433-432. See also de Broe 2008 p. 827.
¹⁵⁸ See Tenore 2010a p. 234. See also Terra - Wattel 2012 p. 648 where the provision was deemed to lack independent relevance in comparison with the ECJ doctrine.

¹⁵⁹ See Freedman 2011 p. 369-370, Vanistendael 2011 p. 421-422, and Lang 2011 p. 457.

¹⁶⁰ See recitals 2-4 of the Directive 2009/133/EC and recitals 4-8 of the Directive 2011/96/EU.

¹⁶¹ C-321/05 Kofoed para. 38 and C-126/10 Foggia para. 50.

¹⁶² See Kofler - Tumpel 2009 p. 480.

that the principle is not applicable within the scope of direct tax directives.¹⁶³ What is more, the two anti-abuse provisions differ in wording since the PSD provision contains both objective and subjective tests, similarly to *Cadbury Schweppes*, while the Merger Directive requires only the objective to avoid taxation although, in some occasions, the tests have been considered to be similar.¹⁶⁴

On the other hand, although the VAT cases could support the principal purpose test, these cases have had similar references to sole purpose test in *Halifax* and *Cadbury Schweppes*, and it is not evident whether this case law could be given relevance within the field of direct taxation as there have been differing opinions on this issue.¹⁶⁵ What, however, connects the VAT and the direct tax directives is that they both include, albeit different, secondary legislation. Nevertheless, even these two situations have been regarded to be separate in respect of the anti-abuse concepts.¹⁶⁶ The case law on the Merger Directive implies, however, that a provision similar to the PSD provision does not necessarily have to be interpreted based on the sole purpose standard, and the similarity of the context could support adopting this interpretation also for the PSD provision.

Nevertheless, it is open to debate how the problematic "one of main purposes" should be interpreted. Such a low threshold has not been used in the direct tax case law on wholly artificial arrangements if one ignores a similarly-worded reference in *Cadbury Schweppes* to Member State legislation, and the test has, as discussed above, situated on essential or sole purpose level.¹⁶⁷ In addition, the interpretation of the Merger Directive could support a restrictive interpretation. In *Foggia*, the tax reasons were not decisive as long as they were not predominant among the several objectives of a transaction which is a higher requirement than one of the principal purposes expressed in the provision.¹⁶⁸

The implementing legislation must be, in addition, interpreted in the light of the directive.¹⁶⁹ Furthermore, the anti-abuse provision must not defeat the objectives of the

¹⁶³ C-321/05 *Kofoed* para. 42 and opinion of the Advocate General 8 Feb 2007 para. 67. See also Sørensen 2011 p. 30-31.

¹⁶⁴ See Jimenez 2012 p. 281 where *Cadbury Schweppes* is compared to *Kofoed*.

 ¹⁶⁵ See, e.g., against Vanistendael 2011 p. 423-424 and for Lyal 2011 p. 434 and Weber 2013 p. 256.
 ¹⁶⁶ See, for instance, Zalasinski 2012 p. 452 where abuse is seen in the first case as a principle of

interpretation and in the second as a principle deriving from the legislative instruments of the Council. See also Freedman 2011 p. 370.

¹⁶⁷ C-196/04 *Cadbury Schweppes* para. 62.

¹⁶⁸ C-126/10 *Foggia* para. 35.

¹⁶⁹ On consistent interpretation, see Tenore 2009 p. 27-31.

directive.¹⁷⁰ It is, therefore, worth considering whether the interpretation of the provision could be restricted by the purpose of the PSD. The Directive strives to create better conditions for the Internal Market by granting tax advantages to cross-border distributions and eliminating any disadvantages between these situations and domestic ones.¹⁷¹ It is, consequently, evident that each time a taxpayer revokes the Directive, or rather the national legislation, he seeks to gain access to a tax benefit. Although the most important purpose for the foreign establishment would be commercial, the decision to engage in cross-border distributions includes with near certainty tax considerations that could constitute a main purpose and fall within the scope of the provision.¹⁷² This is hardly in conformance with the purpose of the Directive or the interpretation of abuse in the case law on the fundamental freedoms and could support a restrictive interpretation in this respect by reading "one of the main purposes" more narrowly.

In conclusion, given the similar formulation of the Merger Directive and its interpretation, the purpose of the PSD, and the general case law on anti-abuse measures, the PSD provision can be interpreted to require mainly tax-driven arrangements. Due to the interpretation of the Merger Directive, supported by other case law, where a lower than sole purpose standard has been accepted, it would appear possible to interpret the PSD provision in this manner. On the other hand, it is difficult to see how an arrangement where tax purposes would not play even a predominant role could represent such artificiality that would fulfill the other conditions of the provision which underlines the need to read the tax purpose test in conjunction with the "non-genuine" test and objective evaluation.¹⁷³ Nevertheless, there may persist doubt whether the formulation could be interpreted differently given the variance of the case law. More relevantly, the ECJ could require the exclusivity of tax purposes although, given the wording of the provision, this would appear to be a somewhat surprising interpretation. A more broad interpretation according to the wording of the provision may seem unlikely since such formulation has not actually been used anywhere in the discussed case law. All in all, although the new formulation can cause an amount of uncertainty, mainly tax-motivated arrangements have been seen to be compatible with the ECJ case law on wholly artificial arrangements.¹⁷⁴

¹⁷⁰ See de Broe 2008 p. 997.

¹⁷¹ See, inter alia, cases C-446/04 FII Group Litigation para. 103, C-284/06 Burda para. 51, and C-48/07 Les Vergers du Vieux Tauves para. 36.

¹⁷² See Petrosovich 2010 p. 562 for a similar criticism of the Merger Directive provision.
¹⁷³ See also Lyal 2011 p. 430-431.

¹⁷⁴ See Pistone 2007 p. 535 where this interpretation is proposed for wholly artificial arrangements.

3.2.3 Further Questions Related to the Purpose Test

It can be considered further whose aims are to be evaluated and how the purpose of the arrangement is established. If the intention cannot be established outright, it has to be derived from objective circumstances.¹⁷⁵ It has been held that the subjective element should not be established on the basis of the taxpayer's intention but, rather, on the basis of objective factors that indicate the abusive intent of the transaction.¹⁷⁶ Equally, it has been stated that the subjective intentions can be found in the artificial character of the transaction.¹⁷⁷ The same position was introduced by the Advocate General in Halifax, where it was considered that abuse of Community law is found in the objective elements of the case which indicate, therefore, the abusive intention of the transaction and which are more important than the assessment of the taxpayer's intention.¹⁷⁸ This distinction may not be, in practice, of great relevance since the tax avoidance purpose can be, arguably, derived in most cases from the objective circumstances without the need to investigate the taxpayer's subjective intentions. In the PSD provision, relevance is attached to the purpose of the arrangement even though it is of course evident that an arrangement has always a taxpayer that initiates it. Consequently, in establishing the purposes of the arrangement, the importance of different purposes can be deducted from the characteristics of the arrangement.

This leads to the second question on the relation between the artificiality evaluation and the establishment of the purpose of the arrangement. The PSD provision requires explicitly that the arrangement should be non-genuine. In *Cadbury Schweppes*, the existence of a wholly artificial arrangement was demonstrated by the subjective and objective elements, but, even in the presence of tax motives, the transaction could not be disregarded if it represented economic reality.¹⁷⁹In other words, if the objectives of the fundamental freedoms are attained through a genuine establishment in the Member State, the tax intentions become irrelevant.¹⁸⁰ On the other hand, if there are no valid commercial reasons for the arrangement, i.e., it is essentially tax driven, the arrangement can be seen to

¹⁷⁵ See Weber 2013 p. 252-253. See also Weber 2005 p. 191-192 and Peteva 2009 p. 490.

¹⁷⁶ See Schaper 2013 p. 390 where this is seen as "objective intent". See also Vogenauer 2011 p. 538-539.

¹⁷⁷ See Piantavigna 2009 p. 171. See also Snell 2011 p. 226 where the artificiality of an arrangement is seen to, obviously, include the intent as well.

¹⁷⁸ See opinion of the Advocate General 7 Apr. 2005 in *Halifax* paras. 70-71.

¹⁷⁹ C-196/04 Cadbury Schweppes paras. 64-65.

¹⁸⁰ See Vanistendael 2006 p. 194-195, Piantavigna 2011 p. 144-145, and Jimenez 2012 p. 276.

be artificial.¹⁸¹ It has been estimated that the principal purpose test could actually be fulfilled only in the case of wholly artificial arrangements.¹⁸² Furthermore, the Advocate General established in *Cadbury Schweppes* that artificiality cannot be inferred from the purpose to reduce taxation.¹⁸³ This lends itself to the conclusion that the tax purpose test of the PSD provision cannot in itself indicate the existence of abuse but only as a part of the abuse test that establishes the artificiality of the arrangement and where the predominance of tax purposes supports the presumption of artificiality. This is due to similarity with the case law on wholly artificial arrangement in the respect that genuine transactions are required, and their existence should rend the tax considerations unimportant.

There have also been opinions that a subjective test is not needed in anti-abuse provisions.¹⁸⁴ This view has been defended also by the argument that objective evidence is required which may make the motives of the taxpayer irrelevant.¹⁸⁵ It is certainly somewhat artificial to debate whether the tax saving purpose is main or sole purpose since the precise "level" of these purposes may be hard to ascertain, and the abusive purpose may be evident when the arrangement contains other artificial elements. What is more relevant is that it is not the taxpayer whose purposes need to be examined but that the purpose of the arrangement can be derived from objective circumstances. In reality, however, the purpose test may be so intertwined with the other elements of the provision that it does not stand out as a separate, clearly distinguishable test.

3.2.4 Obtainment of a Tax Advantage

Abuse of tax provisions requires the existence of a tax advantage, and if the conduct of the taxpayer has not lead to such an advantage, the legislation cannot be considered to have been abused. ¹⁸⁶ In *Cadbury Schweppes*, this was established when the arrangement was, "with a view to escaping the tax normally due," while in *Halifax*, "the essential aim of the transactions concerned is to obtain a tax advantage."¹⁸⁷ The application of anti-abuse provisions requires, therefore, a connection between the transaction and a tax advantage.¹⁸⁸ It has been, however, established by the ECJ that the mere enjoyment of tax advantages

¹⁸¹ See Freedman 2011 p. 374. For VAT-situations, see C-425/06 Part Service para. 62.

¹⁸² See Picq 2009 p. 477 where attention is given to the provision of the Merger Directive.

¹⁸³ Opinion of the Advocate General 2 May 2006 in *Cadbury Schweppes* para. 115.

¹⁸⁴ See Almendral 2005 p. 567 and Lang 2011 p. 449.

¹⁸⁵ See Sørensen 2006 p. 457.

¹⁸⁶ See Weber 2005 p. 181-182.

¹⁸⁷ C-255/02 *Halifax* para. 75 and C-196/04 *Cadbury Schweppes* paras. 55, 64.

¹⁸⁸ See Almendral 2005 p. 573.

arising from the differences in Member State legislations cannot be considered to be abusive which means that the taxpayers cannot be prevented from benefiting from these advantages.¹⁸⁹ It should be, of course, clear that gaining access to the benefits of the PSD does not as such constitute abuse of the Directive if this access does not fulfill the other conditions of the provision.

Articles 4-5 of the Directive 2011/96/EU require that the distributions within the scope of the Directive are exempted from the withholding tax in the state of source and are not taxed or are granted a tax credit in the state of the parent company or that of the PE. These advantages, entailing a lesser tax burden, form the principal benefit that can be gained from the application of the Directive, and it is, actually, difficult to see which other advantages could be gained by the abuse of the PSD. In VAT cases, it has been established that mere financing advantages arising from the deferral of tax payments cannot be considered to be abusive.¹⁹⁰ This type of situation should be less relevant with regard to the PSD since the distributed profits should have been already taxed at the level of the company before they can be accorded the benefits of the Directive.

It deserves, nevertheless, to be considered whether benefits that are external to the PSD could trigger the application of the provision. The provision requires the existence of a tax advantage contrary to the purpose of the Directive which does not set any explicit requirement that only the tax advantages provided by the Directive could be found abusive. It may be asked whether, for example, abuse of rules that concern other profit distribution situations could lead to application of the provision.¹⁹¹ It could be argued that since these tax advantages are not regulated by the Directive and do not affect its application, they should not either form a tax advantage relevant from the point of view of the PSD. What is more relevant is that with regard to the Merger Directive, which concerns the nearest comparable situation, the ECJ stated in *Zwijnenburg* that only taxes which are included in the Directive and which can be subject to its benefits can come within the scope of the anti-abuse provision.¹⁹²

It has been, however, concluded that also tax benefits external to the Directive could be relevant for the application of the anti-abuse provision in the Merger Directive. This has

¹⁸⁹ See, *inter alia*, cases C-294/97 *Eurowings* para. 44, C-9/02 *De Laysterie du Saillant* para. 60, and C-196/04 *Cadbury Schweppes* para. 49.

¹⁹⁰ See Weber 2013 p. 254 and C-103/09 *Weald Leasing* para. 38.

¹⁹¹ See, e.g., Panayi 2006 p. 152 for treaty-shopping arrangements that abuse also the benefits of the PSD.

¹⁹² C-352/08 Zwijnenburg paras. 50-56.

been defended by *Kofoed* where the ECJ allegedly permitted the prevention of such advantages and by the fact that otherwise there would be an erroneous link between the tax motives external to the Directive and its internal motives.¹⁹³ In *Kofoed*, the relevant tax advantage was not explicitly specified although two such advantages were distinguishable: one related to an exchange of shares and another related to a distribution following this exchange although it was the latter which could be regarded as the purpose of the transaction.¹⁹⁴ The ECJ found that the exchange of shares was a transaction to which the benefits of the Directive applied, but these could be, however, withdrawn in the case of abuse.¹⁹⁵ The question whether the advantages related to a dividend distribution after the transaction could be caught the anti-abuse provision was not answered explicitly.

Nevertheless, a later case *Zwijnenburg* established clearly that the tax benefits could not be withheld when the taxpayer sought, "to avoid the levying of a tax such as that at issue in the main proceedings, namely transaction tax, where that tax does not come within the scope of application of that directive."¹⁹⁶ The same view was adopted by the Advocate General due to the exceptional nature of the provision which could not expand its scope to other taxes that were not within the scope of the Directive.¹⁹⁷ This is, arguably, the most reasonable conclusion since otherwise the anti-abuse rule in the Merger Directive would have an unlimited scope of application because any tax advantage, although not related to the benefits of the Directive and not within its scope of harmonization but connected to its transactions, could lead to withdrawal of these benefits. Therefore, if the somewhat unclear *Kofoed* is regarded in the light of *Zwijnenburg*, it appears that tax advantages which do not relate to the benefits of the Directive cannot lead to application of the anti-abuse provision in the Directive.

These cases support a similar interpretation of the PSD provision which would imply that only the avoidance of those taxes that are connected with the benefits of the Directive could be considered to constitute a relevant tax advantage. It must be noted that in contrast to the Merger Directive, which regulates such transactions that can be used to avoid also other taxes in addition to those mentioned in the Directive, the distributions regulated by the PSD cannot, generally speaking, be used to attain other tax goals since the PSD

¹⁹³ See Jimenez 2012 p. 282.

¹⁹⁴ C-321/05 *Kofoed* paras. 14-20.

¹⁹⁵ Ibid. para. 48.

¹⁹⁶ See C-352/08 Zwijnenburg para. 56.

¹⁹⁷ See opinion of the Advocate General 16 July 2009 in Zwijnenburg para. 53.

requires the taxation of company profits as a condition to its application.¹⁹⁸ In addition, the provision has a stated aim to prevent abuse of the Directive with respect to taxpayers that come within its scope of application while authorizing the Member States to apply other anti-abuse rules.¹⁹⁹ This implies that the main focus of the provision is clearly abuse of the PSD which supports, additionally, conclusions similar to *Zwijnenburg*. The taxes covered by the Directive apply, most likely, to a larger group of transactions than the one which comes within the scope of the PSD, but since such situations are not regulated by the Directive and cannot be accorded its benefits, they should not trigger the application of the provision. Consequently, a treaty-shopping arrangement where the benefits of a tax treaty are misused should not trigger the application of the provision if the abusive arrangement has not lead to a tax advantage which arises from the Directive.

Last, it may be considered whether in the absence of Member State taxation of comparable distributions, there could still be a tax advantage. In this case, it would appear *prima facie* that the situation of the taxpayer is not any better when he avails himself of the benefits of the PSD since he was not subjected to any taxation in the beginning, and there is, therefore, no tax advantage that could be obtained abusively. There are, however, always two countries that can grant the benefits to a certain distribution which means that the lack of taxation either in the source state or in the state of the parent company should not prevent the arrangement from gaining abusively the benefits of the Directive in the other country.

Nevertheless, the anti-abuse provision of the PSD qualifies the tax advantages further by requiring that they are obtained against the purpose of the Directive which is, of course, necessary, since the main purpose of the Directive is to grant these advantages. The analysis of this condition will follow in the next section.

3.3 How the Purpose of the Directive is Defeated

The requirement in the new provision that the tax advantage, "defeats the object or purpose of this Directive," reflects the objective test in the anti-abuse case law of the ECJ.²⁰⁰ In *Emsland-Stärke*, this was formulated as, "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."²⁰¹ The test was supplanted in direct taxation

¹⁹⁸ Critique on the *Zwijnenburg* in this respect, see Petrosovich 2010 p. 561.

¹⁹⁹ See recital 2 of the preamble to the Directive 2015/121/EU and Art. 1(4) of the same Directive.

²⁰⁰ See Weber 2011 p. 396.

²⁰¹ See case C-110/99 *Emsland-Stärke* para. 52.

in *Cadbury Schweppes* where the conduct was evaluated in the light of the objectives of the freedom of establishment.²⁰² In general, abuse in the EU law requires that the benefit is obtained in a way that is contrary to the purpose of the rule in question.²⁰³ The assessment on whether the objectives of the EU legislation have been attained or not is a task of the ECJ since the interpretation of the purposes of the Union legislation remains within the competence of the Court.²⁰⁴ Since the purpose of the PSD was already discussed, this section analyses how a tax advantage can be contrary to this purpose. The expressions object and purpose, stated in the provision, can be deemed to be synonymous.

Before the arrangement can be considered to be against the purpose of a provision, there must have been formal observance of the rule. This implies that the taxpayer has complied with the conditions laid down in the wording of the provision.²⁰⁵ With regard to the PSD, this means that the taxpayer has fulfilled the requirements set down in the Directive and has, therefore, gained access to the tax benefits. Accordingly, there must be a company of a Member State which complies with the criteria set down in the Directive.

In the next step, it must be established that, despite the fulfillment of the formal requirements, the purpose of the provision would be compromised if the advantage was granted. Occasionally, the problem in this evaluation may be that the purpose of the provision is contested.²⁰⁶ This would not appear to be the case with the PSD since the Directive states clearly the purpose of alleviating tax hindrances and supporting cross-border establishment. Consequently, a company fulfilling the formal criteria and gaining access to the advantages of the PSD is the main way how the purpose of the Directive is attained. This is one of the aspects where the approach of the new provision has been questioned since the purpose of the PSD is addressed to the Member States instead of the taxpayers, and it emphasizes that granting the tax benefits should be generally in line with this purpose.²⁰⁷ On the other hand, it would appear that, given the specific conditions laid down in the Directive, the purpose of the PSD could be defeated if some party gained access to these benefits when it would not, due to wrong place of residence, company form, tax-free status, or lacking shareholding, be entitled to them directly. Furthermore, the

²⁰² C-255/02 Halifax para. 74 and C-196/04 Cadbury Schweppes para. 64.

²⁰³ See Vogenauer 2011 p. 537.

²⁰⁴ See Weber 2005 p. 186 where the case-by-case nature of this analysis is underlined.

²⁰⁵ C-110/99 *Emsland-Stärke* para. 52 and C-196/04 *Cadbury Schweppes* para. 64. See also Vogenauer 2011 p. 531.

²⁰⁶ See Snell 2011 p. 225.

²⁰⁷ See Tavares - Bogenschneider 2015 p. 491.

purpose could not be attained if the arrangement did not aim to improve cross-border grouping of companies within the Member States.²⁰⁸

The PSD strives to improve the position of company groupings in the Member States in comparison with purely domestic situations. Therefore, the PSD can be considered not to be aimed to alleviate the taxation of non-Member State entities.²⁰⁹ If the tax advantages were to ultimately benefit third-country companies, it could be argued that the obtainment of these advantages has been contrary to the Directive's purpose. The benefits are, of course, always initially granted to companies of Member States, but if the objective of this company was to function only as a conduit for a non-Member State beneficiary, the distribution would not contribute, arguably, to the grouping of companies in the EU and the creation of the Internal Market. It has been considered that passive holding companies serving only the purpose of third-country residents would not attain the purposes laid down in the Directive.²¹⁰ There have also been opinions that this could be, in reality, the only way how the tax advantages could be obtained contrary to the purpose of the PSD.²¹¹

It may be, therefore, asked whether the objective test could be fulfilled in purely EU situations i.e., how a tax advantage in these cases could be against the purpose of the Directive. First, it may be considered whether a tax advantage could accrue to a company not entitled to it. All the Member States are obliged to grant the benefits to companies that fulfill the requirements, but different Member States may have enacted the Directive more strictly or more generously.²¹² For instance, it is possible that a company in a Member State could, due to lacking shareholding, exploit the lower participation exemption rules in other Member States in order to gain access to the PSD benefits.²¹³ Elsewhere, this type of situations has been considered to fall within the scope of the new provision.²¹⁴ This interpretation appears to be, in principle, possible although seeking access to more advantageous legislation in force in other Member States cannot in itself constitute abuse.²¹⁵ Moreover, it has been considered that it is not relevant from the perspective of the Directive in which Member State the taxes are ultimately paid and how the companies

²⁰⁸ Similarly Picq 2009 p. 475.

²⁰⁹ See Rousselle - Liebman 2006 p. 563.

²¹⁰ See de Broe 2008a p. 148. See also COM(2007) 785 p. 8 and Weber 1997 p. 26-27.

²¹¹ See Knobbe-Keuk 1992 p. 489, Rädler - Lausterer - Blumenberg 1997 p. 98, and Debelva - Luts 2015 p. 226.

 $^{^{212}}$ See Tenore 2010a p. 233 and footnote 81. See also Picq 2009a p. 537.

 $^{^{213}}$ See de Broe 2008 p. 23-24 and examples p. 34, 37.

²¹⁴ See Weber 2016 p. 116.

²¹⁵ See e.g. C-212/97 Centros para. 27 and C-9/02 De Laysterie du Saillant para. 60.

establish subsidiaries in other EU countries.²¹⁶ It is equally difficult to see how the fact that the shareholders would enjoy more beneficial taxation in one Member State could bring the purpose of the distribution against the purpose of the Directive since the shareholders are, inherently in the case of the PSD, in different Member States. When the obtainment of these benefits entails, however, artificial conduct, the purpose may not be attained.

Second, it can be examined whether the establishment of companies in other Member States in order to benefit from the Directive could be against the purpose of facilitating cross-border grouping of companies. First, it could be argued that short-term ownership of shares with the only purpose of gaining the benefits of the Directive could be contrary to this purpose, but since this type of abuse is dealt with in the Article 3(2) of the PSD, it should not be countered by the general anti-abuse provision.²¹⁷ On the other hand, it could be considered that even low-substance arrangements with the purpose of benefiting from the advantages of the Directive would contribute to the grouping of companies across Member State borders since the absence of such an establishment would not achieve this purpose and would lead to taxation that the PSD tries to avoid.²¹⁸ It appears, in general, that establishing companies in other Member States could only rarely if ever be against the purpose of facilitating cross-border groupings since these establishment actually attempt to improve these groupings. The possible breach of the purpose of the Directive can, therefore, arise mostly in situations where the ultimate shareholder would not be entitled to these benefits in the absence of the arrangement.

However, it is possibly to advance the argument that granting the tax advantages would be in accordance with the purpose of the Directive even in the cases with a third-country link. The fact that a company in a Member State has shareholders outside the EU or conducts business only in these countries does not imply that the company would warrant less protection under the freedom of establishment.²¹⁹ This view on the purpose of the PSD has been considered restricted also due to the fact that the free movement of capital has been expanded to cover also third-country situations.²²⁰ Consequently, it is not possible to regard all companies with foreign shareholding as abusive arrangements. Moreover, if the Member State has extended the benefits of the PSD to third-country companies, it can be

²¹⁶ See Knobbe - Keuk 1992 p. 489 and Rädler - Lausterer - Blumenberg 1997 p. 98.

²¹⁷ See Brokelind 2003 p. 162.

²¹⁸ Similarly Rousselle - Liebman 2006 p. 563.

²¹⁹ See Tenore 2010a p. 234 and Poulsen 2013 p. 234. See also C-476/98 *Open Skies* para. 146 and Schelpe 1997 p. 21.

²²⁰ See Panayi 2006 p. 154.

hard to argue that the attainment of these benefits would be contrary to the purpose of the Directive.

On the other hand, since the Directive makes reference to improving the productivity and competitive strength of Member State companies, the purpose has been read to require something more than the mere obtainment of tax advantages i.e., the PSD does not only aim to grant tax benefits, but it aims to grant them with the purpose of creating better conditions for cross-border business in the Internal Market.²²¹ Therefore, the purpose of creating companies with the sole aim of gaining these tax benefits can be included in the evaluation.²²² Nevertheless, the Directive does not actually require that the companies concerned should have economic activities and it cannot be, consequently, regarded as a further condition to its application.²²³ The lack of economic purpose serves, however, a role in the evaluation of the genuineness of the arrangement.

In conclusion, the situations where the tax relief granted to purely EU groups could defeat the purpose of the Directive appear to be quite scarce, but could exist if a difference in the Member State legislations could be exploited to obtain the benefits without a real aim to create a grouping of companies. More relevance may reside in the situations with a third-country connection where there could be an incentive to utilize the benefits of the PSD for abusive aims. All in all, it is not enough that a conduct as such could appear to against the purpose of the provision but there must be, in addition, evidence of abusive practices.²²⁴

3.4 Non-Genuine Transactions

3.4.1 General Notions on the Concept

The PSD anti-abuse provision requires that the arrangements are not genuine which is the case, "to the extent that they are not put into place for valid commercial reasons which reflect economic reality." Genuine as a word was utilized in *Cadbury Schweppes* with reference to actual use of the freedom of establishment through "genuine economic activities."²²⁵ Interestingly, a new directive proposal on countering tax avoidance practices

²²¹ See Weber 1996 p. 66 and de Broe 2008 p. 1015. See also Recital 4 of the preamble to the Directive 2011/96/EU.

²²² See C-283/94, C-291/94, C-292/94 *Denkavit-VITIC-Voormeer* para. 31 and Schelpe 1997 p. 22.

²²³ See Terra - Wattel 2012 p. 616 where it is stated that substantive activity instead of passive investment in the subsidiary cannot be required.

²²⁴ See Snell 2011 p. 225.

²²⁵ C-196/04 *Cadbury Schweppes* paras. 54, 66 and 75.

proposes a general anti-abuse rule with a wording similar to the PSD provision and where non-genuine is explicitly equated with wholly artificial arrangements.²²⁶ Valid commercial reasons, on the other hand, is an expression that is used in the anti-abuse provision of the Merger Directive.²²⁷ The notion economic reality has been developed in the case law on direct taxation where it has been contrasted with wholly artificial arrangements i.e., a transaction is wholly artificial if it is not based on economic reality, and this reality was based on establishment in line with the purpose of the provision.²²⁸

The PSD provision appears prima facie to use a new formulation to define abuse which leads to the question whether the PSD provision aims to create a new, different standard to define the artificiality of the arrangement. An analysis of the case law and of the development of different expressions present in distinct fields of taxation is needed in order to develop the boundaries of the PSD anti-abuse provision.

3.4.2 Valid Commercial Reasons

The anti-abuse provision of the Merger Directive states that if the operation has not been carried out based on valid commercial reasons, "such as the restructuring or rationalisation of the activities of the companies participating in the operation," the operation can be presumed to have an abusive purpose.²²⁹ Valid commercial reasons and tax avoidance are, therefore, contrasted in the provision. It was discussed earlier what significance the tax reasons should have in establishing the abusive nature of the arrangement, and, although these notions are not reproduced here, the evaluation of valid commercial reasons can be seen to be integrally connected with this analysis since in the absence of valid commercial reasons, the transaction can be considered to be abusive.²³⁰

The content of valid commercial reasons has been defined further in the ECJ case law. In Leur-Bloem and repeated in Foggia, the ECJ stated that these reasons include, "more than the attainment of a purely fiscal advantage."²³¹ In *Kofoed*, the valid commercial reasons were not defined further, but abusive transactions were characterized as, "carried out not in the context of normal commercial operations."232 Furthermore, as established above, the

²²⁶ See recital 9 to the preamble and Art.7 of COM(2016) 26.

²²⁷ See Art. 15(1) of the Directive 2009/133/EC.

²²⁸ For example, C-196/04 Cadbury Schweppes paras. 55, 64, 65 and C-524/04 Thin Cap Group Litigation para. 74.

Art. 15(1)a of the Directive 2009/133/EC.

²³⁰ See Jimenez 2012 p. 281.

²³¹ C-28/95 Leur-Bloem para. 47 and C-126/10 Foggia para. 34.

²³² C-321/05 Kofoed para. 38.

ECJ stated in *Foggia* that the existence of tax reasons does not preclude the possibility that the transaction could have valid commercial reasons as long as the former are not predominant, and if the sole reason of the transaction was the obtainment of a tax advantage, the valid commercial reasons would not exist.²³³ The Court went, however, further and established that since the tax advantage, acquisition of losses, was very substantial, the fact that the merger had also effects on the cost structure, which were deemed inherent to the transaction, could not constitute valid commercial reasons.²³⁴

Although the exclusivity of fiscal reasons indicates, necessarily, the absence of commercial reasons, it is, however, possible to reach the same conclusion if the tax reasons are predominant or if the commercial reasons are only ancillary and not in proportion to the tax reasons. When there are relevant commercial reasons, the taxpayer can take tax considerations into account when structuring his transactions.²³⁵ There have been commercial reasons excluded, the ECJ would actually accept any reasons as commercial reasons since it has stated that the Merger Directive applies to all transactions within its scope irrespective of their reasons.²³⁶ However, this concerns, as the Court considers, only the eligibility of the transactions to the benefits of the Directive, and the reasons become relevant in the application of the anti-abuse provision. If this is applied to the PSD, the possible commercial reasons would not be sufficient to save the arrangement when its main purpose would be the obtainment of a tax advantage.

Nevertheless, attaching relevance only to the reasons of a transaction may be an inadequate way to establish the abusiveness of the transaction. In the case of the Merger Directive, the ECJ has not separately evaluated the economic reality of the transaction. On the contrary, it was clearly established in *Cadbury Schweppes* that tax motives are not relevant if the transaction reflects economic reality.²³⁷ Furthermore, the ECJ has held that the mere fact that the transaction or establishment leads to tax benefits cannot justify restrictive actions.²³⁸ Given the similar wording of the PSD provision, it can be required that, in addition to the existence of tax reasons, the arrangement must also be artificial according

²³³ C-126/10 *Foggia* paras. 35-36.

²³⁴ Ibid. paras. 47-52.

²³⁵ See Terra - Wattel 2012 p. 696.

²³⁶ See Petrosovich 2010 p. 563 and C-352/08 Zwijnenburg paras. 41-42.

²³⁷ C-196/04 *Cadbury Schweppes* para. 65.

²³⁸ See, for example, C-294/97 *Eurowings* para. 44, C-9/02 *De Laysterie du Saillant* para. 60 and C-196/04 *Cadbury Schweppes* para. 37.

to objective circumstances i.e., it does not reflect economic reality.²³⁹ Economic reality signifies that the company carries out genuine economic activity in the Member State of establishment or that its operations are not otherwise artificial.²⁴⁰ If the criteria are contrasted, it can be, however, assumed that a transaction which has no valid commercial intent at all would also be artificial under the criteria of economic reality since in these cases it is probable that there is nothing else but the structure needed to attain the tax benefit. A transaction can be found artificial if it does not have a valid commercial purpose besides the tax saving purpose.²⁴¹ The PSD provision establishes a link between the valid commercial reasons of the arrangement and economic reality, and it is reasonable to conclude that the concepts are not meant to be evaluated separately.

What is, therefore, the impact of the expression "valid commercial reasons" for the PSD provision? In the first interpretation, the valid commercial reasons can be seen only to emphasize the economic reality of the arrangement if it is seen in the light of formulation in *Cadbury Schweppes* which required "actual establishment" and "genuine economic activities."²⁴² Valid commercial reasons could be interpreted also as one expression of the subjective test, and they are, essentially, evaluated in this context as a counterweight to tax reasons.²⁴³ If economic reality of the arrangement has been established, there is no further need to consider whether there are valid commercial reasons since they have already been demonstrated by real economic activity. It is of course possible to envisage a situation where there, evidently, would be genuine commercial activity but which would not have any reasonable commercial purpose i.e., it would not, for instance, aim to gain profits.

The second interpretation would be to weight valid commercial reasons against the tax purposes as it was done in *Foggia*. There economic reality was not evaluated, similarly to case law on wholly artificial arrangements, with regard to the substance of the arrangement but rather in relation to its tax purposes, and if these purposes were predominant, the transaction could be considered to be abusive. The obvious difference is the parallel between the PSD provision and the formulation of *Cadbury Schweppes*. This may lead to the conclusion that balancing the reasons of the arrangement should not alone determine the existence of abuse although they are part of this evaluation. As a consequence, the

²³⁹ See Lyal 2011 p. 430-433.

²⁴⁰ See de Broe 2008a p. 144, Poulsen 2012 p. 206, and C-196/04 *Cadbury Schweppes* paras. 66-68.

²⁴¹ See Freedman 2011 p. 374 where the purpose test is seen as a possible proxy to economic reality.

²⁴² C-196/04 *Cadbury Schweppes* para. 66.

²⁴³ For this interpretation, see Debelva - Luts 2015 p. 227.

concept "economic reality" must be given a closer look first, regarding the elements which can indicate the lack thereof and, second, regarding the level of artificiality required.

3.4.3 Economic Reality

Before starting to evaluate the significance of the economic reality criterion, it should be considered whether this criterion, developed in *Cadbury Schweppes*, is suitable for dividend taxation. In this and subsequent cases on direct taxation, the economic reality was contrasted with wholly artificial arrangements, "with a view to escaping the tax normally due on the profits generated by activities carried out on national territory."²⁴⁴ This criterion may be more complicated to apply to cases of dividend taxation, such as that of the PSD, since they do not actually concern allocation of income but rather avoidance or circumvention of dividend tax.²⁴⁵ It has been proposed that these cases should require additional tests in addition to allocation of income in establishing the abusive nature of the transaction.²⁴⁶ Evaluating whether the allocation of taxes between the Member States has been distorted is evidently not a relevant element in the application of the anti-abuse provision of the PSD since the distributed profits should have already been subjected to taxation on the level of the company. The economic reality test can, however, be applied to the cases concerning avoidance of taxes on distributions if it is adapted to the specifics of these situations. In direct tax cases, the economic reality has been evaluated in the context where the transaction did not allegedly correspond to normal economic conduct.²⁴⁷ What is needed, therefore, is an evaluation of the content of the arrangement in the light of the purpose of the provision in question.²⁴⁸ In the cases of outright fraud, the provision can most probably be applied without this evaluation.²⁴⁹

This entails that the relevant elements of economic reality in the context of the PSD are established. As a starting point can be utilized the concept in *Cadbury Schweppes* where it was required that, first, there is actual establishment and, second, genuine economic activity.²⁵⁰ The Court considered this with regard to physical existence of the company in

²⁴⁴ C-196/04 *Cadbury Schweppes* para. 55. See also e.g. C-524/04 *Thin Cap Group Litigation* para. 74 and C-105/07 *Lammers & Van Cleeff* para. 28.

²⁴⁵ See Weber 2013 p. 258 and Poulsen 2013 p. 240. See also joined cases C-436/08 and C-437/08 *Haribo-Salinen* para. 123.

²⁴⁶ See Poulsen 2012 p. 211.

²⁴⁷ See, *inter alia*, C-524/04 *Thin Cap Group Litigation* para. 80, C-182/08 *Glaxo Wellcome* paras. 89-91, C-318/10 *SIAT* paras. 40-42, and C-282/12 *Itelcar* para. 35.

²⁴⁸ This was presented as substance over form analysis in COM(2007) 785 p. 4.

 $^{^{249}}$ See Sørensen 2006 p. 431 where it is considered that fraud can be combated more broadly in the EU law.

²⁵⁰ C-196/04 *Cadbury Schweppes* para. 66.

terms of staff and property and with reference to "letter box" companies that do not fulfill these requirements.²⁵¹ If, for example, a company in a PSD arrangement would be completely void of substance and activities, this approach could lead to its consideration as an abusive arrangement. The test contains, however, issues with regard to abuse of the PSD. First, there is the question of substance regarding the establishment i.e., what is required so that a company can be regarded to be genuinely established in a Member State since the amount of substance required is tied to the characteristics of the establishment in question.²⁵² The Commission considered in its communication on anti-abuse measures that since holding and financing companies may require relatively little in terms of physical presence, the Cadbury Schweppes substance requirement may not function as such in these situations.²⁵³ The limited amount of substance, such as office space and staff, that is required by these companies should not lead to an automatic conclusion that the companies lack economic reality if the assets are actively managed.²⁵⁴

The problem is equally related to the required amount of economic activity. First, the ECJ has considered in several cases on corporate law that the parent company can actually conduct all its business in the Member States of its subsidiaries.²⁵⁵ What is, however, relevant to notice is that the PSD arrangements involve, inherently, at least two companies in different Member States. Consequently, there must a company whose profits are paid as distributions to the parent company which does not have to have own activities. These cases of secondary establishment require the pursuit of economic activity for an indefinite period in the host state.²⁵⁶ If the subsidiary does not engage in any activities other than passive management of assets or if the activity actually takes place in the state parent company in the EU or in a third country, it may be considered not to fulfill the requirements for secondary establishment.²⁵⁷ The same conclusion can be made if the subsidiary does not have sufficient physical substance or if the establishment cannot be deemed to be cross-border.²⁵⁸ If the activities and the establishment of the subsidiary cannot be, therefore, considered to be adequate for a real establishment to have occurred,

²⁵¹ Ibid. paras. 67-68.

²⁵² See Poulsen 2013 p. 245 where the establishment is seen to require only such substance that is enough to pursue its activities. 2^{53} S = 225

See COM(2007) 785 p. 4.

²⁵⁴ See De Broe 2008a p. 144.

²⁵⁵ See cases C-79/85 Segers para. 16, C-212/97 Centros para. 29, and C-167/01 Inspire Art para. 139. See also de Broe 2008 p. 856-859.

²⁵⁶ See C-221/89 Factortame para. 20 and C-196/04 Cadbury Schweppes paras. 53-54.

²⁵⁷ See Evers - de Graaf 2009 p. 284, C-196/04 *Cadbury Schweppes* para. 68, and C-386/04 *Stauffer* para. 19.

²⁵⁸ Ibid. p. 284-285. See also de Broe 2008 p. 855 where passive companies are seen to fail the test.

the arrangement could be seen not to fulfill the conditions of the economic reality test of the PSD provision. In the cases where the establishment entails real economic functions that are effected in the state of the subsidiary, this conclusion cannot be reached. It has been considered that the lack of economic activities by the parent company or the fact that the management of the subsidiaries takes actually place in a third country can be relevant factors in this kind of assessment.²⁵⁹

Nevertheless, the definite amount of activity that saves the arrangement from the provision may be more complex to establish. Since the usage of different holding company structures can be regarded as a normal way of organizing international groups, the fact that such companies may carry few operations cannot rend them outright abusive. ²⁶⁰ It was considered by the Advocate General in Columbus Container Services that holding and capital management could not be regarded to constitute purely artificial conduct when they are combined with actual establishment.²⁶¹ The activity can be considered genuine even if it would relate to management of income or similar functions if this level of activity can be regarded to be sufficient in the case at hand.²⁶² What can be considered as genuine economic activity and, as a consequence, sufficient for not to constitute a non-genuine arrangement cannot be, therefore, unequivocally established. Nevertheless, it is apparent that considering holding companies or other entities with relatively thin substance and few actual activities as always failing the economic reality test of the PSD would not be an acceptable interpretation of the PSD anti-abuse provision.²⁶³ The economic reality test requires a careful consideration of the facts of the case and an evaluation of the substance and the level of activity that actually is required for a certain type of situations.

This should not, however, imply that the PSD provision could not actually be applied to holding companies or financing companies. What is required is that the company carries out activity which is sufficient to its purpose, taxation excluded, and that it does not represent artificiality.²⁶⁴ In some situations, the company could be considered to have its residence outside the Union which could lead to the denial of the benefits without a need to recourse to the anti-abuse provision.²⁶⁵ In most situations, caution must be exercised since

²⁵⁹ See Evers - de Graaf 2010 p. 245-246 where a test for preventing conduit arrangements is discussed.

²⁶⁰ See Lang 2011 p. 445 and Poulsen 2013 p. 246. See also de Broe 2008 p. 845-846.

²⁶¹ See opinion of the Advocate General 29 March 2007 in *Columbus Container Services* paras. 181-183.

²⁶² See Robert - Tof 2011 p. 438, 442.

²⁶³ See also Debelva - Luts 2015 p. 227.

²⁶⁴ See Lang 2011 p. 445 and Jimenez 2012 p. 286-287.

²⁶⁵ See Brokelind 2003 p. 162 where this requirement was seen to be in accordance with former Art. 1(2).

the interpretation of economic reality by the ECJ requiring wholly artificial arrangements sets, arguably, a high standard.²⁶⁶ The evident problems in evaluating abuse under the PSD provision in the light of genuine establishment may lead to the conclusion that also other elements are needed.²⁶⁷

The concept of economic reality should, therefore, be defined further in order to establish the elements that are relevant for a specific situation. For example, in Thin Cap Group Litigation, the analysis concerned the commercial terms of the arrangement which were different from those between independent companies.²⁶⁸ It has been considered that such elements as close timing of the transactions, distribution of risks between different companies in a group, and the authority of the intermediate company to decide on the use of its income can be used to evaluate whether the arrangements concerning directiveshopping can be found to be artificial.²⁶⁹ The fact that a company does not bear risk corresponding to its activities or cannot dispose of its income and pays it immediately to a higher group company can also serve as an indication of the lack of economic reality.²⁷⁰ Furthermore, it has been suggested that the fact that the arrangement transfers dividends to third-country companies with a lower tax burden than in direct payments could indicate abuse.²⁷¹ In conclusion, there appears to be various factors which can be included in the evaluation of the economic reality of the arrangement and which can establish that the arrangement has not been set up for commercial purposes. The national legislators cannot, however, implement general and automatic provisions which would deny the benefits of the directive in all cases fulfilling certain, predetermined criteria.²⁷²

What may be considered further is the specific situation where the holding in the company does not reach such levels that the shareholder could actually control the management of the company. The Article 3(a)i of the PSD requires a holding of more than 10 % which leaves room for relatively small holdings to gain access to the benefits of the Directive and which would be shielded by the free movement of capital.²⁷³ The difference between this freedom and the freedom of establishment has been established, on the one hand, on the basis of definite influence that the holding gives to the taxpayer and, on the other hand,

²⁶⁶ See also Memo 13/1040 25 Nov 2013 p. 3 where the wholly artificial scenario is evoked.

²⁶⁷ See also Sørensen 2015 p. 107-108 where the initial provision was seen to concern the aim of activities.

²⁶⁸ See C-524/04 *Thin Cap Group Litigation* para. 80.

²⁶⁹ See Poulsen 2013 p. 247-249.
²⁷⁰ Ibid. See similarly Weber 2016 p. 124.

²⁷¹ See Picq 2009 p. 474-475.

²⁷² See C-28/95 *Leur-Bloem* para. 44 and C-451/05 *ELISA* para. 91.

²⁷³ For a case where both freedoms where examined, see C-387/11 Commission v Belgium paras. 34-35.

examining whether the national legislation concerns groups of companies or holdings giving definite influence or whether it is neutral although there is amount of ambiguity in this respect.²⁷⁴ These situations do not require actual establishment in a Member State, and the aforementioned substance criteria is less adequate to establish abuse in these situations which underlines the relevance of other criteria in examining the economic reality.²⁷⁵

In conclusion, if the arrangement does not have a valid commercial foundation, its economic reality can be questioned. ²⁷⁶ Given the issues related to the substance test, it may be more relevant to evaluate the abuse in the context of the PSD with regard to other factors that show the non-genuine nature of the arrangement. What will these factors be is, ultimately, depended on the finer composition of the facts of the case.

3.4.4 The Level of Required Artificiality

After examining the elements of economic reality, it should be considered how high the level of artificiality should be in the case of the PSD provision. The provision does not use the expression wholly artificial arrangements which was not present in the initial proposal either.²⁷⁷ More crucially, the provision requires that the tax reasons should be only one of the main reasons for the arrangement which could, if not interpreted to require the predominance of tax purposes as was suggested above, imply a different standard. It should be, therefore, discussed whether such a conclusion could be reached.

The EU legislature has discretion to enact measures differing from the ECJ case law although this intent cannot be discerned from the Commission proposal, and the measures should, at any rate, respect the fundamental freedoms.²⁷⁸ There are, however, several issues that could surface with an interpretation that departs from the wholly artificial standard. If the artificiality criterion would be lower, the PSD provision could interfere not only with artificial arrangements but also with arrangements that have relevant business reasons. It is, nevertheless, possible to consider whether in the case of third-country constructions this would be unjustified, since these companies are not actually, under any circumstances, entitled to the benefits of the PSD. In this case, the issue lies in the fact that the provision is always applied to Member States entities no matter where their parent company resides.

²⁷⁴ See, *inter alia*, C-251/98 *Baars* para. 22, C-196/04 *Cadbury Schweppes* para. 31, C-524/04 *Thin Cap Group Litigation* para. 33, and C-157/05 *Holböck* paras. 22-24. See also Cordewener 2009 p. 261-262.

 ²⁷⁵ See also Lang 2011 p. 447 where it is concluded that a stricter concept of abuse could apply here.
 ²⁷⁶ Similarly Poulsen 2013 p. 250.

²⁷⁷ COM(2013) 814 p. 9 where the expression "artificial arrangement" is used.

²⁷⁸ See Kofler - Tenore 2010 p. 314-316 on the relation between fundamental freedoms and the directives.

It can be, therefore, considered what a lower standard for artificiality would mean for EU companies. First, it could lead to situation where "normal" holding companies, whose substance may be inherently low, could be considered to be non-genuine and be denied the benefits of the PSD. Furthermore, it could even lead to the exclusion of such companies that have some real and verifiable activity but in which the tax reasons would still present themselves as a relevant objective. This would be evidently in disaccord with the previous ECJ case law and could lead to serious consequences to multinational groups in the EU.

Nevertheless, the secondary legislation including the PSD anti-abuse provision must be interpreted in the light of the fundamental freedoms by choosing the interpretation that best conforms to their purpose.²⁷⁹ This is also the way how the ECJ avoids conflicts between secondary and primary law.²⁸⁰ In order to prevent restrictions to the fundamental freedoms, the ECJ has consistently evaluated the economic reality criterion in its direct tax case law in connection with wholly artificial arrangements.²⁸¹ The same interpretation has been established in several VAT cases.²⁸² This consistent case law supports clearly the interpretation where the economic reality criterion is not set lower than wholly artificial arrangements, and it would be somewhat unexpected if the ECJ interpreted the criterion less strictly than it has done before.²⁸³ Even the Commission stated explicitly that "normal" transactions should not be constrained by the provision.²⁸⁴

The interpretation of lower artificiality could also jeopardize the purpose of the PSD since it could make the grouping of companies more difficult even in non-abusive situations by making the establishment in other Member States less attractive. Although combating tax abuse is a legitimate aim, it should not undermine or even render ineffective the purpose of alleviating the obstacles to cross-border groups within the Union. Should the required artificiality be lower than the level adopted so far by the ECJ, the common system of taxation created by the PSD could be seriously compromised since even situations other than pure letter-box companies could be found abusive. Ironically, this could make the

²⁷⁹ See C-168/01 *Bosal Holding* para. 26, C-471/04 *Keller Holding* para. 45, and C-138/07 *Cobelfret* para. 55. See also Szudoczky 2010 p. 191-193.

²⁸⁰ See Sørensen 2011a p. 341, 344.

 ²⁸¹ See, *inter alia*, C-105/07 *Lammers & Van Cleeff* para. 28, C-303/07 *Aberdeen* para. 64, C-318/10 *SIAT* para. 40, C-80/12 *Felistowe* para. 33, and C-282/12 *Itelcar* para. 34.
 ²⁸² See, *inter alia*, C-162/07 *Ampliscientifica* para. 28, C-504/10 *Tanoarch* para. 51, and C-653/11 *Newey*

 ²⁸² See, *inter alia*, C-162/07 *Ampliscientifica* para. 28, C-504/10 *Tanoarch* para. 51, and C-653/11 *Newey* para. 46.
 ²⁸³ See also Teverse. Dependent in the 2015 of the teverse for the second second

 ²⁸³ See also Tavares - Bogenschneider 2015 p. 494 who see the rule to require wholly artificial arrangements.
 ²⁸⁴ See SWD(2013) 474 p. 23.

distributions under the PSD less secure than the distributions outside of it.²⁸⁵ Even the new provision echoes the ECJ case law by requiring that the application should be proportionate and "serve the specific purpose" of combating non-genuine arrangements.²⁸⁶

In conclusion, if the economic reality criterion is interpreted in the light of case law on the fundamental freedoms where it has been developed, it should, even in the absence of an explicit mention, require the existence of a high level of artificiality. This interpretation has also been seen to conform to the main purpose test which is a possible interpretation of the tax purpose test in the provision.²⁸⁷ It is, moreover, supported by analogy by the text of the new directive proposal on countering tax avoidance practices where a remarkably similarly worded provision requiring non-genuineness is, in its preamble, explicitly aimed at "wholly artificial arrangements" which could imply that this is the interpretation actually intended.²⁸⁸ In addition, the economic interest is, in the case of the PSD, that of the Member States which does not support any wider scope for the provision. All in all, the ECJ would, arguably, make quite a radical change if it were to interpret the provision more broadly than previously. The different choice of wording is, nevertheless, regrettable given the fact that the Commission underlined the compatibility of the PSD provision with the Treaty freedoms and stated that it reflects the ECJ case law on abuse of rights.²⁸⁹

3.5 Conclusions on the Interpretation of the PSD Anti-Abuse Rule

In the previous chapters, the general anti-abuse provision of the PSD has been interpreted in the light of ECJ case law on abuse of tax law. Since the abusive situations in the ambit of the PSD require, necessarily, a company that gains access to the benefits of the Directive, the conditions on the existence of an arrangement and a tax advantage are fulfilled nearly automatically although the arrangement can also include other, relevant steps. A tax advantage is contrary to the purpose of the PSD essentially in such situations where a taxpayer who would not have been entitled to the benefits directly gains access to them through a non-genuine arrangement.

More questions relate to the tests on subjective purpose and economic reality. Since artificiality is expressly required, a mere tax saving purpose cannot turn the arrangement abusive. The new language of the PSD provision creates, however, suspicions whether it

²⁸⁵ See Brokelind 2015 p. 824.

²⁸⁶ See recital 6 of the Directive 2015/121/EU and C-524/04 *Thin Cap Group Litigation* para. 79.

²⁸⁷ See e.g. Cerioni 2010 p. 805-806 and Weber 2013 p. 256.

²⁸⁸ See recital 9 to the preamble and Art. 7 of COM(2016) 26.

²⁸⁹ COM(2013) 814 p. 3. See also SWD(2013) 474 p. 22.

should be applied differently from the established ECJ case law. The tax purpose test can be regarded, in light of the Merger Directive and other case law, to require predominance of tax purposes which has been proposed also as an interpretation for the wholly artificial arrangements although certain doubt may persist whether the exclusivity of tax purposes could still be required.²⁹⁰ The formulation of the economic reality test may leave uncertainty whether the provision actually sets the Member a more widespread obligation to combat abuse in comparison with the previous case law.²⁹¹ The possible issues raised by this approach can be circumvented by an interpretation that conforms both to the primary law and to the purpose of the PSD since, at the last stage, the ECJ selects the interpretation which fulfills best the aims of the Union, and the vague wording of the provision does not preclude the opportunity to reach this interpretation.²⁹²

It can be, however, asked whether the effectiveness of the PSD would require a broader concept of abuse. First, it seems that the main reasons to enact the new provision were the variance of anti-abuse practices in different Member States and the lack of clarity for the taxpayers which were to be remedied by a common, minimum standard.²⁹³ Effective application of the provision appears to require its application in all Member States and the prevention of abuse. The purpose of the PSD is mainly compromised if the benefits accrue to such companies that are not entitled to them. The anti-abuse provision creates, however, additional burden to EU companies and, therefore, restricts the effectiveness of the Directive. As a consequence, the purpose of the PSD should rather require the exclusion of such situations only that are clearly not entitled to its benefits so that the common tax system is not rendered void.

In conclusion, the provision can be interpreted to require mainly tax-driven arrangements as well as a high level of artificiality in the light of wholly artificial arrangements, and, if this interpretation is adopted, the provision should not create more severe issues in this respect. It may be, nevertheless, questioned whether this way of vague legislating has been necessary since the Member States have already had the opportunity to combat abusive arrangements within the boundaries of ECJ case. A more restricted provision could have targeted the situations that were deemed to be most harmful without creating the

²⁹⁰ See Vanistendael 2006 p. 195, Pistone 2007 p. 535, and Cerioni 2010 p. 805. See also Jimenez 2012 p. 278 and Weber 2013 p. 256-257. ²⁹¹ See also Brokelind 2015 p. 819 where the same question is raised.

²⁹² See Sørensen 2011a p. 341.

²⁹³ See COM(2013) 804 p. 4-6 and recital 4 of the Directive 2015/121/EU.

uncertainty the new provision creates. The more important consequences caused by the enactment of the provision may actually reside in the other effects of its implementation.

4 Effects of the Provision as a Part of European Direct Tax Legislation

4.1 How the Provision is Applied

4.1.1 What Benefits are Denied and How Double Taxation is Relieved?

First issue to be examined is which benefits the Member States have to deny when applying the anti-abuse provision. The PSD provision requires that, if the conditions for the application of the provision are fulfilled, the Member States, "shall not grant the benefits of this Directive." Here the relevant benefits are the same that can constitute a tax advantage capable of being abused i.e., on the one hand, the Article 4 exemption or credit in the state of the parent company or that of the PE and, on the other, the Article 5 exemption from withholding tax in the state of the subsidiary.²⁹⁴ In addition to their initial denial, it can be assumed that the benefits can be withdrawn also later if the arrangement is characterized as abusive at this stage.

As the provision does not specify which of the benefits need to be withdrawn, it is possible that the Member States should, in the case of abuse, deny both of the mentioned benefits. It has been, however, considered to be disproportionate if both of the benefits were denied at the same time.²⁹⁵ Furthermore, the Commission considered it its statement to the political agreement on the enactment of the anti-abuse provision that the new provision should not affect national participation exemption systems.²⁹⁶ In spite of this statement, which does not manifest itself in the amending Directive, the provision has been regarded to be applicable to both of the benefits.²⁹⁷ This is a reasonable conclusion since otherwise one would expect to find an explicit limit to the application of the provision. The question is, rather, whether the provision requires the simultaneous denial of the benefits.

The plural form of the expression "benefits" could support the view that both of the mentioned benefits should be denied at the same time, and there is nothing in the provision that would expressly prevent this conclusion. The conclusion may be supported, furthermore, since the Commission stated in its memorandum on the PSD that the

²⁹⁴ See Art. 4-5 of the Directive 2011/96/EU.

²⁹⁵ See Allevi - Celesti 2016 p. 78 and Weber 2016 p. 128.

²⁹⁶ Political agreement Brussels 5 Dec. 2014, no. 16435/14 p. 11.

²⁹⁷ See Weber 2016 p. 107-108.

provision could lead to the denial of benefits "including" the withholding tax although not specifying the benefits in question.²⁹⁸ As both benefits are, without doubt, benefits granted by the PSD, it could appear inconsistent if one or another was maintained in the case of abuse. Since there are no precedents to this end in the case law on harmonized direct taxation, the question cannot be given a definite answer although there have been also other opinions that both of the benefits should be denied simultaneously.²⁹⁹

If the provision is seen to require the simultaneous withdrawal of both of the benefits granted by the Directive, which involves necessarily two Member States, different interpretations can lead to problematic situations. For example, the source state could conclude that the arrangement is abusive and levy withholding taxes while the state of the parent company could regard the situations as non-abusive which leads to question how the tax levied in the other country should be taken into account. Interestingly, the Advocate General concluded in *Thin Cap Group* Litigation, although in different context, that the Member State applying the anti-abuse provision should ensure, via double tax convention, that the other state would make a corresponding adjustment.³⁰⁰ Although all of the Member States should be assumed to reach similar conclusions in the harmonized system of the provision, it is easy to foresee that situations comparable to the aforementioned case will surface and which will require, ultimately, the interpretation of the ECJ.³⁰¹ The principle of loyalty, discussed more below, could also influence the discretion of the Member States especially in the cases where the abusive nature of the arrangement seems obvious.³⁰²

What is, furthermore, not considered in the provision is how the Member States should address these distributions, and this is probably left to the discretion of the Member States. Nevertheless, there does not appear to stem any actual obligation to tax the distributions which would be the case, for example, when the Member State in question would not usually levy withholding taxes on outgoing distributions. As a consequence, even if the arrangement was regarded to be abusive, the actual effects of the provision depend on the domestic tax law of the Member State in question. It may be asked, in addition, whether the loss of benefits only leads to non-application of further exemptions or whether it requires the repayment of already exempted taxes. It has been concluded that when

²⁹⁸ See Memo/13/1040 25 Nov 2013 p. 3.

²⁹⁹ See Tavares - Bogenschneider 2015 p. 484 and Debelva - Luts 2015 p. 228.

³⁰⁰ Opinion of the Advocate General 29 June 2006 in *Thin Cap Group Litigation* para. 69.

³⁰¹ See also Vogenauer 2011 p. 549 where this phenomenon is seen as an integral part of EU law.

³⁰² See Evers - de Graaf 2009 p. 297. On the principle, see also Wittock 2014 p. 172-173.

monetary benefits are abused, requiring the repayment of exempted taxes even with retroactive effect could be allowed.³⁰³ In *Halifax*, the Member States were given certain leeway to determine the collection of taxes in such situations within the boundaries of ECJ case law which could lead to repayment of taxes from several years if this case were to apply to direct taxation.³⁰⁴

Nevertheless, the withdrawal of benefits can lead to double taxation of distributions which the PSD explicitly strives to avoid. Without the double taxation relief of the Directive, the distributions can be, at least *prima facie*, subjected to withholding taxes in the source state and to further taxation in the state of the parent company. If this concerns e.g. third-country companies that would not be actually entitled to the benefits, the double taxation may not be that problematic from the perspective of the Directive. The withdrawal of the PSD benefits concerns, however, always companies in the EU. The proportionality of this approach has been questioned since the shareholders may face cumulative taxation both in the source state and in the state of residence.³⁰⁵ The problem is exacerbated more if both of the benefits were to be denied simultaneously.

The consequences depend on whether the Member States have to alleviate the double taxation of such distributions that do not come within the scope of the PSD or which have been withdrawn its benefits. In the scope of the corporate tax directives, the Member States cannot relieve the double taxation less advantageously than required by the directives.³⁰⁶In other situations, there have been several cases where the ECJ has concluded that parallel, non-discriminatory exercise of taxing powers does not require that the Member States should remove double taxation arising from this exercise.³⁰⁷ In *Haribo-Salinen* and *Kerckhaert-Morres*, the state of residence of the taxpayer was not obliged to grant credit for the withholding taxes levied in the state of source.³⁰⁸

This does not, however, mean that the Member States could treat distributions that do not come within the ambit of the PSD in a way that contravenes the fundamental freedoms.³⁰⁹

³⁰³ See Vogenauer 2011 p. 542 and C-255/02 *Halifax* para. 95.

³⁰⁴ C-255/02 *Halifax* para. 91.

³⁰⁵ See Debelva - Luts 2015 p. 228.

³⁰⁶ See Helminen 2014 p. 394-395.

³⁰⁷ See, *inter alia*, C-298/05 *Columbus Container Services* para. 51, C-67/08 *Block* para. 31, C-96/08 *CIBA* paras. 27-28, and C-128/08 *Damseaux* para. 27.

³⁰⁸ C-513/04 *Kerckhaert-Morres* para. 24 and joined cases C-436/08 and C-437/08 *Haribo-Salinen* paras. 169-173.

³⁰⁹ See C-374/04 ACT Group Litigation para. 54, C-379/05 Amurta para. 24 and C-48/07Les Vergers du Vieux Tauves para. 46. See also Englisch 2010 p. 201.

If the dividends paid to a company within the same Member State are either exempted or otherwise subjected to preferable treatment and the situations are deemed comparable, levying taxes on outbound dividends may constitute a restriction of the fundamental freedoms.³¹⁰ Equally in the case of inbound dividends, the Member State of residence of the shareholder may not subject the dividends distributed by non-resident companies to more disadvantageous treatment than to which the dividends distributed by resident companies are subjected by not granting same exemptions or options available in the latter cases.³¹¹ It may be asked whether those distributions to which the PSD provision has been applied are in a comparable situation to those distributions that have been made outside the scope of the Directive. It could be argued that these situations do not differ from normal distributions which could require the expansion of preferable domestic treatment. Falling outside the scope of the PSD, this is the manner how these distributions would have been treated in absence of the abusive arrangement, but it is unclear whether these distributions can be deemed to be comparable to the non-abusive situations.³¹²

4.1.2 Can Similar Benefits be Obtained from Other Bases?

The aforementioned considerations lead to question whether the arrangements that have been denied the PSD benefits could gain access to similar benefits on different bases. It is possible that the Member States have either in their domestic tax legislation, as discussed above, or, more relevantly, in tax treaties granted benefits similar to those of the PSD. For example, in *Denkavit* it was required that the source state extended the withholding tax relief in domestic situations to non-residents.³¹³ Nevertheless, the PSD provision does not explicitly require the Member States to deny other benefits in addition to those of the Directive. It has been concluded that this in combination with the Article 7(2) of the PSD, which states that the Directive does not affect other domestic or agreement-based provision that alleviate double taxation, could mean that the Member States are allowed to grant the benefits of other legislation even if the provision was applied.³¹⁴ However, this Article deals with the imputation systems in the Member States which has been seen to mean that it should not have relevance in the situation at hand.³¹⁵

³¹⁰ See, inter alia, C-170/05 Denkavit para. 41 and C-379/05 Amurta para. 61.

³¹¹ See, *inter alia*, C-35/98 *Verkooijen* paras. 35-36, C-315/02 *Lenz* paras. 20-22, and C-446/04 *FII Group Litigation* para. 72.

³¹² See Kofler - Tenore 2010 p. 328-329 on the treatment of distributions outside the scope of the PSD.

³¹³ See C-170/05 *Denkavit* para. 37.

³¹⁴ See Debelva - Luts 2015 p. 231-232.

³¹⁵ See Weber 2016 p. 105. On the Article 7 of the PSD, see Terra - Wattel 2012 p. 641-642.

It is, nevertheless, problematic with view to the effectiveness of the PSD anti-abuse provision if the benefits could be obtained in another way. It has been concluded that the principle of sincere cooperation and the effectiveness of the provision require its application also to tax treaties.³¹⁶ It is, of course, possible that the Member States could deny the benefits of this other legislation by applying domestic or treaty-based anti-abuse provisions which are authorized by the Article 1(4) of the amending Directive 2015/121/EU. If the arrangement was found to be abusive under the PSD provision, the same could happen, equally, when applying other anti-abuse provisions. Another question is whether the Member States are obliged to reach this conclusion based on the principle in the Article 4(3) of the TEU since it is accepted in the ECJ case law that the Member States are not obliged to combat abuse outside the scope of EU legislation as this belongs to the discretion of the Member States.³¹⁷ The question is, essentially, whether the benefits in tax treaties could be considered to be benefits of the PSD and to come, therefore, within the scope of Union law which would require sincere cooperation.³¹⁸

In conclusion, the PSD provision leaves open many questions related to the exact composition of the benefits to be denied and how this should occur. Most importantly, should the provision require the simultaneous withdrawal of all of the benefits in the PSD or should the situations be considered separately, and, in addition, could the arrangements gain access to similar benefits through other bases.

4.1.3 Which Taxpayers are Denied the Benefits?

Since the PSD provision applies specifically to arrangements, it does not define further which parties should lose the benefits when the provision is applied. In the least complex scenario, there would be two companies: a parent company or a PE and a wholly owned subsidiary which could be both subjected to the provision depending on the interpretation whether both of the benefits in the PSD should be denied. It is, however, more complex to assess other scenarios which are equally possible in international groups. It can be, nevertheless, noted that it is the shareholder that is ultimately subjected to the provision since the withholding taxes mentioned in the PSD are taxes on the holders of shares.³¹⁹

³¹⁶ See Weber 2016 p. 104-105.

³¹⁷ See C-417/10 *3M Italia* paras. 32-33. See also Weber 2013 p. 263-264.

³¹⁸ See Allevi - Celesti 2016 p. 79 where this possibility is regarded to exist.

³¹⁹ For the definition of withholding tax, see C-58/01 *Océ Van der Grinten* para. 47, and C-284/06 *Burda* para. 61.

It is, for instance, possible that the subsidiary could have several shareholders which are entitled to the PSD benefits. If one of these relations was considered abusive, could this lead to withdrawal of benefits from all of the shareholders? The issue is not dealt with by the provision since it only requires that the "arrangement" is denied the benefits, and the scope of the arrangement is not, as discussed above, limited to any specific elements. If several shareholders formed part of the arrangement, the benefits could, on the basis of the provision, be withdrawn from all of them. The definition of the arrangement gets more complicated if, for example, it would have been initiated by one shareholder alone or if several parties would have contributed to it at different stages.

It is, however, a well-established part of the anti-abuse doctrine of the ECJ that anti-abuse provisions can lead to the loss of benefits only to the extent there has been abuse.³²⁰ In general, although the companies would form part of the same group, the benefits should, in accordance with the principle of proportionality, be denied only to those companies that can be proved to have participated in the abusive arrangement.³²¹ If one of the shareholders was a non-genuine conduit company, a reasonable conclusion would be to withdraw the benefits only with regard to this company which is supported also by the preamble of the amending Directive which proposes a "to the extent approach." ³²² The extent of withdrawal depends on the fact which companies and shareholdings fall within the scope of the arrangement which may be occasionally complicated to establish.

Further issues may arise in cases beyond the immediate parent-subsidiary relation when several companies in a row have profited from the benefits of the PSD due to the fact that the Directive requires the extension of the credit or the exemption to lower-tier subsidiaries fulfilling the necessary conditions.³²³ If, for instance, one of the companies in this kind of a structure was considered non-genuine, does this imply that only the distributions received by that company or also those made by the company, even to other companies outside the scope of the arrangement, should be denied the PSD benefits? This appears to depend, again, on the scope of the arrangement, and the distributions can be denied the benefits to the extent they originate from non-genuine subsidiaries or are otherwise non-genuine. The complexity of group structures means that it is not difficult envisage also other issues which could surface, but the provision itself does not contain any guidance in this respect.

³²⁰ See C-524/04 Thin Cap Group Litigation para. 83, C-318/10 SIAT para. 52, and C-282/12 Itelcar para. 38.

³²¹ Similarly Weber 2016 p. 112. On the proportionality of anti-abuse rules, see Zalasinski 2007 p. 316-319.

 $^{^{322}}$ See recital 8 of the preamble to the Directive 2015/121/EU.

³²³ See Art. 4(1)b of the Directive 2011/96/EU.

4.1.4 The Obligation to Combat Abuse

One of the most important characteristics of the PSD anti-abuse provision is its obligatory application. Since the Member States, "shall not grant the benefits of this Directive," there appears to arise an obligation to combat abuse in the situations that come within the scope of the new provision. The earlier PSD anti-abuse provision as well as those of other direct tax directives only authorized the usage of national anti-abuse rules.³²⁴

Even earlier, there were comments that the principle of abuse of rights could entail an obligation for the Member States to combat abuse.³²⁵ The ECJ declared, however, in its 3M Italia case that within the field of non-harmonized direct taxation the Member States do not have an obligation to combat abuse.³²⁶ The judgment has been justified by the principle nature of the abuse of rights, which should not in itself limit the rights of the taxpayers, and by the case-by-case evaluation of abuse.³²⁷ There have been, however, opinions that an obligation to combat abuse could arise in such fields of law where the Member States have been subjected to harmonization measures and, as a consequence, have given a part of their sovereignty in combating abuse to the EU.³²⁸ In Halifax, for example, the ECJ required the Member States to redefine the transaction when it was found to be abusive.³²⁹ The PSD anti-abuse provision represents this situation and can be, therefore, seen to create an obligation to refuse the benefits of the Directive in certain situations. Here there is a contrast with the Merger Directive where the ECJ stated in Kofoed that without voluntary implementation of the anti-abuse rule in the Directive, the taxpayers could not be denied the rights on the basis of the provision.³³⁰ This kind of obligation raises, nevertheless, questions. First, how should this obligation be applied in practice? And second, what would be the consequences of non-compliance?

The obligation requires the withdrawal of the benefits from the arrangement when the conditions of the provision are fulfilled. This may, however, not be as simple as it may appear. First, the PSD provision, as established above, contains an amount of uncertainty on its application. The conditions to be fulfilled are relatively vague and leave much discretion to the Member States. As a consequence, it is, in general, quite hard to indicate

³²⁴ See Art. 5 of Directive 2003/49/EC, Art. 15 of Directive 2009/133/EC, and Art. 1(2) of Directive 2011/96/EU.

³²⁵ See Sørensen 2006 p. 440.

³²⁶ See C-417/10 *3M Italia* para. 32.

³²⁷ See Zalasinski 2012 p. 453.

³²⁸ See Weber 2013 p. 263. See also Weber 2005 p. 173 and de Broe 2008 p. 833.

³²⁹ C-255/02 *Halifax* para. 94. See also Lang 2011 p. 453.

³³⁰ C-321/05 Kofoed paras. 42-45.

in which situations the obligation to apply the provision should actually materialize. Does this obligation mean that the Member States should control all possibly abusive situations in order to determine whether the conditions have been fulfilled? This kind of comprehensive control of abusive practices has been seen, rightfully, as impractical since abuse may be hard to detect and is usually found only afterwards.³³¹ Furthermore, this could raise issues with regard to the principle of proportionality since the ECJ has regarded as disproportionate such general anti-abuse rules that are not applied on a case-by-case basis which would be the case if all arrangements would be initially subjected to control.³³²

Most of all, the Member States cannot anymore decide freely whether the abuse of PSD benefits should combated but they are, instead, obliged to do this. The aim of this obligation was, in the words of the Commission, to ensure a common standard in the application of the anti-abuse provision and to prevent directive-shopping through lessstringent legislation in some Member States.³³³ The problem is, as evoked above, the fact that PSD arrangements involve several countries which could reach different conclusions on the abusiveness of the arrangement. On the one hand, some Member States could apply the PSD provision more broadly and deny the access to the benefits of the Directive for a wider range of arrangements while other Member States could be more lenient in this respect. If the Member States were to qualify an arrangement differently, which decision should prevail? Should a Member State be obliged to apply the provision if the other Member State had applied it? In this matter there have been different opinions while some have seen this to belong essentially to the decentralized nature of EU law, whereas others have considered that the Member States should adopt uniform conclusions.³³⁴ It has been concluded that the Member States should at least investigate the existence of abusive arrangements when so requested by other Member States.³³⁵ The question depends, equally, on the issue whether the benefits should be denied in the both countries or only in one of them since the latter conclusion would not lead to these problems.

The Article 4(3) TEU on Member State loyalty could, however, have relevance in this respect since it requires the Member States to take relevant measures in order to achieve the aims of the Union legislation and not to initiate measures that may be detrimental to

³³¹ See Zalasinski 2012 p. 453 where the obligation is considered to require a case-by-case analysis.

³³² See C-28/95 *Leur-Bloem* para. 44 and Zalasinski 2007 p. 316.

³³³ See SWD(2013) 474 p. 23 and COM(2013) 814 p. 4-5.

 ³³⁴ See Vogenauer 2011 p. 549 and, to the contrary, Evers - de Graaf 2009 p. 297.
 ³³⁵ See Sørensen 2015 p. 114 where it is also considered that the obligation should be more closely defined.

these aims. In tax matters, this means that the Member States must not undermine the Union legislation by national decisions.³³⁶ With regard to the directives, the ECJ required already early that the Member States should implement all necessary measures in order to comply with the directives.³³⁷ In such situations where abuse would appear to be evident, such as wholly artificial arrangements, the other Member State could most probably be obliged to apply the anti-abuse provision if abuse had been established in another Member State since this could be required to achieve the aims of the Directive in the light of the Article 4(3) TEU. Nevertheless, in the large group of more uncertain situations and especially before the ECJ has given any guidance on the interpretation of the anti-abuse provision, this obligation may be somewhat harder to verify. What is more, in some situations the principle of loyalty could be actually seen to require the Member States to refrain from characterizing the arrangement as abusive if the conditions would not clearly have been fulfilled.

The question on the consequences of non-compliance regarding the obligation to combat abuse may have, nevertheless, immediate relevance for the application of the provision. If a Member State does not comply with its European obligations, the Commission may bring the matter before the ECJ. According to the Articles 258-260 TFEU, the Court may impose a payment on the Member States that do not comply with their Treaty obligations. It has been stated, however, that the ECJ has not so far subjected Member States to such penalties in tax matters.³³⁸ It is equally possible that a Member State would be judged to pay compensation for private taxpayers if its actions breach the rights of the taxpayer and fulfill the conditions created by the ECJ for such compensation.³³⁹ This would entail repayment of illegally levied taxes.³⁴⁰ As a consequence, the Member States are in a somewhat challenging situation at least until further guidance has been given on the interpretation of the PSD provision. On the one hand, they must apply the provision to combat abuse, but if they were to apply the provision too broadly, these actions could be deemed to be not in accordance with the EU law. On the other hand, if they were to combat abuse too leniently, the Member States could risk the possibility of infringement procedures.

³³⁶ On the principle, see Wittock 2014 p. 174.

³³⁷ C-14/83 Von Colson para. 26. See also C-62/00 Marks & Spencer para. 24.

³³⁸ See Terra - Wattel 2012 p. 157.

³³⁹ On the Union loyalty and liability, see Wittock 2014 p. 182-183.

³⁴⁰ See van Thiel 2009 p. 306-307.

4.2 National Implementation of the Anti-Abuse Provision

4.2.1 The Way of Implementation

The PSD anti-abuse provision creates, in the words of the amending Directive, a minimum anti-abuse rule.³⁴¹ Article 288 TFEU stipulates that the directives are binding only with regard to their objectives but the Member States are free to choose the form of implementation. It should be noted that the Article 115 TFEU, which is used to enact legislation within the Direct tax area, makes possible only the approximation of national laws, not complete harmonization. If the legislation was to be completely harmonized, the Member States implementation measures would be tested only against the directive while in other situations the Member State legislation is examined in the light of both primary and secondary law.³⁴² It should be examined, first, how the Member States should implement the provision and, second, what is their discretion to adopt different solutions.

First, the ECJ stated already in an early phase that the directives in general cannot create obligations to individuals if they have not been properly transposed into national legislation.³⁴³ Furthermore, given the fact that anti-abuse provisions instead of granting rights to individuals aim to deny certain rights, the anti-abuse provisions in the direct tax directives, as established in *Kofoed*, do not have direct effect which would allow the Member States to apply them without national implementation.³⁴⁴ What leaves, however, considerable latitude to the Member States is that they are free to decide on the way of implementation. This implies that all the Member States are not necessarily required to actually enact new legislation or legislate with the same expressions if their national legislation already fulfills the legislative purpose of the directive and enables the taxpayers to find the extent of their rights and obligations.³⁴⁵ Whatever the form of legislation would be, it should be interpreted in the light of the purpose of the directive and, more generally, according to the European legal order in general.³⁴⁶

It may be, therefore, considered how the PSD provision should be enacted in the national legislation. The provision itself is quite broadly and vaguely formulated which means that in some cases the national anti-abuse provisions as such could already constitute sufficient

³⁴¹ See Recital 5 of the preamble to the Directive 2015/121/EU.

³⁴² See Syrpis 2015 p. 464.

³⁴³ See, inter alia, C-14/86 Pretore di Salò paras. 19-20 and C-80/86 Kolpinghuis Nijmegen paras. 9-10.

³⁴⁴ See C-321/05 *Kofoed* para.42 and Zalasinski 2007a p. 573-574.

³⁴⁵ See C-456/03 *Commission v Italy* para. 51, C-428/04 *Commission v Austria* para. 99, and C-321/05 *Kofoed* paras. 43-44.

³⁴⁶ C-14/83 Von Colson para. 26, C-80/86 Kolpinghuis Nijmegen para. 14, and C-138/07 Cobelfret para. 55.

implementation. On the other hand, this may constitute a problem since the Member States cannot be completely certain which level of abuse the provisions actually requires and whether it marks a departure from the previous doctrine of the ECJ. It has been concluded that the Member States should, in order to guard the effectiveness of the provision, take it as a part of the national legislation.³⁴⁷ This conclusion could be supported by the fact that the provision strives to improve consistency of Member State anti-abuse measures which could be jeopardized if the Member State legislation would not have a similar content.³⁴⁸ The most essential part of the provision, the obligation to prevent abuse, should in any case be expressed in the national legislation.

Of further relevance are the opportunities that the Member States have in enacting different provisions which is explicitly allowed by the Directive. In cases of minimum harmonization, the Member States have the competence to enact stricter provisions within the boundaries of the Treaties.³⁴⁹ Since the PSD provision forms the minimum level which the Member States have to implement in any case, they cannot apply more lenient provisions, but more stringent provisions should be, at least prima facie, possible. All Member State rules implementing the Directive should, nevertheless, respect the principle of proportionality and the limits created by the fundamental freedoms.³⁵⁰ There have been different opinions on how far the Member States could actually go in creating different solutions. On the one hand, it has been considered that such provision are possible, but they could possibly lead to infringement of fundamental freedoms.³⁵¹ On the other hand, it has been seen that fundamental freedoms could prevent the application of any more stringent anti-abuse provisions.³⁵² It has been even concluded that the provision leads to full harmonization which prevents all exercise of Member State discretion.³⁵³

The question is, therefore, how the Member States could actually depart from the standard created in the PSD provision. First, it could be possible to apply the provision to a larger number of benefits than that come within the scope of the PSD. This should not, however, pose any serious complications since these cases would most likely concern either national law or tax treaties where combating abuse as such remain at the discretion of the Member

³⁴⁷ See Weber 2016 p. 104.

 $^{^{348}}$ See recitals 4-5 of the preamble to the Directive 2015/121/EU.

³⁴⁹ See Dougan 2000 p. 855.

³⁵⁰ See C-28/95 *Leur-Bloem* para. 48 and Kofler - Tenore 2010 p. 312-313. See also C-168/01 *Bosal Holding* para. 26. ³⁵¹ See Debelva - Luts 2015 p. 231.

³⁵² See Tavares - Bogenschneider 2015 p. 486, 494.

³⁵³ See van den Hurk 2014 p. 494.

States. In these cases, the question would be more of an issue of domestic law which should, should a relevant link exist, conform to the ECJ case law. More issues arise if the Member States enacted a provision that would use a lower limit to establish the abusive nature of the arrangement. If the provision itself was interpreted to involve a broader standard than the one that has been present in the ECJ case law, it would be more than difficult to argue that an even broader provision could be proportionate. Regarding the situation where the provision is interpreted in the light of the established ECJ doctrine, wider application would face the limits of the fundamental freedoms, and it is doubtful whether even this kind of deviation from the ECJ case law would be accepted if the Court does not change its doctrine. In conclusion, the possibility to enact stricter provision may be rather limited although explicitly allowed. The Member States may, of course, continue to apply stricter anti-abuse rules to other benefits outside the scope of the PSD. Given these considerations, concrete Member State implementing measures should be examined.

4.2.2 Legislative Choices in the Member States

The examination is commenced in Finland where the PSD provision was implemented in the new paragraph 6a § of the Business Income Tax Act (Laki elinkeinotulon verottamisesta) which is in all relevant aspects identical to the provision enacted by the Council.³⁵⁴ The way of implementation was decided by consistency with the proposed provision, and although the Finnish tax legislation contains already a common anti-abuse provision, the provision was considered to be justified.³⁵⁵ It is interesting to note that since the 6a § concerns not only distributions within the scope of the PSD but also such distributions, the exception created by the anti-abuse provision encompasses a wider range of distributions than required by the provision. In specialist opinions, it was feared that the provision could be applied randomly, given its unclear wording, and that it was too broad and should be applied according to the sole purpose or predominant purpose test used elsewhere in the domestic legislation.³⁵⁶ The Finance Committee responded by underlining the application of the provision in the light of the purpose of the Directive and the possibility to apply the provision only to a part of the arrangement.³⁵⁷

³⁵⁴ See EV/81/2015 and HE 59/2015.

³⁵⁵ See VaVM 13/2015 p. 4-6.

³⁵⁶ See opinion of the Confederation of Finnish Industries 12 Nov 2015 p. 2-3 and opinion of the Federation of Finnish Enterprises 12 Nov 2015.

³⁵⁷ See VaVM 13/2015 p. 5-6.

In Sweden, on the contrary, the anti-abuse provision was enacted by relatively restricted modifications of the national legislation. The legislation in force contained a common antiabuse rule, which was considered to cover the inbound situations in a way comparable to the PSD provision, although the scope of the national rule was wider which was, however, considered to be allowed by the new provision.³⁵⁸ With regard to the outbound distributions, the law in question (Kupongskattelag), which contains a further anti-abuse provision, was not considered to fully cover these distributions, and the national provision was regarded to contain some issues with regard to its applicability in the PSD situations.³⁵⁹ The legislation was, therefore, changed only with regard to the latter rule whose scope of application was clarified to encompass also the relevant abusive situations, but no new anti-abuse clause was actually implemented.³⁶⁰ Initially, there was an intention to widen the scope of the general anti-avoidance rule, but the proposition was changed after widespread criticism.³⁶¹There were, furthermore, concerns that the PSD provision was not in accordance with the principle of subsidiarity.³⁶²

In the Netherlands, the PSD provision was implemented in Article 17 of the Wet op de vennootschapsbelasting and in the Article 1 of the Wet op de dividenbelasting.³⁶³ The implemented provisions correspond with certain modifications to the wording of the amending Directive. Interestingly, the legislator discussed the amount of required substance which could constitute valid commercial reasons, and the fact that a company did not in itself have commercial activities was not found to constitute a non-genuine arrangement if the company functioned as a link within a group.³⁶⁴ The approach chosen was a worldwide approach which is applied equally to EU as well as to non-EU companies.³⁶⁵ The possible broader scope of application of the new provision in comparison with the ECJ case law was questioned although the government noted the opinion of the Commission where the provision was considered to be in line with the primary law and that the change in wording should not lead to a change in the national practice.³⁶⁶

³⁵⁸ See Prop. 2015/16:14 p. 29-32.

 ³⁵⁹ See Prop. 2015/16:14 p. 33-35.
 ³⁶⁰ See Prop. 2015/16:14 p. 35-43, 52 and 4a§ of Kupongskattelag 1970:624.

³⁶¹ See memo of Finansdepartementet April 2015 p. 4-7 and Prop. 2015/16:14 p. 11.

³⁶² See Melbi 2014 p. 137 and 2013/14 SkU23 p. 6-7.

³⁶³ See Wet implementatie wijzigingen Moeder-dochterrichtlijn 2015 (Wet van 23 december 2015).

³⁶⁴ Memorie van toelichting of the aforementioned law p. 9.

³⁶⁵ Ibid. p. 5.

³⁶⁶ Advies afdeling advisering raad van state en nader rapport p. 4-6.

A similar way of transformation according to the wording of the proposed provision was adopted also in other Member States. In Denmark, the provision was implemented with a similar wording but, remarkably, the scope of application was widened to encompass also the Merger Directive and the Interest Royalty Directive.³⁶⁷ In Portugal, the provision was implemented in a form nearly identical to that of the amending Directive although requiring that the arrangement defeats the purpose of, "elimination of double taxation."³⁶⁸ In France, an identical provision was implemented to replace a former anti-abuse provision applicable in PSD situations.³⁶⁹

Of the six Member States analyzed, five had decided to implement the PSD anti-abuse provision as such or with minor modifications. This may confirm the issues that the open and broad nature of the provision has for diverging domestic rules. When the application of the provision is uncertain, it is more difficult to create different solutions since they could create the risk of breaching the intended objectives of the proposed provision if the domestic rules were not applied similarly and as broadly as was intended. Consequently, the new provision which aims to function as a minimum rule may, as concluded by some commentators, actually turn into a baseline from which the Member States do not dare to depart.³⁷⁰ There seems to exist doubts, whether the provision, as discussed above, departs from the established ECJ case law or whether it should be interpreted according to it. As a consequence, this has an evident effect on legal certainty before the ECJ has ruled on the application of the provision which may take several years. Before that, the Member States will face a severe challenge in trying to find the mode and scope of application that is not only in line with the ECJ case law but also with the objectives of the new provision.

4.3 Application of Other Anti-Abuse Provisions

A further question is how other domestic anti-abuse provisions are affected by the new provision. The Article 1(4) of the provision authorizes the Member States to apply, "domestic or agreement-based provisions required for the prevention of tax evasion, tax fraud or abuse." This is emphasized also in the recitals of the amending Directive where it is stated that: "This Directive should not affect in any way Member States' ability to apply their domestic or agreement-based provisions aimed at preventing tax evasion, tax

³⁶⁷§ 3 of the LOV nr 540 af 29/04/2015.

³⁶⁸ See Decreto N.^o 10/XIII.

³⁶⁹Art. 29 of Loi nº 2015 - 1786 du 29 décembre 2015 de finances rectificative pour 2015. On the old Article, see Picq 2009 p. 472. ³⁷⁰ See also van den Hurk 2014 p. 494 and Tavares - Bogenschneider 2015 p. 494.

fraud or abuse.³⁷¹ This authorization raises two different questions. First, what measures are actually allowed by the provision? And second, how does the existence of the PSD provision affect these measures? The former anti-abuse provision of the PSD contained similar language although only fraud and abuse where stated. It must be assumed that since the new provision deals with the abuse of the Directive, the authorization concerns rules applicable to other situations.

It must be, therefore, considered what is meant with the concepts tax evasion, tax fraud and abuse. First, tax evasion is regarded as an illegal way to avoid taxation by withholding required information.³⁷² Interestingly, the French version of the amending Directive differs by authorizing measures against tax evasion (fraude fiscal) and abuse (abus) without mentioning tax fraud. The tax fraud indicates in some countries a specific form of tax evasion.³⁷³ It has been seen to signify a behavior where, similarly or identically to tax evasion, certain information has been concealed.³⁷⁴ Abuse, in its turn, has been defined as the use of artificial constructions in order to exploit the benefits granted by the tax legislation.³⁷⁵ The word "required" has been seen to implicate in the context of the former PSD anti-abuse provision a higher level of necessity for the existence of these rules.³⁷⁶ Despite the conceptual difficulties, rules preventing tax evasion, which is regarded as criminalized conduct, should not most probably pose problems regarding the PSD provision since the application of these rules and their consequences is based on different premises.

With regard to the rules preventing abuse, the authorized measures could either coincide with the new provision or cover different situations. Given the way of minimum harmonization and obligatory application, the Member States must, however, apply in the scope of the PSD a provision that is at least as strict as the proposed provision.³⁷⁷ If the Member States have applied other national provisions to combat abuse of the PSD, they are, effectively, displaced by the new provision to the extent they do not comply to the standard of the provision.³⁷⁸ On the other hand, any stricter anti-abuse provisions face the restrictive effect of the fundamental freedoms, and the implementation of the PSD

³⁷¹ See recital 9 to the preamble of the Directive 2015/121/EU.

³⁷² See Zalasinski 2008 p. 159.

³⁷³ See Merks 2006 p. 273.

³⁷⁴ See Piantavigna 2011 p. 136.

³⁷⁵ See Zalasinski 2008 p. 159-160.

³⁷⁶ See de Broe 2008 p. 999-1000.

³⁷⁷ On minimum harmonization, see Dougan 2000 p. 855.

³⁷⁸ Effects of the EU law, see Weber 2009 p. 56-60.

provision may leave, as discussed above, little space to create different domestic rules within its scope. This can, actually, lead in the case of some Member States to an obligation to lower the standards of the former anti-abuse provisions, when applied to the PSD benefits, if they do not represent a similar level of evaluation.³⁷⁹ More dramatic effects could arise if the new provision is seen to require the denial of benefits arising also from other bases.

In the case of other national provisions, the effects are depended on the scope of the provisions in question. If they apply only to situations where the PSD does not apply, for instance to purely domestic situations, the new provision may not produce any apparent consequences. Possible interference could arise in such circumstances where the abusive arrangements contain several, relevant steps to which multiple anti-abuse rules could be applicable. There could be, for example, a domestic restructuration which was conducted in order to attain abusively a tax advantage and which was followed by abuse of the PSD benefits. If there is no overlap between the benefits of these national provisions applicable to the restructuration and those of the PSD, the new provision should not affect the application of different anti-abuse provisions to the restructuration itself. Of great relevance is, nevertheless, the question whether the PSD provision with the principle of loyalty could require the denial of equivalent benefits which could in certain situations lead to the displacement of national anti-abuse rules also outside the scope of the PSD.

Furthermore, it is possible that the new provision would affect the application of other supranational anti-abuse rules. The first group is, evidently, other European anti-abuse rules in the tax directives but they should not, due to their different scope, coincide with the application of the PSD anti-abuse provision. Regarding the other provisions of the PSD itself which can be used to prevent abusive situations, such as the Article 3(2) minimum holding period, the ECJ has considered that the general anti-abuse provision cannot be applied when the situation falls within the scope of such special provisions.³⁸⁰ The same applies most probably to the new anti-hybrid rule.³⁸¹ Although the rule leads to some extent to the same results as the general anti-abuse provision by requiring the taxation of distributed profits in the state of the parent company, it is applied differently and it does not require that there is actually abuse but only the existence of a deduction in the state of

³⁷⁹ See van den Hurk 2014 p. 494.

³⁸⁰ See joined cases C-283/94, C-291/94 and C-292/94 *Denkavit-VITIC-Voormeer* para. 31.

³⁸¹ See Directive 2014/86/EU.

the subsidiary which does not, most probably, form a relevant element in assessing the abuse on the basis of the general anti-abuse provision. More interesting situations can arise with regard to a similarly worded general anti-abuse rule proposed by the Commission as a part of a new directive against tax avoidance in the EU.³⁸²

In conclusion, the Member States are even after the implementation of the new anti-abuse provision allowed to apply other domestic provisions that are used to combat different kind of abuse. If these rules apply also to the benefits of the PSD, their application is excluded unless they comply with the standard of the provision. In the cases where multiple anti-abuse rules could be applied to deny the same benefits, it is most probably of no relevance which of them is actually applied as long as the abuse is denied based on the, arguably broad, conditions of the PSD provision.

4.4 The PSD Anti-Abuse Provision and the EU Primary Law

4.4.1 Does the Provision Create a Restriction on the Fundamental Freedoms?

Being secondary legislation, the PSD must be applied according to the primary law of the Union.³⁸³ Here, at least two distinct issues can be detected. First, the PSD anti-abuse provision could in itself be considered not to be in accordance with the primary law.³⁸⁴ Second, the application of the domestic legislation enacted on the basis of the provision can be constrained by the fundamental freedoms especially in such cases where the national legislation is more restrictive than the Directive.³⁸⁵ In the first case, the whole provision could be considered to breach the primary law of the EU and be found invalid according to the Article 263 TFEU. In the second case, the question is whether the fundamental freedoms could be restricted by the application of the provision. The question arises both with regard to the application of the provision in its proposed form as well as in situations where the Member States have departed from it.

First, it can be considered how the fundamental freedoms can be breached. The case at hand does not deal with a traditional discriminatory tax measure enacted by the Member States but with harmonized legislation with an explicit obligation to combat abuse, but this remains, like all EU measures, under the scope of the Treaty prohibition of

³⁸² See Art. 7 of COM(2016) 26.

³⁸³ See C-138/07 *Cobelfret* para. 55 and Szudoczky 2010 p. 191-193.

³⁸⁴ See Debelva - Luts 2015 p. 228-229 and Brokelind 2015 p. 824.

³⁸⁵ See Tavares - Bogenschneider 2015 p. 486, 492, 494.

discrimination.³⁸⁶ Directives that do not respect this can be examined against the fundamental freedoms.³⁸⁷ The TFEU prohibits differential treatment in situations which can be considered to be comparable.³⁸⁸ Discrimination can be either direct, when it is based on nationality, or indirect, when it is based on other factors but in reality has effects on the nationals of other Member States.³⁸⁹ The ECJ has, furthermore, both in tax and non-tax cases created the notion of restriction i.e., if the national measure forms an obstacle to the exercise of the freedom of movement, although not directly making difference between nationals of different Member States, the measure is considered to be against the EU primary law.³⁹⁰ The Court has, however, turned later back to a more discrimination-based approach even though certain inconsistencies remain in this doctrine.³⁹¹

Second, it has to be considered whether the PSD provision either discriminates or is nondiscriminatory. The comparison between the nationals of one Member State and nonresidents is an essential step in establishing whether there is discrimination.³⁹² The ECJ has found PEs to be comparable to the companies of the same Member State.³⁹³ The same has been found in relation to such distributions by resident companies to non-resident shareholders which are subjected to taxation in the state of source.³⁹⁴ Equally regarding double taxation relief on inbound dividends, these dividends have been found to be comparable to dividends paid by resident companies.³⁹⁵ In the case at hand, the distributions under the PSD appear, therefore, to be comparable to domestic distributions between subsidiaries and parent companies.

The ECJ has found a restriction in several cases with regard to such Member State antiabuse provisions which are applied essentially to cross-border situations.³⁹⁶ The Court has found even such provisions, comparable to the PSD provision, which do not automatically

³⁸⁶ See Mortelmans 2002 p. 1317-1318 on the relation between secondary and primary law.

³⁸⁷ See Kofler - Tenore 2010 p. 315-316 and opinion of the Advocate General 24 Sep 2002 in *Bosal Holding* para. 58.

³⁸⁸ On the concept of discrimination, see Zalasinski 2009 p. 283-284.

³⁸⁹ On the definitions, see Dahlberg 2005 p. 93-94.

³⁹⁰ See C-55/94 Gebhard para. 37, C-324/00 Lankhorst-Hohorst para. 32, and C-371/10 National Grid Indus para. 36. See also Vanistendael 2003 p. 137.

See Kingston 2007 p. 1335-1336. See also Wattel 2015 p. 542-543.

³⁹² See Dahlberg 2005 p. 100.

³⁹³ See C-311/97 Royal Bank of Scotland para. 29.

³⁹⁴ See e.g. C-374/04 ACT Group Litigation para. 68, C-170/05 Denkavit para. 35, and C-379/05 Amurta para.

³⁹⁵ See C-315/02 *Lenz* para. 32 and C-319/02 *Manninen* para. 36.

³⁹⁶ See, inter alia, C-324/00 Lankhorst -Hohorst para. 32, C-436/00 X and Y para. 45, C-196/04 Cadbury Schweppes para. 46, and C-105/07 Lammers & Van Cleeff para. 23.

prevent certain transactions but which create this possibility to be restrictive.³⁹⁷ The PSD provision creates a risk of exclusion which targets solely cross-border situations and which may prevent companies in Member States from establishing or investing in other Member States. The restriction appears in two relations. First, between a parent company that has subsidiaries or PEs abroad and a one that has not and, second, between a subsidiary or a PE having international parents and on that has its parent company in the same country.³⁹⁸ The restriction can affect the freedom of establishment or the free movement of capital depending on the exact scope of the shareholding.³⁹⁹ Regarding the latter, the scope of the freedom may rise the issue also in third-country situations although there may be more discretion in this respect.⁴⁰⁰ Even the existence of rules applicable to domestic situations may not change the conclusion since the ECJ has also found such rules that apply without distinction to both domestic and cross-border situations to be restrictive.⁴⁰¹

It some situations, however, the rules may be reasonably applicable only to cross-border situations since similar domestic situations do not exist.⁴⁰² The PSD provision denies access to benefits that are only required to be available in cross-border distributions. The Directive's function is, essentially, to reinforce the fundamental freedoms, and it goes further in its relief of cross-border double taxation than the freedoms go which means that the distributions outside its scope are not discriminated since they benefit from the fundamental freedoms.⁴⁰³ This could allow to argue that the restrictions of the Directive cannot be compared with domestic situations. Nevertheless, the PSD is, alongside the other direct tax directives, the primary way to alleviate double taxation within the Union and with the aim to make cross-border situations comparable to domestic ones.⁴⁰⁴ Many domestic situations may benefit from similar double taxation relief, and there does not appear to arise reasons why the situations could not be considered to be comparable. It is, furthermore, possible to find a restriction if the provision is applied so broadly that it restricts the fundamental freedoms more than the ECJ has considered acceptable.

³⁹⁷ C-524/04 *Thin Cap Group Litigation* para. 62 and C-311/08 *SGI* para. 50.

³⁹⁸ As examples of such restrictions on subsidiaries, see C-264/96 ICI para. 21, C-446/03 Marks & Spencer para. 31, and C-374/04 ACT Group Litigation para. 43. For restrictions on PEs, see e.g. C-311/97 Royal Bank *of Scotland* para. 30 and C-141/99 *AMID* paras. 29-31. ³⁹⁹ On this demarcation within the field of dividend taxation, see Englisch 2010 p. 199-201.

⁴⁰⁰ See, e.g., Weber 2013a p. 320 where the Member States are seen to have more leeway in third country situations.

⁴⁰¹ See Weber 2005 p. 94-97 and Terra - Wattel 2012 p. 54, 92.

⁴⁰² See Wattel 2015 p. 553 where one of the examples given are the thin capitalization rules.

⁴⁰³ See Szudoczky 2010 p. 216, 220-221. See also C-247/08 *Gaz de France* paras. 47, 59.

⁴⁰⁴ See Helminen 2014 p. 394. See also recital 6 of the preamble to the Directive 2011/96/EU.

It is, nevertheless, important to consider whether the existence of the anti-abuse provision itself is the source of issues. The measures enacted by the EU can be justified on same conditions as the Member State measures but the Union has, to some extent, even more discretion in this respect.⁴⁰⁵ In *Gebhard*, the Court required that national measures had to be non-discriminatory, justified, suitable to attain their aim, and proportional.⁴⁰⁶ All the direct tax directives have already had, although non-obligatory, anti-abuse clauses, and the ECJ has not, at least to the date, found them in itself to lead to restriction of the freedom of movement even though the national legislation implementing these clauses has been occasionally found to be restrictive.⁴⁰⁷ Combating tax abuse has been accepted by the ECJ as a legitimate reason to restrict the fundamental freedoms although it is subjected to several conditions.⁴⁰⁸ Therefore, the Court has accepted that the application of anti-abuse clauses in a directive as such does not constitute an unjustifiable breach of the fundamental freedoms or discrimination although they are, inherently, applied only to cross-border situations. Taken this together, it appears that, regarding the PSD provision, the restriction of the fundamental freedoms is tied to the suitability and proportionality of the provision and not to its application as such.⁴⁰⁹

It is here where the issues of the new provision can surface. As discussed above, the wording of the provision, which requires that one of main purposes of the arrangement is a tax advantage as well as the lack of reference to wholly artificial arrangements, may lead to conclusion that the level of required artificiality is lower than required by the ECJ in its consistent case law. The Court has in many occasions and consistently required that the anti-abuse rules must counter only wholly artificial arrangements.⁴¹⁰ Although with regard to the Merger Directive the Court has not explicitly required this, it is most probably caused by the different formulation of the respective provision, and even here the ECJ has made reference to solely abusive transactions.⁴¹¹ If the PSD provision is applied according to its wording, it can lead to exclusion of such arrangement which have not been considered to be abusive by the ECJ and which have some relevant commercial content and, consequently, lead to restriction of the freedom of movement. The provision could

⁴⁰⁵ See Sørensen 2011a p. 355-356.

⁴⁰⁶ See C-55/94 *Gebhard* para. 37. See also Dahlberg 2005 p. 117-118.

⁴⁰⁷ See C-28/95 *Leur-Bloem* paras. 44-45 and C-352/08 *Zwijnenburg* paras. 54-56.

⁴⁰⁸ See e.g. C-196/04 *Cadbury Schweppes* para. 51 and C-524/04 *Thin Cap Group Litigation* para. 72.

⁴⁰⁹ For other cases, see e.g. C-28/95 *Leur-Bloem* para. 44, C-318/10 *SIAT* para. 59, and C-282/12 *Itelcar* para. 40.

⁴¹⁰ See, *inter alia*, C-264/96 *ICI* para. 26, C-9/02 *De Laysterie du Saillant* para. 50, C-196/04 *Cadbury Schweppes* para. 55, and C-282/12 *Itelcar* para. 34.

⁴¹¹ See C-321/05 Kofoed para. 38 and C-126/10 Foggia para. 50.

make it less advantageous to group companies within the EU if the groups in question could be considered as abusive in the context of the PSD even if this was not the case outside the scope of the Directive.

Nonetheless, this effect is created only if the provision is actually interpreted more broadly both by the Member States and by the ECJ. The provision is vaguely worded, and the lack of further guidance does not allow to make definite conclusions on its application. Given the possible broad implications of the provision on the effectiveness of the PSD, it should be, as discussed above, interpreted in accordance with the Directive and the ECJ case law as a whole. This is the way in which the Court consistently avoids apparent collisions of secondary and primary law.⁴¹² A similar subjective test has been approved as such in the case of the Merger Directive, and the economic reality test, although not mentioning wholly artificial arrangements, can be interpreted to require a high level of artificiality which is defended both by practical considerations and the consistent ECJ case law. Even the Commission emphasized the compatibility of the provision with the Court's doctrine. It is, therefore, more than possible that the ECJ could interpret also the new provision in the light of its previous case law which would remove the apparent risk of restriction on the freedom of movement. Since the provision does not include any definite rules that would exclude certain situations outright, interpreting the provision in conformance with the ECJ case law should not be manifestly impossible.

4.4.2 Is the Provision Consistent with the Principle of Subsidiarity?

Nevertheless, there is a chance that the PSD provision could raise problems with regard to the principle of subsidiarity since in such areas where the EU does not have exclusive competence, its actions may not go further than necessary, and they can go only so far as some aim is better achieved at the level of the Union.⁴¹³ According to Articles 263-264 TFEU, the ECJ has a possibility to declare secondary legislation void if the legislation infringes the Treaties or procedural requirements in its implementation.⁴¹⁴ In general, the ECJ does not easily find grounds to declare secondary legislation void, but it rather arrives to a Treaty-conformant interpretation and, furthermore, the Union has a somewhat broader discretion to enact restrictive measures in comparison with the Member States.⁴¹⁵

⁴¹² See Sørensen 2011a p. 341-344. From cases e.g. C-22/08 and C-23/03 Vatsouras-Koupatantze para. 44.

⁴¹³ See Zalasinski 2014 p. 309-310 and the Art. 5 of TEU.

⁴¹⁴ As an example of non-tax cases where such conclusion was reached, see C-376/98 *Tobacco Advertising*.

⁴¹⁵ See Sørensen 2011a p. 344-347 and Syrpis 2015 p. 468. See also Mortelmans 2002 p. 1332-1334.

As direct taxation has not been mentioned in the Treaties, the complete harmonization of tax rules cannot be achieved within the competences conferred to the Union.⁴¹⁶ For example in Sweden, there were comments that the PSD provision would go further than necessary with regard to the principle of subsidiarity since anti-abuse rules are best enacted nationally and adapted to national conditions.⁴¹⁷ The Commission, on the contrary, considered the provision to be necessary exactly because the national anti-abuse rules contained such variance that allegedly made individual actions by the Member States ineffective.⁴¹⁸ The question revolves around the limits on harmonization by the Article 115 TFEU, and it appears that the biggest issue is the obligatory, minimum-level nature of the new anti-abuse rule.

The Article 115 authorizes such approximation of law which, "directly affect the establishment or functioning of the internal market." This has been considered as a mean to remove either restrictions on the fundamental freedoms or distortions of competition.⁴¹⁹ With regard to the first, the PSD provision seems to rather possibly restrict the fundamental freedoms than to remove such restrictions which is, essentially, the purpose of the PSD. If the application of the provision described, namely, the exploit of legislation in such Member States which do not have anti-abuse provisions. Furthermore, it has been considered that the ECJ could actually interfere with the harmonization measures on the basis of the principle of subsidiarity only in such cases where the breach would be apparent, and that the unanimity requirement would serve as a proof of conformance with the principle.⁴²⁰ Although further discussion is not possible, it appears that there could be grounds to maintain the PSD provision also with regard to the principle of subsidiarity.

4.4.3 Does Application of the Provision in the Member States Create a Restriction?

Such as the PSD provision itself, the Member State implementation legislation can lead to restriction of the fundamental freedoms. The effects of the provision are, in any case, visible essentially when the Member States actually apply it. In situations where the Member States are applying the implemented provision, two issues can surface. If the provision has been enacted identically or close to the proposed provision, it is possible that

⁴¹⁶ See Hrehorovska 2006 p. 163.

⁴¹⁷ See statement 2013/14:SkU23 and Melbi 2014 p. 137.

⁴¹⁸₄₁₀ COM(2013) 814 p. 5-6 and SWD(2013) 474 p. 23.

⁴¹⁹ See Schrauwen 2010 p. 18-20.

⁴²⁰ See Grau - Herrera 2003 p. 31-32.

it is applied more broadly than originally intended. In the second situation, the Member States may have created stricter anti-abuse rules or their national legislation may already contain such rules. In the cases of minimum harmonization such as the PSD provision, the Member States measures are tested both against the directive as well as the primary law.⁴²¹ The ECJ has concluded that the Member States may exercise their options granted by the directives only in accordance with the fundamental freedoms.⁴²² From this it can be clearly seen that any Member State anti-abuse provisions which go further than the proposed provision must be implemented and applied in accordance with the fundamental freedoms.

The first scenario evoked above is related to the unclear interpretation of the PSD provision which is set to persist until the ECJ rules on the issue or the EU issues other guidance. It is possible that the Member States apply the provision more broadly than has been allowed by the ECJ in its case law on national anti-abuse rules and, should the ECJ keeps its standard, the Member States measures could be found to breach the fundamental freedoms. The question in this case is, however, one of the correct interpretation and does not have effects on the implemented legislation as it follows the letter of the amending Directive.

The second scenario involves similar conclusions. As stated above, it is hard to see how the Member States could actually depart from the enacted provision since it itself seems to go further than the ECJ has gone if the provision is not interpreted in a way compatible with the PSD and the ECJ case law. There is, therefore, a real risk that stricter Member State provisions could breach the fundamental freedoms. In such cases, these provision would be replaced by the conformant ECJ interpretation to the extent the provision is not in conformance with the freedoms.⁴²³ It has been considered that the Member States can continue to apply the provisions in those situations where the restriction does not materialize.⁴²⁴ The anti-abuse rules could, therefore, be applied to domestic situations and, if their scope was limited by national courts, to cross-border distributions.

5 Conclusions

In the preceding chapters, the new anti-abuse provision of the PSD has been analyzed with regard to its possible interpretations and its effects as a part of the European direct tax

⁴²¹ See Kofler - Tenore 2010 p. 317.

⁴²² See C-168/01 *Bosal Holding* para. 26 and C-471/04 *Keller Holding* para. 45.

⁴²³ See Weber 2009 p. 56-60. See also C-106/77 Simmenthal para. 24.

⁴²⁴ See Ståhl 2008 p. 550-551 on the effects of national rules conflicting with the EU law.

legislation. The most evident conclusion is uncertainty i.e., how is the provision actually meant to be applied and how will it in practice affect cross-border corporate taxation in the Member States. Although the ECJ has created an ever-broadening field of case law related to direct taxation and defined in several judgments the boundaries of abuse within this area of tax law, it has issued, to date, relatively few judgments concerning the anti-abuse provisions in the direct tax directives. Since the PSD anti-abuse provision is without precedent both with regard to its detailed wording and its obligatory application, it can be expected with certainty that the Court will have to rule on the exact boundaries of the provision in the following years.

The first research question on the interpretation of the provision can lead to different conclusions. Most interestingly, the provision omits any reference to the established "wholly artificial arrangements" concept although it is formulated somewhat similarly in comparison with the Court's definition in the landmark *Cadbury Schweppes* case. If read literally, the wording of the provision can appear to define abuse in the context of the PSD more broadly than has been accepted in the established case law. Whether the Council purposively intended to enact a provision that would give the Member States more latitude in combating abuse or whether it just used a different wording to tell the same the ECJ has done in several occasions, appears somewhat unclear. The provision is, nevertheless, open to various interpretations, and the brief survey of the implementation measures in the Member States appears to confirm the uncertainty on the exact boundaries of the provision.

If the provision is, however, given an interpretation that is based on the ECJ case law and which takes into account the purpose of the PSD and the fundamental freedoms, it can be regarded to require mainly tax-motivated arrangements that reflect high level of artificiality with regard to their content. Whether these arrangements should be characterized as wholly artificial arrangements, depends on the suitability of the main purpose test in this context although the exact level of required tax motivation appears to be one of the most uncertain questions in the ECJ case law on tax abuse. The arrangements may contain certain lesser commercial aims, but these should be secondary to the tax motives. The provisions applies principally to such situations where a company, either in a Member State or, perhaps more relevantly, in a third-country, initiates the arrangement with the purpose of obtaining the benefits of the Directive if it would not be, without the arrangement, entitled to them. This is how the purpose of the Directive is contravened. In

addition to this, the arrangement must have elements that show its lack of economic reality, and this may be, actually, the most important step in the application of the provision. As discussed more extensively above, the substance requirement in *Cadbury Schweppes* may not always function as a reliable indicator of economic reality in international group structures, and this evaluation needs, consequently, also other factors. At any rate, the interpretation of the provision should avoid compromising the effectiveness of the PSD.

With regard to the second research question on the effects of the provision, most significance can be attributed to its compulsory, minimum-nature and the possible conflicts with the national legislation. The Member States are, effectively, precluded from applying other national anti-abuse provisions within the scope of the new provision. This entails, essentially, a displacement of competence from the Member States towards the ECJ. The effect is strengthened if the provision is seen to require the withdrawal of other, similar benefits arising from the tax treaties and other tax legislation which, alongside the exact scope of denial of the benefits of the PSD, depends on the actual interpretation of the provision. Most saliently, from now on the Member States are obliged to combat abuse of tax law in the field of direct taxation, and the way how this obligation is to be fulfilled may contain some friction. It is also questionable whether the Member States have in reality any discretion to enact different national solutions since they, inevitably, risk the breach of the fundamental freedoms which means that the authorization in the provisions to this end may prove to be illusory.

In the end, it can be returned to the two ideas presented in the introduction i.e., does the provision restrict the freedom of movement in the Internal Market, and is it effective in combating abuse? First, the provision is, in itself, liable to create additional burden on cross-border distributions within the scope of the PSD. Whether this restricts fundamental freedoms is a matter of interpretation. If the provision is interpreted according to the established case law, it cannot be necessarily considered to create unjustifiable burden on these freedoms. The Member States have been, after all, authorized to apply such measures even before. Whether the PSD would have actually needed such a provision is, of course, subject to another discussion, and even the interpretation adopted may create uncertainty amongst the taxpayers. More relevant is the possible impact of the provision on the functioning of the PSD itself.

Since the scope of this research does not include an evaluation of the most effective antiabuse measures, the effectiveness of the provision must be seen, essentially, with regard to its objectives i.e., the need to combat abuse in all Member States and consistency of these measures. It may be seen to success in creating an unified system where all the Member States must combat abusive arrangements which means that these arrangements cannot be effected through the Member States with the weakest anti-abuse legislation. Regarding the consistency, the effectiveness of this approach can be questioned. The vagueness of the provision and the lack of guidance mean that the Member States are set to reach varying conclusions before the scope of the provision has been clarified. The uncertainty this creates for the taxpayers and for the tax administrations would have supported a more narrowly-defined provision that could have countered the abusive arrangements deemed most harmful.

In the end, the problems discussed should be kept in mind when new anti-abuse measures are designed in the EU. The PSD provision will function as a test case for a new approach in the field of European tax law. If the experiences proves to be negative or even counter-productive, it may discourage the European legislator from creating similar provisions in the future. On the other hand, the true significance of the PSD provision may become clearer only after several years if the time required by the national processes and the subsequent ECJ deliberation is taken into account. During this time, it would be recommendable that the Commission would publish guidance on the application of the provision.

If the provision is interpreted according to the established case law, it may turn out to be a relatively small amendment that does not radically change the landscape of European tax law. On the other hand, there is a risk that its interpretation creates such uncertainty and issues that will make the Member States, the ultimate decision-makers in the field of taxation, think twice before embarking to harmonize legislation in this manner. The experience will be relevant also when the Member States contemplate whether abuse should be best combated on the level of the EU or nationally. Most of all, it is recommended that any new initiatives with the aim of combating tax abuse should either contain more detailed clarifications or be worded with regard to established case law.