

## 10. EU Corporate Tax Policy and Switzerland - Emerging Limits to EU Fiscal Protectionism

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### Introduction

EU corporate tax policy has recently been very much driven by the desire to implement the OECD/G20 Base Erosion and Profit Shifting project (BEPS) within the internal market. The most comprehensive expression of this initiative crystallized in July 2016 with the adoption of the Anti-Tax Avoidance Directive (ATAD). ATAD, which was adopted after an intense political debate, will require Member States to transpose into their domestic laws, as a general rule by December 31, 2018<sup>1)</sup>, certain measures forming part of the BEPS initiative. At the same time, however, ATAD goes further than the OECD project as it is intended to set a common minimum framework against aggressive tax planning within the European Union. Accordingly, measures which have only led to recommendations and best practices at the OECD level become a mandatory standard under the ATAD<sup>2)</sup>.

This being said, from a policy perspective, ATAD also marks a shift towards a form of fiscal protectionism. A good example of this trend is the so-called “categorical” controlled foreign company rule found in the ATAD, which, on the one hand, will not apply to substantive economic activities within the internal market (so-called “carve-out clause”) but, on the other hand, may be applied by Member States to operations conducted in third countries even if such operations represent genuine business activities. The same trend is also confirmed by the proposals on a Common and Consolidated Corporate Tax Base (CCCTB) which were released by the European Commission on October 25, 2016. As it has been argued, this policy runs counter the core principles of the BEPS project which seeks to establish a level playing field to fight aggressive tax planning<sup>3)</sup>. Further, as regards Switzerland, this approach is also difficult to reconcile with the joint EU-Swiss statement of October 2014 in which it was agreed that anti-avoidance rules should apply only if they are “justified”.

Hopefully, when implementing the categorical CFC rule, some Member States (for example France) will choose to also apply a carve-out for genuine business activities conducted in third countries such as Switzerland. Further, other Member States (typically those that do not currently have a CFC legislation) may opt for the alternative “transactional model” provided by the Directive which applies evenly within and outside the internal market and is limited to: “[t]he non-distributed income of the entity or permanent establishment arising from non-genuine arrangements which have been put in place for the essential purpose of obtaining a tax advantage (Art. 7(2)(b)).”

In this contribution we show, in addition, that the case law of the Court of Justice of the European Union (CJEU), with which Member States have to comply, may well in the future represent a strong and welcome limit to this form of political fiscal protectionism. Two recent examples are provided to support this view. The first example is the judgment of November 24, 2016, delivered by the CJEU in the SECIL case dealing with the application of free movement of capital to third countries<sup>4)</sup>. The second example is the opinion of Advocate General Kokott of January 19, 2017 in the Egiom SAS case (previously Holcim France) concerning a group structure involving Switzerland<sup>5)</sup>.

### EU Free Movement of Capital and Third Countries: The SECIL Case

As it is well known, free movement of capital applies both within the EU and to third countries. Art. 63 of the Treaty on the Functioning of the European Union (TFEU) provides in this respect that: “Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited”. In the landmark SECIL decision, the CJEU, in line with its recent case law, confirmed first of all that, with respect to a third country, free movement of capital becomes applicable as soon as the legislation at issue is not exclusively applicable to controlled group structures<sup>6)</sup>. In the affirmative, a company established in a Member State may therefore rely on free movement of capital “in order to call into question the legality of such legislation, irrespective of the size of its shareholding<sup>7)</sup>”. Secondly, the Court also held that, even in relation to a third country, a rule applying beyond “wholly artificial arrangements which do not reflect economic reality<sup>8)</sup>” may not be justified. In other words, the CJEU made it clear that provisions establishing an un rebuttable presumption of tax evasion are not acceptable even where third countries such as Switzerland are involved<sup>9)</sup>.

Based on this case law, it could, thus, in the future be argued that a European domestic CFC rules designed according to ATAD and applying to third countries such as Switzerland beyond wholly artificial arrangements could possibly be regarded as an unjustified restriction to free movement of capital. This is because the ATAD CFC model potentially applies to cases in which the parent company is merely entitled to receive more than 50 % of the profits of the subsidiary<sup>10)</sup>. In other words, the recent case law of the CJEU could represent a limit to EU fiscal protectionism and dictate, for example in the area of CFC legislation, that the same carve-out for genuine business activities apply within and outside the internal market. Interestingly, in a decision rendered on March 1, 2017, the French Conseil Constitutionnel has gone in this direction holding that a broader application of a CFC regime to third countries was contrary to the principle of equality of treatment<sup>11)</sup>.

### EU Parent- Subsidiary Directive Involving a Group Structure Ultimately Controlled by a Swiss Resident Company

The second example which could ultimately be setting a limit to fiscal protectionism is the Egiom SAS case (previously Holcim France) for which the Advocate General delivered her opinion on January 19, 2017. The case concerns the application of the EU Parent-Subsidiary Directive and the exemption from withholding tax on dividend distributions made by a French subsidiary to a Luxembourg company owned by a company in Cyprus which was in turn controlled by a company with its seat in Switzerland.

At issue in the present case is the application of a provision of the French Tax Code (“Code Général des Impôts”) – Art. 119b(3) CGI – which provides for a reversal of the burden

of proof against the taxpayer where, as is the case in the present instance, a dividend distribution is made to an EU company ultimately controlled by a resident of a third country. In her opinion the Advocate General first of all considered that this provision is not compatible with Art. 1(2) of the EU Parent Subsidiary Directive which provides that: “[t]his Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud or abuse.” The Advocate General rightly noted that this provision requires the application of domestic anti-abuse rules of Member States to remain proportionate in the framework of the Directive. From this perspective, art. 119b (3) CGI is not compatible with the Directive in that it leads to a presumption of abuse in relation to third countries such as Switzerland and it is then up to the taxpayer to provide proof that the chain of interests is not essentially for tax purposes.

This opinion, which is to be approved, stresses first of all that when fighting aggressive tax planning, Member States may not adopt disproportionate anti-abuse rules even where third countries, such as Switzerland in the present instance, are involved. In our opinion, the analysis of the Advocate General as regards the need to comply with principle of proportionality in relation to Art. 1(2) of the EU Parent Subsidiary Directive could also be transposed to art. 9 of the EU-Swiss amending protocol to the Savings Agreement which contains a very similar language: “Without prejudice to the application of domestic or agreement-based provisions for the prevention of fraud or abuse in Switzerland and in Member States, dividends paid by subsidiary companies to parent companies shall not be subject to taxation in the source State.” Accordingly, it could be argued that the same limitation should apply with respect to dividends paid by a EU subsidiary to its Swiss parent company. It is therefore to be hoped that the CJEU will be following the reasoning of the Advocate General.

### Concluding Remarks

At the political level, recent EU corporate tax policy has been marked by a shift towards fiscal protectionism. This trend is clearly reflected in the recently adopted ATAD. At the same time, however, the case law of the CJEU, with which Member States must comply, seems to be moving in the opposite direction: According to the Court, the access to information and the global trend towards fiscal transparency seems to support the idea that the same rules – in particular anti-avoidance provisions – should apply within and outside the European Union. It is to be hoped that this trend, which is fully consistent with the BEPS initiative to which Switzerland is committed as a third country, will be confirmed by the CJEU in the coming years.

- 1) See Art. 11 of Council Directive (EU) 2016/1164 of 12 July 2016 and the derogations thereby provided.
- 2) The common framework established by ATAD of a minimum nature since, as mentioned by Art. 3, the Directive “shall not preclude the application of domestic or agreement-based provisions aimed at safeguarding a higher level of protection for domestic corporate tax bases.” For this reason, the compatibility of the directive with EU primary law, notably the principles of subsidiarity and proportionality, is fueled with controversy.”
- 3) Robert J. DANON, *La règle sur les sociétés contrôlées de la directive européenne anti-évasion fiscale. Analyse critique et impact pour la Suisse*, in IFF Forum 2016/4, p. 291 and ff (see in particular p. 315).
- 4) CJEU, judgment of 24.11.2016, SECIL, case C-464/14
- 5) Opinion of Advocate General Kokott of 19 January 2017 in case C-6/16
- 6) In this latter case, freedom of establishment, which is not applicable to third countries, would indeed become solely relevant
- 7) ECJ, judgment of 24.11.2016, SECIL, case C-464/14
- 8) ECJ, judgment of 24.11.2016, SECIL, case C-464/16, paragraph 59
- 9) ECJ, judgment of 24.11.2016, SECIL, case C-464/16, paragraph 60
- 10) See Art. 7(1) of the ATAD.
- 11) Decision n°2016-614 QPC of 1 March 2017. See also Conseil d’Etat, Decision n°404270 of 15 December 2016

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