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THE CJEU CASE LAW RELEVANT TO THE GENERAL ANTI-AVOIDANCE RULE (GAAR) UNDER THE ANTI-TAX AVOIDANCE DIRECTIVE (ATAD)[1]AND[2]

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ABSTRACT

This study concentrates on the Court of Justice of the European Union (CJEU) case law in order to reconstruct from it an interpretative guidance for the proper understanding and thus application of general anti-abuse rule included in Article 6 ATAD (the ATAD's GAAR). Although Article 6 aims to harmonises general anti-abuse rule in the domain of tax law among all MSs, its wide scope and its phraseology raises a plethora of issues, in particular in respect of its proper – EU compatible – understating and thus application. The analysis of the relevant CJEU case law, as undertaken in this

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paper, will set a scene for the question of compatibility of the ATAD's GAAR with the concept of abuse developed by the CJEU in cases regarding abusive practices of taxpayers. This piece aims to contribute in determining the reasonable understanding of the core elements of the ATAD's GAAR in accordance with the EU primary law, as interpreted by the CJEU. This may provide the readers with a useful interpretative guideline to the ATAD's GAAR, which could be of an assistance not only for tax authorities, but by all stakeholders, including taxpayers, courts, and MSs' legislative bodies.

Keywords: GAAR, ATAD, BEPS, CJEU, tax avoidance, global tax policy, interpretation, proportionality, artificiality.

1 INTRODUCTION

1.1 GENERAL REMARKS ON THE ATAD'S GAAR

The general anti-abuse rule included in Article 6 ATAD (the ATAD's GAAR) is a unique EU provision, not least because it is the first provision under the EU law, which generally aims against abuse

of tax law[4] of Member States (MSs),[5] but also due to its challenging structure and wording which is supposed to fit all MSs in prevention of abuse of tax law. It reads as follows:

> General anti-abuse rule
>
> 1. For the purposes of calculating the corporate tax liability, a Member State shall ignore an arrangement or a series of

[4] More generally, even if one accepts that EU or international law prohibits the abuse of law (abuse of rights), it is still debatable whether or not the concept of "abuse of law" constitutes a general principle of international law or a general principle of EU law. For EU law see De la Feria; Vogenauer (2011); Piantavigna (2009); Saydé (2014). Although some recent CJEU's case law implies that the prohibition of abuse of tax law stems from or is identified with general principle of EU, such implication has a weak doctrinal foundation and seems to be at odds with its settled case law (see *infra* sec. 4). For international public law see Fitzmaurice (1986); Kiss (1992); Crawford (2003); Byers (2002). See, also the Permanent Court of International Justice's judgement of 7 June 1932, *Free Zone of Upper Savoy and Gex case*, PCIJ Reports, Series A/B, n.º 46, 1032, 167 and International Court of Justice's judgement of 27 August 1952, *United States Nationals in Morocco* case, I.C.J. Reports, 1952, 212.

[5] Before its entry into force, i.e. 1 January 2019, several GAARs have been contained in partially harmonised areas of direct tax law in order to prevent the abuse of the EU directives. See: Article 1(2)-(4) of the 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 (recast), [2011] OJ L 345, p. 8, as amended by Council Directive 2013/13/EU, [2013] OJ L 141, p. 30, Directive 2014/86/EU, [2014] OJ L 219/40, and the Council Directive Council Directive (EU) 2015/121 of 27 January 2015 – hereinafter the Parent-Subsidiary Directive (PSD); Article 5 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, [2003] OJ L 157, p. 49, as amended by Council Directive 2006/98/EC, [2005] OJ L 157, p. 203, and Council Directive 2013/13/EU, [2013] OJ L 141, p. 30 – hereinafter the Interest-Royalty Directive (IRD); and Article 15(1)(a) of the Council Directive 2009/133/EC 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, [2009] OJ L 310/34, as amended by Council Directive 2013/13/EU, [2013] OJ L 141, p. 30 hereinafter the Merger Directive (MD).

> 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 the applicable tax law, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one step or part.
> 2. For the purposes of paragraph 1, an arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality.
> 3. Where arrangements or a series thereof are ignored in accordance with paragraph 1, the tax liability shall be calculated in accordance with national law.

The crucial outcome of Article 6 is that it harmonises a general anti-abuse rule in the domain of tax law among all MSs. Hence it has a very wide scope and its phraseology is not too precise, including expressions such as "the main purpose or one of the main purposes", "defeats the object or purpose of the applicable tax law", and "not genuine [arrangement]".

Structurally, Article 6 is composed of three core elements: (i) an arrangement; (ii) a tax advantage; and (iii) abuse. All three must appear for Article 6 to be triggered. The structure of Article 6 is designed so that it initially opens its gate very broadly by setting low thresholds for identifying "an arrangement" and "a tax advantage", but then narrow it down to what should be considered as "abusive" (cf. to the UK GAAR at BURCHNER; CAPE; HODKIN, 2018, p. 810). However, the abusive part of Article 6 (at least linguistically) does not seem to be narrow enough (or high enough) to be in line with the standard of abuse developed by the CJEU[6] and to delineate between abusive and non-abusive arrangements with a clarity so much needed to comply with the legal certainty and foreseeability principles. This puts Article 6 at odds with its balancing function, which is clearly articulated in the recital 11 of the preamble to the ATAD (concurring: MORENO; ZORNOZA PÉREZ, 2019, p. 118

[6] See *infra* sec. 2-5.

and 126-130; WILDE, 2018, p. 308-314):

> GAARs should be applied to arrangements that are not genuine; otherwise, the taxpayer should have the right to choose the most tax efficient structure for its commercial affairs.

The approach of the EU Council follows from the essential nature of the GAAR which is to cover and prevent the widest possible range of tax abuse cases. It is also needed to achieve its purpose: to *tackle abusive tax practices that have not yet been dealt with through specifically targeted provisions*, such as transfer pricing or CFC rules.[7]"[8] That is to say, the drafters of Article 6 seem to have been motivated by a desire to design a very vague and broad anti--abuse rule, which will function as a deterrent for taxpayers. To a certain extent the drafters seem also to be inclined by a desire to undo what the CJEU had already achieved, i.e. to lower the standard of abuse in tax cases under EU law.

1.2 THE PIVOTAL IMPORTANCE OF CROSS-BORDER SITUATIONS FOR THE RELEVANCE OF THE CJUE'S CASE LAW

Article 6 aims to cover cross border situations (between MSs and between MSs and third countries) and domestic ones. In fact, recital 11 of the preamble to the ATAD emphasises that Article 6 should be applied in cross-border and domestic situations in a uniform manner. This a very important feature of Article, which seeks to prevent the discriminatory application of EU harmonised GAARs by requiring that the scope and results of their application in

[7] See recital 11 of the preamble to the ATAD.

[8] One could argue in accordance with recital 1 of the preamble to the ATAD that the broadest purpose of the GAAR is "the need for ensuring that tax is paid where profits and value are generated". This is, however, highly debatable and questionable (WILDE, 2018, n. 4, p. 319).

domestic and cross-border situations do not differ (see ZALASIŃSKI; OLESIŃSKA, 2018, p. 620; MORENO, 2016, p. 143 et seq.). Moreover, this feature highlights the fact that the practical impact of Article 6 may be in practice much wider than only international arrangements, since that rule covers the whole spectrum of corporate income tax, and many tax avoidance arrangements (perhaps not as sophisticated as those cross-border) are purely domestic.

This feature of Article 6 should not be seen as a way to circumvent a possible scrutiny of the CJEU because of the lack of discrimination or restriction of cross-border situations compared to domestic situations.[9] Fundamentally, the ATAD is secondary EU law and given its inferiority to the primary law, all provisions of that Directive must be compatible with EU Treaties and the relevant CJEU case law, in particular in cases regarding abuse of tax law under fundamental freedoms (see *further* sec. D). Indeed, the EU Commission in the proposal of the ATAD pointed out that in "compliance with the *acquis*, the proposed GAAR is designed to reflect the artificiality tests of the CJEU where this is applied within the Union."

Moreover, as implied by the CJEU case law,[10] the consequences of evaluating whether domestic provisions are compatible with EU law should be drawn not only from their *formal* (*ipso iure*) scope of application, but also from their actual (*ipso facto*) scope of application. Because GAARs target tax avoidance, the phenomenon which typically occurs in cross border situations due to difference in levels of taxation on income among countries and disparities existing in their tax systems, there is a risk that GAARs'

[9] Such attempt was made by the OECD in respect of CFC rules, see OECD (2015, para 22).

[10] See AG P. Léger's opinion of 20 May 1999, paras 31-48 to *Sandoz* case and the corresponding judgments of the CJEU, C-439/97, 14 October 1999, ECR 1999, p. I-07041, para. 19. See also *Baxter*, 8 July 1999, C-254/97, ECR 1999, p. I-04809, paras 12-13.

actual scope of application will cover resident taxpayers which are engaged in cross border arrangements more often than resident taxpayers involved in purely domestic arrangements. It means that the GAARs of MSs would not – in the CJEU's eyes – be immune to analysis of their *ipso facto* (indirect) restrictive effect on fundamental freedoms even though there is case law confirming that, *ipso iure*, not treating domestic and foreign investments differently is enough to avoid a restriction. Only if their *actual* application to cross border and domestic situations would be alike, no restriction arises.

This shows that the proper understanding of the relevant CJEU's case law may prove to be invaluable for determining the appropriate implementation and application of the ATAD's GAAR by MSs. This, naturally, pertains to cross border situations, as purely domestic situations are not within the purview of the CJEU. Hence, this study will focus on potential cross-border use of the ATAD's GAAR, although its application reaches not only cross-border, but also domestic arrangements and transactions.

1.3 THE SCOPE AND THE PURPOSE OF THIS STUDY

The CJEU's case law in the field of abuse law (the relevant CJEU's case law) plays a prominent role in an appropriate implementation and application of the ATAD's GAAR. Firstly, it delineates the compatibility range for the ATAD's GAAR with EU fundamental freedoms. Secondly, it helps to understand the key concepts under the ATAD's GAAR, which aim to cover the notion of abuse of tax law. The importance of the CJEU case law for drafting the ATAD's GAAR was duly noticed by the European Commission, which stated in the proposal to the ATAD that "in compliance with the acquis, the proposed GAAR is designed to reflect the artificiality tests of the CJEU where this is applied within the Union" (see PROPOSAL, 2016, p. 9).

The analysis of the relevant CJEU case law in sections 2-5 below will set a scene for the question of compatibility of the ATAD's GAAR with the concept of abuse developed by the CJEU in cases regarding abusive practices of taxpayers.[11] The attention is given to the structural elements of the concept of abuse under the CJEU case law and this Court's perception of threshold of abuse concerning the taxpayer's intention to obtain a tax advantage. The analysis will be followed by its synthesis and conclusions in the section 6.

This piece aims to contribute in determining the reasonable understanding of the core elements of the ATAD's GAAR in accordance with the EU primary law, as interpreted by the CJEU. This may provide the readers with a useful interpretative guideline to the ATAD's GAAR, which could be of an assistance not only for tax authorities, but by all stakeholders, including taxpayers, courts, and MSs' legislative bodies.

2 THE ORIGIN OF ABUSE

The CJEU's concept of abuse of law has its origin in 1970 in the judgment in *Van Binsbergen* case. In that case, the CJEU for the first time pointed out that a MS may restrict the fundamental freedom (here: the freedom to provide services) to prevent the circumvention of domestic rules insofar as EU law does not protect an activity that is "*entirely or principally* directed towards its territory [...] *for the purpose of avoiding* [its domestic rules]" (the emphasis added by the author).[12] This implies that for the CJEU the circumvention of

[11] The present analysis focuses only on the milestones in the CJEU case law on abuse of law and it does not necessarily follow a chronological order of the judgments. The aim is to succinctly and effectively compose the historical and current state of art in the area of abuse of tax law as developed by the CJEU case law.

[12] See the CJEU, 3 December 1974, C-33/74, *Van Binsbergen*, EU:C:1974:131, para. 13. The quoted findings stemming from this landmark judgment has been used by the CJEU in many other cases regarding the fundamental freedoms, i.e.

domestic rules in certain circumstances equals an abusive practice that is not protected by EU law. This is in particular pertinent to U-turn schemes. Although U-turn schemes have been usually identified as a source of abusive practices in VAT cases,[13] they have been also identified in blatant tax avoidance cases regarding direct taxation (see KUŹNIACKI, 2017, sec. 3.4.2). This shows that the reasoning of the CJEU used to initiate the concept of the abuse of law in respect of the freedom to provide services was from the very beginning relevant to some types of abuse in the field of tax law. Until 2000, however, no much guidance was given by the CJEU on the way to determine the abuse.

freedom to provide services (the freedom of establishment, the free movement of goods and the free movement of workers). CJEU, 18 March 1980, C-52/79, *Debauve*, EU:C:1980:83; CJEU, 25 July 1991, C-288/89, *Stichting Collectieve Antennevoorziening Gouda*, EU:C:1991:323; CJEU, 16 December 1992, C-211/91, *Commission v. Belgium*, EU:C:1992:526; CJEU, 3 February 1993, C-148/91, *Veronica Omroep Organisatie*, EU:C:1993:45; CJEU, 10 September 1996, C-11/95, *Commission v. Belgium*, EU:C:1996:316; CJEU, 10 September 1996, C-222/94, *Commission v. United Kingdom*, EU:C:1996:314; CJEU, 5 June 1997, C-56/96, VT4, EU:C:1997:284 and CJEU, 9 July 1997, C-34/95, C-35/95 and C-36/95, *De Agostini and TV-Shop*, EU:C:1997:344. 8 CJEU, 7 February 1979, C-115/78, *Knoors*, EU:C:1979:31; CJEU, 6 October 1981, C-246/80, *Broekmeulen*, EU:C:1981:218; CJEU, 22 September 1983, C-271/82, Auer, EU:C:1983:243; CJEU, 19 January 1988, C-292/86, *Gullung*, EU:C:1988:15; CJEU, 27 September 1988, C-81/87, *Daily Mail*, EU:C:1988:456; CJEU, 27 September 1989, C-130/88, *Van de Bijl*, EU:C:1989:349; CJEU, C-61/89, 3 October 1990, *Bouchoucha*, EU:C:1990:343; CJEU, 9 March 1999, C-212/97, *Centros*, EU:C:1999:126 and CJEU, 30 September 2003, C-167/01, *Inspire Art*, EU:C:2003:512. 9 CJEU, 10 January 1985, C-229/83, *Leclerc*, EU:C:1985:1. 10 CJEU, 23 March 1982, C-53/81, *Levin*, EU:C:1982:105; CJEU, 27 March 1985, C-249/83, *Hoeck*x, EU:C:1985:139; CJEU, 3 June n1986, C-139/85, *Kempf*, EU:C:1986:223 and CJEU, 21 June 1988, C-39/86, *Lai*r, EU:C:1988:322 and CJEU, 26 February 1991, C-292/89, *Antonissen*, EU:C:1991:80. The case law cited after: Prats et al. (2018, p. 7 at footnotes 7-10).

[13] For that see Weber (2005, p. 196-201 and 206-208).

3 THE TWO-PRONGED TEST, THE OBJECTIFIED INTENTION, AND THE ESSENTIAL PURPOSE

The CJEU gave more clarity to the concept of abuse of law in its judgment of 14 December 2000 in the *Emsland-Stärke* case by introducing a two-pronged test in finding the abuse: (i) a combination of objective circumstances in which, despite formal observance of the conditions laid down by the EU rules, the purpose of those rules has not been achieved; (ii) a subjective element consisting in the intention to obtain an advantage from the EU rules by artificially creating the conditions laid down for obtaining it.[14] This test turn out to be the role model for determining abuse in EU. It became useful for that purpose across all areas of the CJEU's juridical purview and was integrated into several anti-abuse rules in EU secondary law which partly harmonises the area of taxation (see PRATS at al., 2018, p. 8).

The two-pronged test for the first time was applied by the CJEU in tax matters on 21 February 2006 in the *Halifax* case regarding VAT, i.e. fully harmonised area of taxation at the EU level. In this landmark case, the CJEU objectified the second prong of the abuse test by saying that in order to determine the abuse of VAT Directive,[15] it must be "apparent from *a number of objective factors* that the *essential aim* of the transactions concerned is to obtain a tax advantage" (the emphasis added by the author).[16] This finding of the CJEU showed that a determination of taxpayers' tax avoidance intention must not be based on the subjective, but the objective elements of the taxpayers' arrangement (the objectified purpose/

[14] See the CJEU, 14 December 2000, C-110/99, *Emsland-Stärke*, EU:C:2000:695, paras 52-53.

[15] The Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes - Common system of value added tax: uniform basis of assessment, OJ L 145, 13.6.1977, p. 1-40.

[16] See the CJEU (Grand Chamber), 21 February 2006, C-255/02, *Halifax plc*, EU:C:2006:121, para 75.

intention),[17] and that the *essential* rather than the *sole* purpose to avoid taxation is enough to pass the subjective part of the abusive test in the domain of VAT.

4 THE SOLE, THE ESSENTIAL, THE PREDOMINANT, THE MAIN, AND THE ONE OF THE MAIN PURPOSES' STANDARD OF ABUSE UNDER EU SECONDARY LAW

Historically, the CJEU used the threshold of abuse in line with the standard of sole/essential/predominant/main intention to obtain a tax advantage by a taxpayer under EU directives to identify the abuse of law. Interestingly, it was done so irrespective of the fact that the wording of the anti-abuse rules under the directives reflected the standard of one of the principal/primary intentions/motives. For instance, in the *Kofoed* case of 5 July 2007,[18] the CJEU dealt with the question of abuse which under the analysed MD was coined in respect of the taxpayer's intention part as "principal objective or as one of its principal objectives tax evasion or avoidance".[19] Despite this wording, the CJEU implied in para 38 of its judgement that the abusive practices in light of the MD exists only if transactions were carried out not in the context of normal commercial operations, but *solely for the purpose of wrongfully obtaining advantages* provided for by Community [now: EU] law" [emphasis added by the author].

This passage was repeated by the CJEU in para. 50 of its judgment of 10 November 2011 in the *Foggia* case.[20] Although in para 35 of this judgment, the CJEU implied the lower threshold of abuse than the sole purpose by saying that "tax considerations, can constitute a valid commercial reason provided, however, that those

[17] Cf. AG P. Maduro opinion of 7 April 2005 on *Halifax Plc.*, para 70. See more on the objectified intention in tax avoidance cases in Tran (2008, p. 86); Weber (2013, p. 252).

[18] See the CJEU judgment of 5 July 2007, C-321/05, *Kofoed*, EU:C:2007:408.

[19] Article 11(1)(a) of MD (Directive 90/434.

[20] See the CJEU judgment, 10 November 2011, C-126/10, *Foggia*, EU:C:2011:718.

considerations are not *predominant* in the context of the proposed transaction" (emphasis added by the author), the abuse threshold was still more demanding for the tax authorities than under the MD, i.e. *predominan*t purpose according to the CJEU's interpretation vs *one of the principal purposes* according to the wording of the MD. One can also infer from this juxtaposition that according to the CJEU the phrase „one of the principal purposes" should be understood as „the predominant purpose". That is to say, the taxpayer's tax intention cannot be lower than *predominant* to meet the standard of abuse under the EU secondary law.

In more recent *Eqiom* case of 7 September 2017[21] and *Deister Holding* and *Juhler Holding* joined cases of 20 December 2017,[22] the CJEU further clarified that the objective of combating abuse under EU secondary law has the same scope as under EU primary law and therefore must be justified in the same way, i.e. by the need to exclusively target wholly artificial arrangements which do not reflect economic reality, the purpose of which is to unduly obtain a tax advantage.[23] Although no explicit reference to the degree of the taxpayer's intention to obtain a tax advantage was made by the CJEU, the use of the wholly artificial arrangement's mantra from the *Cadbury Schweppes*[24] implies that the Court had in mind the *sole* purpose rather than the *principal or one of the principal purposes.* This deviation from the wording of the anti-abuse rule under EU secondary law was implicitly justified by the CJEU by saying that the derogation from providing tax advantage under PSD must be

[21] The CJEU of 7 September 2017, Case C-6/16, *Eqiom* SAS, ECLI:EU:C:2017:641.

[22] The CJEU 20 December 2017, Joined Cases C-504/16 & C-613/16, *Deister Holding and Juhler Holding*, ECLI:EU: C:2017:1009.

[23] See para 30 and 60 of the *Eqiom* and *Deister Holding and Juhler Holding*, respectively.

[24] See the CJEU, 12 September 2006, Case *Cadbury Schweppes*, EU:C:2006:544. Indeed, the CJEU in *Eqiom* directly referred to the *Cadbury Schweppes* in para. 30 and indirectly did so in the *Deister Holding and Juhler Holding* by referring in para. 60 to para. 30 of the *Eqiom* in the case law cited there, i.e. also *Cadbury Schweppes*.

interpreted strictly. Otherwise the overarching purpose of this Directive, which is to ensure fiscal neutrality for distribution of profits from subsidiaries to their parent companies, may be frustrated.[25]

This settled case law of the CJEU indeed provided a far-reaching protection of taxpayers who optimize their taxation, including the use of pure holding companies or pure management companies in the EU with ultimate shareholders in third countries (see more in KUŹNIACKI, 2019, p. 312-323).

In the Danish beneficial ownership cases on 26 February 2019[26] the abuse of IRD and PSD, the CJEU seems to compose the concept of abuse under EU secondary law by referring to the *principal objective or one of the principal objectives* to obtain a tax advantage, i.e. by sticking to the wording of anti-abuse rules under IRD and PSD, rather than to the *sole* or the *essential* or the *predominant* objective of doing so. However, a closer look at the entire sentence of the CJEU in which the abovementioned phrase was used implies that the standard of abuse under EU secondary law does appear to be lowered down at all, or, at most, it was lowered down only in respect of the taxpayer's intention to obtain a tax advantage.

> A group of companies may be regarded as being an artificial arrangement where it is *not set up for reasons that reflect economic reality*, its structure is *purely one of form* and its principal objective or one of its principal objectives is to obtain a tax advantage running counter to the aim or purpose of the applicable tax law.[27] [the emphasis added by the author]

[25] See para. 26 *Eqiom* and paras. 49-50 *Deister Holding and Juhster Holding*. See also CJEU, 25 September 2003, Case C-58/01, *Océ van der Grinten*, ECLI:EU:C:2003:495, para. 86.

[26] See CJEU's judgments of 26 February 2019 in the "Danish Beneficial Ownership Cases", C-115/16, C-118/16, C-119/16, C-299/16, *N Luxembourg 1, X Denmark A/S, C Danmark I (C-119/16), Z Denmark ApS,* ECLI:EU:C:2019:134 regarding the abuse under the IRD and C-116/16 and C-117/16, *T Danmark and Y Denmark Aps*, ECLI:EU:C:2019:135, on the abuse of the PSD.

[27] See Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16 regarding IRD, para. 127 and Joined Cases C-116/16 and C-117/16 on PSD, para. 100.

In this author's opinion, if an arrangement is not set up for reasons that reflect economic reality and its structure is purely one of form, it is inconceivable that only one of its principal objectives is to obtain a tax advantage. The sole, or at least essential/predominant/main objective that outranks all other of its objectives, seems to be associated to such artificial arrangement. Accordingly, the use of the phrase "one of the primary objectives" by the CJEU does not seem to change much (if anything at all) in relation to determining the standard of abuse of EU secondary law.

It is also worth to mention that the CJEU with the Danish Beneficial Ownership cases has introduced the obligation for the tax authorities of MSs to deny a tax advantage in the area of partly harmonised direct taxation by relying on an unwritten, general EU principle to prevent abuse, even in the absence of domestic or agreement-based anti-abuse provisions.[28]'[29] Despite a weak doctrinal foundation of this conclusion of the CJEU,[30] being at odds with its settled case law,[31] which may only be explained on account of the

[28] In relation to the fully harmonised indirect taxation, see CJEU: 18 December 2014, Joined Cases in *Italmoda*, C-131/13, C-163/13 and C-164/13, EU:C:2014:2455, para.62, 22 November 2017, *Cussens*, C-251/16, EU:C:2017:881, para. 33.

[29] See paras. 117-118 of C-115/16 and paras. 89-90. of C-116/16.

[30] See Haslehner and Kofler (2019) Cf. Zalasiński (2012, sec. 5). See more generally in Weber (2005); De la Feria and Vogenauer (2011); Dourado (2017).

[31] See CJEU, 5 July 2007, Case C-321/05, *Kofoed*, EU:C:2007:408, para. 42, where the CJEU stated that: "the principle of legal certainty precludes directives from being able by themselves to create obligations for individuals. Directives cannot therefore be relied upon per se by the Member State as against individuals". See also the opinion of AG Kokott, who clarified that recourse to "any existing general principle of [EU] law prohibiting the misuse of law" would be barred, as the anti-abuse rule under EU secondary law is a concrete expression of such principle. See Opinion AG Kokott, 8 February 2007, Case C-321/05, *Kofoed*, EU:C:2007:86, para. 67, and Opinion AG Kokott, 16 July 2009, Case C-352/08, *Zwijnenburg*, EU:C:2009:483, para. 62.). "It is clear that no general principle exists in European Union law which might entail an obligation of the member states to combat abusive practices in the field of direct taxation and which would preclude the application of a provision such as that at issue in the main proceedings where the taxable transaction proceeds from such practices and European Union law is not involved", as noted by CJEU, 29 March 2012, C-417/10, *3M Italia*, EU:C:2012:184, para. 32.

specificities of Danish legislation and socio-political after-BEPS pressure, this finding of the Court is of little practical relevance at the present and in the future due to the implementation of ATAD's GAAR by MSs. Since that rule embodies the general principle of prevention of abuse in the area of taxation, MSs will always have in force a written rule to deny a tax advantage. The retrospective effect of that CJEU judgment, in turn, appears to be very doubtful under the principles of rule of law and legal certainty.

5 FROM THE SOLE TO ONE OF THE PRINCIPAL PURPOSES' STANDARD OF ABUSE UNDER EU PRIMARY LAW BETWEEN MSs AND BETWEEN MSs AND THIRD COUNTRIES

After the analysis of cases in the field of indirect taxes fully harmonised under EU secondary law and direct taxes partly harmonized under EU secondary law, it is now wise to turn the attention to CJEU case law in the area of direct taxes, which is not fully or even largely harmonised under EU secondary law. Although the ATAD's GAAR sets the general standard of abuse, thus applying to harmonised and not harmonised areas of taxation, it appears reasonable to argue that the GAARs under Directives (EU secondary law) should trump the ATAD's GAAR. Consequently, CJEU case law analysed below seems to be of outmost relevance and importance in completing the scene for a proper understanding of the abuse standard under the ATAD's GAAR.

The CJEU already in 1986 in *Avoir Fiscal* fully acknowledged that a taxpayer may rely on EU law to choose and enforce the most favourable tax route in their affairs.[32] Since then such finding

[32] See CJEU: 28 January 1986, *Commision vs France (Avoir Fiscal)*, 270/83, EU:C:1986:37, para. 25; 26 October 1999, C-294/97, *Eurowings Luftverkehr*, EU:C:1999:524, para. 44 et seq.; 11 December 2003, Case C-364/01, *Barbier*, ECLI:EU:C:2003:665, para. 71.

constituted a point of departure in the CJEU's reasoning in all tax avoidance cases.[33] This is why recital 11 of the preamble to ATAD says that the taxpayer should have the right to choose the most tax efficient structure for its commercial affairs. That is also why simply counteracting a tax avoidance does not amount to abuse of EU primary law.[34] Such abuse, in turn, constitutes only the qualified tax avoidance, i.e. through the use of wholly artificial arrangements intended solely to escape taxation.

The CJEU for the first time coined the phrase "wholly artificial arrangement" in its judgment of 16 July 1998 in *ICI* case[35] and since then it was repeated in nearly all cases on tax avoidance,[36] including the landmark case *Cadbury Schweppes* of 12 September 2006.[37]

In para. 64 of judgement in the *Cadbury Schweppes* case, the CJEU stated the two-pronged test applies to determine the existence a wholly artificial arrangement. In that respect, the references were made to paras. 52-53 of the judgements in the *Emsland-Stärke* and *Halifax* cases,[38] even though the terms used in those paras. were "abuse" and "an abusive practice", not "wholly artificial arrangement". This implies that the phrase "a wholly artificial arrangement" could be understood as "an abusive practice" in the area of not harmonised direct taxes (see SAYDÉ, 2014, p. 92) (by analogy in the area of harmonised direct taxes).

[33] See, for example, CJEU: 26 October 1999, C-294/97, *Eurowings Luftverkehr*, EU:C:1999:524, para. 44 et seq.; 11 December 2003, Case C-364/01, *Barbier*, ECLI:EU:C:2003:665, para. 71.

[34] See C-39/13, C-40/13 and C-41/13, para. 42 and AG J. Kokott in her opinion delivered on 12 September 2006 in C-231/05, para. 62.

[35] C-264/96, EU:C:1998:370, para 26.

[36] See, for example, 21 November 2002, C-436/00, *X and Y*, EU:2002:704, para. 61; C-324/00, *Lankhorst-Hohorst*, ECR I-11779, para. 37; *De Lasteyrie du Saillant*, para. 50; and *Marks & Spencer*, para. 57.

[37] See CJEU, 12 September 2006, C-196/04, *Cadbury Schweppes*, ECLI:EU:C:2006:544, paras. 51, 55, 56, 57, 61, 63, 68, 69, 72, 75, and 76.

[38] C-110/99 and C-255/02 respectively.

Also, from the *Cadbury Schweppes* follows that the threshold for abuse in relation to the tax avoidance's intention is *sole*.

> It follows that, in order for a restriction on the freedom of establishment to be justified on the ground of prevention of abusive practices, the specific objective of such a restriction must be to *prevent* conduct involving the creation of *wholly artificial arrangements* which do not reflect economic reality, *with a view to escaping the tax normally due* on the profits generated by activities carried out on national territory.[39]
>
> [...] the fact that none of the exceptions provided for by the legislation on CFCs applies and that the intention to obtain tax relief prompted the incorporation of the CFC and the conclusion of the transactions between the latter and the resident company does not suffice to conclude that there is a wholly artificial arrangement *intended solely to escape that tax*.[40] [the emphasis added by the author].

A contrario, there is no abuse if a taxpayer shifts its *genuine economic activities* to other MS for the sole purpose to avoid taxation (see PRATS et al. 2018. p. 12). That being said, the abuse exists only if: (i) there is no genuine economic activity being conducted by the taxpayer and (iii) their sole purpose is to conduct that non-genuine activity in order to avoid taxation.

The CJEU recognized the abuse in the field of direct taxation in more sophisticated way than by referring to wholly artificial arrangements in cases regarding the free transfer of profits in the form of tax deductible expenses/losses at the choice of a taxpayer.[41] Arrangements or transactions which trigger transfers of expenses/losses, typically covered by domestic transfer pricing or thin capitalisation rules, can be considered abusive (artificial), even if they

[39] See *Cadbury Schweppes*, para. 55.
[40] See *Cadbury Schweppes*, para. 63.
[41] See the CJEU: 18 July 2007, *OY AA*, C-231/05, ECLI:EU:C:2007:439, para. 63; 21 January 2010, *SGI*, C-311/08, ECLI:EU:C:2010:26, para. 66.

are conducted by entities engaged in genuine economic activities, *to the extent* that they *exceed* the arm's length "compatible" value.[42] In such cases, however, the taxpayer should have an opportunity to provide a commercial justification for their non-arm's length arrangements or transactions, without being subject to undue administrative constraints.[43]

The cross border non-arm's length arrangements or transactions, according to the CJEU, may undermine a balanced allocation of the power to impose taxes between the MSs via increasing the taxable base in the low-tax MS and reducing it in the high-tax MS to the extent of the losses/expenses that will be transferred on non-arm's length basis.[44] Thus, in such cases, safeguarding the balanced allocation of taxing powers between MSs can be considered a separate autonomous justification.[45] In other cases, the balanced allocation of taxing powers between MSs may constitute a justification in combination with other reasons, e.g. prevention of tax avoidance or ensuring coherence of tax system. One may therefore observe that MSs have more scope to apply domestic anti-avoidance provisions within the EU for excluding cross-border offsetting of losses with profits than to apply other types of anti-avoidance provisions (cf. WEBER, 2013, p. 320-322; PISTONE, 2015, p. 445-446), i.e. they can prevent abuse beyond

[42] See 13 March 2007, C-524/04, *Test Claimants in the Thin Cap Group Litigation*, ECLI:EU:C:2007:161, para. 92.

[43] See CJEU, 31 May 2018, *Hornbach-Baumarkt*, C-382/16, ECLI:EU:C:2018:366, para. 49. According to the CJEU, the concept of 'commercial justification' must be interpreted in light of the principle of free competition which, by its nature, rules out acceptance of economic reasons resulting from the position of the shareholder.

[44] See C-446/03, paragraph 46; C-231/05, paragraphs 54-56 and C 337/08, paragraphs 32-33. See also Smit (2012, p. 269); Weber (2013, p. 320-322); Pistone (2015, p. 445-446).

[45] The prevention of double compensation of losses is an autonomous justification for restricting fundamental freedoms since the CJEU judgments of 12 June 2018 in *Bevola* case, C-650/16, ECLI:EU:C:2018:424, paras. 52-53 and in *NN A/S* case of 4 July 2018, C-28/17, ECLI:EU:C:2018:526, paras. 42-48.

wholly artificial arrangements.[46]

The CJUE through the case law discussed above implies that a balanced allocation of the power to impose taxes between MSs would be threatened if tax avoidance via wholly artificial arrangements were to be permitted. In other words, there is a direct causal link between the creation and exploitation of wholly artificial arrangements for the sole purpose of tax avoidance and a risk to the balanced allocation of taxing rights (cf. WEBER, 2013, p. 258). While preventing the former automatically protects the latter, the causal chain does not work in the opposite direction, showing that the CJEU did not consider the need protect the balanced allocation of taxing powers between Member States as a separate justification to apply anti-avoidance provisions in a restrictive manner. Instead the Court regarded that issue as immanently linked with the need to prevent the use of wholly artificial arrangements to avoid tax, or, to put it differently, that the need to safeguard the balanced allocation of taxing powers between Member States is part of an economic substance analysis.

A subtle economic substance analysis, i.e. assessing a transfer of the profits rather than the entire arrangement, can also be found in the recent *X GmbH* case of 26 February 2019.[47] In the *X GmbH*, the Court stated that the free movement of capital between Member States and third countries is intended not to frame the conditions under which companies can establish themselves within the internal market. Therefore:

[46] It should be bear in mind, however, that double compensation of losses may not be abusive at all. For instance, a compensation of losses by a foreign PE in its state of location and in the residence state of its head office does not constitute an abusive practice, if stemming from an ordinary course of business of the PE and its head office.

[47] See CJEU, C-135/17, ECLI:EU:C:2019:136.

> in the context of the free movement of capital, the concept of 'wholly artificial arrangement' cannot necessarily be limited to merely the indications, referred to in paragraphs 67 and 68 of the judgment of 12 September 2006 in *Cadbury Schweppes* case, that the establishment of a company does not reflect economic reality [...].
>
> That concept is also capable of covering, in the context of the free movement of capital, any scheme which has as *its primary objective or one of its primary objectives the artificial transfer of the profits made by way of activities carried out in the territory of a Member State to third countries with a low tax rate*. [the emphasis added by the author].[48]

These findings of the CJEU imply that for the purpose of examining the proportionality of the domestic legislation, which restricts free movement of capital between MSs and third countries, the understanding of the wholly artificial arrangement, reflecting the standard of abuse of EU law in direct taxation cases, amounts to any scheme which has as its primary objective or one of its primary objectives the artificial transfer of the profits made by way of activities carried out in the territory of a MS to third countries with a low tax rate. In this author view, there would be no difference in an intra-EU situation. The main driver for differentiating the approach in determining the standard of abuse may be, however, the differences among the scope and the substantive requirements to be protected under different fundamental freedoms. The freedom of establishment will always triggers the need for scrutinizing premises, people on the ground, physical offices, while the freedom to provide of services or the free movement of capital may require to focus on more subtle constituencies of the arrangements, such as contracts between the companies, transfers of profits between companies (their circularity).

[48] See CJEU, C-135/17, *X GmbH*, para. 84.

6 SYNTHESIS AND CONCLUSIONS

Since the origin of the concept of abuse under CJEU case law, it was clear that the taxpayers have right to choose the most efficient way to route their tax affairs and that their intention to obtain a tax advantage have to be sole or at least essential/predominant/main to enter under the radar of abuse. Identifying the degree of that intention matters for the second prong of the two-pronged test in finding the abuse. The first prong, in turn, requires a combination of objective circumstances in which, despite formal observance of the conditions laid down by the EU rules, the purpose of those rules has not been achieved.

As a result of changes in company tax landscapes since *Cadbury Schweppes* and the preceding cases, both societally and politically (especially in the course of post-BEPS), the CJEU nowadays is more prone to deviate from its settled case law in setting the threshold for abuse. Nevertheless, despite moving from the *sole/essential/predominant/principal* intention of a taxpayer to obtain a tax advantage to *one of the main purposes*, the CJEU keeps saying that an abusive (artificial) arrangement is that which is not set up for reasons that reflect economic reality and its structure is purely one of form. In context of tax cases, it is hardly to imagine that such arrangement is designed by a taxpayer for other purpose than to solely or essentially/predominantly/mainly obtain a tax advantage.

Furthermore, the CJEU has never in the area of not harmonised direct tax law cases among MSs stated that the standard for abuse may rely on the threshold lower than the sole intention to obtain tax advantage. In the scope of partly harmonised direct tax law or fully harmonised indirect tax law, this threshold went below to the essential, predominant or main intention, but never lower, except the recent Danish beneficial ownership cases where the phrase "one of the primary objectives" has been used, but, as observed before, it does not change much in that respect. Only in the *X GmbH* case,

the CJEU used the phrase "one of the primary objectives" in not harmonised direct tax law, but that case regarded the artificial transfer of the profits from a MS to a low tax third country. Again, it is implausible to consider such transfers are realised by a taxpayer for one of the primary objectives to obtain a tax advantage. Rather they are deliberately designed and conducted to solely or essentially/predominantly/mainly obtain a tax advantage.

To sum up: (i) there is nothing in the CJEU relevant case law implying that one of the main purposes to obtain a tax advantage can constitute a threshold of abuse among MSs in not harmonised area of direct tax law; and (ii) beyond that, i.e. partly harmonised direct tax law or not harmonised direct tax law in situations between MSs and third countries, coining the phrase "one of the principal/primary purposes/objectives" is of little relevance insofar as the phrase "artificial" in respect to an arrangement or transaction has been always used as well. In the reality of corporate tax avoidance, artificial arrangements or transactions are not designed by taxpayers to obtain a tax advantage for other than sole or essential, predominant or main purpose. Furthermore, the CJEU relevant case law implies that different circumstances should be taken into account to decide about the existence of abuse, especially in respect of determining the artificiality of the arrangements or transactions, under different fundamental freedoms, different national legislation, and different types of specific arrangements or transactions.[49] In particular, the relevant circumstances to be taken into account include the geolocations of arrangements or transactions (within or outside of the EU) and their type and nature (purely passive financial transactions concluded on paper versus active business transactions triggering changes in the physical world).

[49] Cf. 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*, Brussels 10.12.2007, COM (2007) 785 final, p. 5. Cf. also Weber (2016, p. 117); Lenaerts (2015, p. 329); Robert; Tof (2011, p. 436).

The overall analysis of the CJEU relevant case law implies that the phrases "the main purpose" and "one of the main purposes" should be understood alike as "the main purpose", but more typically as the essential or the predominant purpose. Any lower standard of abuse under the ATAD's GAAR would make this rule either applicable disproportionally (not only to abusive but also to non-abusive practices) or largely dysfunctional by the lack of compatibility with the second and the third test: It is highly unlikely that the taxpayer's arrangement is to be artificial enough to defeat the object and purpose of the tax law if only one of its main purposes was to obtain a tax advantage. This guidance, as stemming from the CJEU relevant case law, once followed, may contribute to a reasonable, proportional and EU compatible way of reading and applying the ATAD's GAAR by tax authorities of MSs.

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