The impact of the CJEU decision ‘Groupe Steria’ in France, the Netherlands, Spain and Italy

On 2 September 2015, the Court of Justice of the European Union (CJEU) ruled in the Groupe Steria case (C-386/14) that the French rules that allow a French parent company a full exemption in respect of dividends received from domestic subsidiaries under a group taxation regime, but effectively tax (up to) 5% of dividends received from shareholdings in EU subsidiaries, are in breach of the freedom of establishment. With this ruling, the CJEU accepted the so called "per-element" approach of a group taxation regime.

As a consequence of this judgment, French parent companies of subsidiaries established in another Member State can claim the repayment of the corporate income tax paid on dividends received from these subsidiaries during 2013 and 2014 fiscal years, which can be evaluated to around 2% of the dividends.

This ruling may also have an impact on regimes in other EU member states, especially countries which have a similar tax consolidation regime. In this tax alert we will analyse the potential impact of this decision on the tax regimes of the Netherlands, Spain and Italy.

France

It is recalled that Article 223 B of the French tax code provides for the neutralisation of the add-back of the proportion of costs and expenses related to the dividends received by a French parent company from a French subsidiary when both companies are members of the same consolidated tax group. The result is a difference of treatment depending on whether the dividends are received from a French subsidiary member of the same consolidated tax group as the parent company or, from a subsidiary established in another Member State which could have been part of this consolidated tax group if it had been established in France. The proportion of costs and expenses is fixed in every case at 5% of the gross dividend.

Following the opinion of the Advocate General, the Court states that it cannot be inferred from the X Holding judgment of February 25th, 2010 (C-337/08) that any difference of treatment between, on the first hand, companies part of a consolidated group and, on the other hand, companies not belonging to such a group is compatible with Article 49 of the TFEU (§ 27). Each tax benefit granted under a tax group regime, other than the transfer of losses within the group, should be considered separately.

In the case of the neutralisation of the add-back of the proportion of costs and expenses, the absence of neutralisation of the partial taxation of costs and expenses related to dividends received by a French company from a subsidiary established in another Member State constitutes a restriction on freedom of establishment which is justified neither by the principle of allocation of the taxation power between the Member States (justification used in the X Holding judgment), nor by the coherence of the tax consolidation regime.

As a consequence of this judgment, French parent companies of subsidiaries established in another Member State can claim the repayment of the corporate income tax paid on dividends received from these subsidiaries during 2013 and 2014 fiscal years, which can be evaluate to around 2% of the dividends.

Furthermore, it is appropriate to consider all the benefits of the French tax consolidation regime with regard to the principle of freedom of establishment (including the exemption from the 3% corporation surtax on dividends which benefits to intra-group dividends).

The Netherlands

The CJEU’s decision may offer opportunities for claiming, in cross-border situations, certain benefits available under the Dutch fiscal unity regime in domestic situations which are not available without a fiscal unity. The Groupe Steria judgement seems to allow for “cherry picking” (per-element approach) of any tax advantage that has been unavailable because of the illegibility to form a cross-border fiscal unity.

Dutch tax law includes rules that allow taxpayers to avoid certain unfavourable tax treatment by entering into a fiscal unity (tax group). As in the case of the French consolidation system, the Dutch fiscal unity regime is limited to Dutch resident companies. Certain disadvantages can therefore only be avoided in domestic situations by the Dutch resident companies entering into a fiscal unity. The Dutch Supreme Court has previously held (in relation to the former thin-capitalisation rules and the loss compensation rules for holding and finance company losses) that the fact that Dutch companies may
avoid the negative implications of tax rules by entering into a fiscal unity did not infringe EU law. The CJEU’s decision may therefore result in change of opinion by the Dutch Supreme Court. The decision seems to indicate that the scope of the CJEU judgment in the X-Holding case seems limited to the element of cross-border loss relief. In practice this means that the denial of any tax advantage because of the ineligibility to form a cross border fiscal unity, can now be examined as to its compatibility with the freedom of establishment.

The Dutch tax advantages limited to a situation in which fiscal unities are formed, mainly concern the following:

- Intra-group transactions
  - Intra-group transactions between companies included in a fiscal unity are ignored for CIT purposes, allowing the entities to transfer assets and liabilities without triggering any taxable capital gain.
- Interest deduction rules (participation interest).
- Possible restrictions on interest deduction regarding the acquisition of participations do not apply if the Dutch subsidiary are included in the fiscal unity after acquisition. These restrictions do apply however if the acquisition concerns a foreign subsidiary which cannot be included in the fiscal unity.
- Loss compensation for holding/finance companies.
- Loss compensation can be restricted if the company is mostly engaged in holding activities and/or intra-group financing activities. Under the fiscal unity regime, such intra-group activities would be ignored, which benefits the loss compensation position.
- Liquidation loss rules.
- The amount of the loss that can be taken into account upon liquidation of a participation differs in the situation that the participation would have been included in a fiscal unity with its parent company.
- A new series of Dutch case law is therefore expected and clients should review whether they can claim certain benefits. The Dutch government will probably react to the Groupe Steria judgement considering the expected impact. The Dutch government has a couple of options in this regard:
  - Canceling the fiscal unity regime
  - Moving to a UK type tax group system
  - Allowing cross border fiscal unities
  - Changing the various rules to bring them into accordance with the Groupe Steria judgement.

At the moment it is not clear which direction the Dutch government will take. On 15 September the 2016 budget and tax plans for 2016 were presented by the government, but these did not include any changes to the fiscal unity regime.

Italy

At first glance, the Groupe Steria case seems not to have an impact on the Italian tax law. Indeed, starting from 2008, dividends received from domestic subsidiaries included in a fiscal unity (i.e. tax consolidation regime) and dividends received from EU subsidiaries are taxed in the same way. Therefore, with regard to dividends, the current Italian law should not be considered in breach of the freedom of establishment.

However, from an in depth analysis of the case, the CJEU seems to embrace a “per element approach” qualifying as a potential violation of the freedom of establishment of any tax advantages reserved only to purely domestic tax consolidation. This may impact, for example, interest deduction rules both for operating and finance companies.

With regard to operating companies, generally, interest expenses are deductible up to 30% of the EBITDA of the company. In case of a domestic tax consolidation group, any interest expenses exceeding 30% of the EBITDA may be used to offset the taxable income of another company within
the tax consolidation, if the 30% EBITDA of such company has not been used to deduct its own passive interests. So far, foreign companies are virtually tax consolidated in order to benefit from such a rule, thus not creating any discrimination among domestic and foreign companies. Starting from 2016, according to the new consolidation tax rules, such benefit is granted only to the members of a domestic tax consolidation while for foreign companies the 30% excess EBITDA is replaced by the dividend distribution. Such different treatment among domestic and foreign companies may lead to a discrimination where the dividend distribution of the foreign company is less advantageous if compared to the 30% EBITDA. It is still unclear if a proper dividend distribution is required by the foreign entity. If this should be the case we believe that a discrimination issue may arise because for interest deduction purposes foreign companies may not have retained earnings.

With regard to finance companies, generally, interest expenses are deductible up to 96% of their amount. In case of a domestic tax consolidation group, intra-consolidation passive interests are fully deductible up to the amount of interest expenses suffered by the members of the fiscal unit towards third parties. Such tax advantage applies only to domestic intra-consolidation passive interests. Therefore, a discrimination issue may arise.

In conclusion, the Groupe Steria case may offer opportunities for claiming, in a cross border scenario, those tax advantages which Italian tax law reserves to the domestic tax consolidation regime.

Spain

Given that only Spanish-resident companies or permanent establishments in Spain of non-resident entities can form part of a Spanish consolidated tax group, the ECJ’s view in the Groupe Steria case could indeed have consequences in Spain. However, to determine its final impact (still uncertain); the following circumstances need to be taken into account:

- Groupe Steria judgement does not allow the inclusion of non-resident (EU) entities in the tax group (nor the transfer of their tax losses), but rather would permit the Spanish entities in the tax group to apply certain advantages arising from tax consolidation which are not available because a given subsidiary does not form part of the tax group (since it is not resident in Spain).

- More than to grant specific “advantages”, the consolidated tax regime in Spain has as its main objective to guarantee the neutrality of intra-group transactions on terms similar to those established in the accounting legislation. Along these lines, the ECJ’s judgment could entail that the results of transactions with EU-resident entities which, had they been resident in Spain, would have formed part of the tax group, should be eliminated from the tax group’s base and, therefore, deferred for tax purposes. In addition, there are certain fiscal limitations or incentives the quantification of which depends on the computation on a tax group basis (e.g. to determine the operating income which acts as a limit on the deduction of financial expenses, or the undistributed income that permits a tax deduction in the so-called “capitalisation reserve”, etc.). Logically, this computation may vary —although not necessarily in a manner favorable to the taxpayer—if the scope of companies affected by the law is expanded to include other EU-resident companies.

- There are other cases in which the existence of a tax group does entail an evident advantage. This is the case, for example, of the exception to the obligation to document the arm’s length valuation of transactions with entities from the tax group, which could be extended to entities which are not from the group but which would be if they were resident in Spain.

- The Spanish legislation adds some further complications, such as the obligation of including in the tax group all of the entities that meet the objective requirements established in the legislation.

In light of the above, and considering that the exclusion of non-resident companies from the tax group is not questioned as such and that, nowadays, there is no difference in Spain in the tax treatment of
dividends received from resident and non-resident subsidiaries (this being the most immediate concern of the Groupe Steria judgment) it would not be surprising that the Spanish legislation is not amended/adapted in the short term. In the meantime, taxpayers should evaluate, on a case by case basis, the possibility of recalculating their final consolidated income/loss in light of the Groupe Steria judgement (are they penalised from a tax consolidation perspective because they hold shares in a non-resident EU entity?), so that the current legislation is interpreted and applied in the manner most consistent with EU law.

The Group Steria case may offer opportunities for tax payers in France, the Netherlands, Spain and Italy to claim the benefits that are only available for group consolidation situations.

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