EU Direct Tax Newsalert

CJEU judgment in Argenta Spaarbank on compatibility of interest payment deduction rules with Parent-Subsidiary Directive

On 26 October 2017, the EU's Court of Justice (CJEU) ruled on the compatibility of the Belgian interest payment deduction rules with the Parent-Subsidiary Directive (PSD) in the case *C-39/16 Argenta Spaarbank vs. Belgische Staat*.

Background

The case concerns the Belgian interest payment deduction rules laid down in Article 198(10) of the 1992 Income Tax Code as it existed before 2002. Under this rule, the deduction of interest payments was disallowed to the extent that in the same tax year the taxpayer had received exempt dividends from shares held for less than one year.

The questions referred to the CJEU were whether these Belgian interest payments deduction rules are compatible with:

- Article 4(2) of the PSD, which determines the deduction of costs relating to holdings in a subsidiary established in another Member State; and
- (Former) Article 1(2) of the PSD, by which Member States may refuse to grant the benefits of the Directive for reasons of preventing tax evasion and abuse.

The CJEU's reasoning

The CJEU pointed out that Article 4(2) of the PSD must be interpreted strictly, and according to settled case-law, cannot be interpreted beyond its actual wording. Therefore, only a literal interpretation of that provision is compatible with the specific objective referred to thereunder - to prevent a parent company from benefiting from a double tax advantage. Article 4(2) of the PSD must therefore necessarily be interpreted as allowing Member States only to prevent a parent company from benefiting from such double tax advantage. Permitting Member States to deny parent companies from deducting interest that is not linked to the acquisition of holdings on which tax-free dividends have been paid out would manifestly go beyond what is necessary to achieve such an objective.

With regard to Article 1(2) of the PSD, the CJEU points out that - as AG Kokott observed in her Opinion – this provision reflects the general EU law principle that abuse of rights is prohibited, and that EU law cannot be relied on for abusive or fraudulent ends.

Contrary to AG Kokott's Opinion, however, the CJEU decided that Article 4(2) of the PSD must be interpreted as precluding a provision of domestic law pursuant to which interest paid by a parent company under a loan is not deductible from the taxable profits of that parent company up to an amount equal to that of the dividends, which already benefit from tax deductibility, that are received from the holdings of that parent company in the capital of its subsidiary companies that have been held for a period of less than one year, even if such interest does not relate to the financing of such holdings.

Furthermore, the CJEU - following AG Kokott - decided that Article 1(2) of the PSD must be interpreted as not authorising Member States to apply a domestic provision to the extent that that provision goes beyond what is necessary for the prevention of fraud and abuse.

Takeaway

Because the CJEU decided that the PSD is applicable in the case at hand precluding the Belgian provision, the judgment can be regarded as further limiting the leeway Member States have in exercising the options available to them under Article 4(2) of the PSD.

This judgment relates to a provision that is no longer in force under the current Belgian tax legislation but clearly has a broader relevance beyond the specific Belgian tax provision reviewed in the judgment.

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