EU Court of Justice holds Dutch fiscal unity regime contrary to EU law in SCA-Holding case

Executive summary

On 12 June 2014, the Court of Justice of the European (CJEU) issued its ruling on the compatibility of the Dutch fiscal unity regime in the light of the freedom of establishment in the case SCA Group Holding BV and others. The Dutch fiscal unity regime allows groups of companies to file one single tax return and to calculate Dutch corporate income tax on a consolidated basis. This means that, for example, losses incurred by one company in the group may be offset against the profits of another.

No fiscal consolidation is possible, however, between a Dutch parent and a Dutch second tier subsidiary which is held by an intermediate company in another EU Member State. Similarly, the regime does not allow two Dutch subsidiary (sister) companies held by a parent company in another Member State to form a fiscal unity between them. This implies that Dutch companies which have their linking company in another Member State cannot benefit from the Netherlands group consolidation regime.

The CJEU in its ruling decided that the Dutch regime infringes upon the freedom of establishment in both respects and that no valid grounds for justification are available. This decision implies that the Netherlands tax authorities should allow for a Dutch fiscal unity between Dutch companies that are linked with each other through an intermediate company in another EU Member State.
Detailed discussion

Background
Under Dutch tax law, companies forming part of a group of companies, are taxable on a stand-alone basis. This means that each company needs to individually file its own corporate income tax return, losses incurred by one group company may not be offset against profits derived by another group company and that intragroup transactions may individually give rise to profits and losses.

However, from the perspective of a group of companies as a whole, taxation on a stand-alone basis may not always be feasible or desirable, as it increases compliance costs and may result in taxation of legal profits that have not been realized from an economic point of view of the whole group. For that reason, Dutch tax law provides for the fiscal unity regime, which allows groups of companies to file one single tax return and to calculate Dutch corporate income tax on a consolidated basis.

Forming a fiscal unity for Dutch corporate income tax purposes is subject to a number of requirements, one of the main of which is that eligible companies should all be corporate tax resident in the Netherlands, or should at least have a sufficient nexus within the Netherlands territory by virtue of a branch situated there. In addition, the head of the fiscal unity should own at least 95% of the shares in other group companies that wish to opt for consolidation.

Fiscal unity between a Dutch parent and second tier subsidiary which is held by an intermediate company in another EU Member State
From the above requirements, it follows that the current fiscal unity rules exclude fiscal unities between a Dutch parent and a Dutch second tier subsidiary which is held by an intermediate company in another EU Member State. In the comparable Papillon case decided by the CJEU Union in 2008, the CJEU ruled that a French parent company and a French second-tier subsidiary company should be able to benefit from the French tax consolidation rules, in spite of the intermediate subsidiary being situated in another Member State.

In two of the joint cases at issue, the taxpayers have requested of the Dutch tax authorities to form a fiscal unity between the Dutch parent and a Dutch lower-tier subsidiary that is held through an intermediate company in another EU Member State. This request however, was rejected. The taxpayers subsequently argued before the Court, referencing the Papillon case, that this rejection is incompatible with the freedom of establishment.

The CJEU agrees with the taxpayer’s position. It rules that the denial of approval to form a fiscal unity constitutes a restriction of the freedom of establishment. This is because, in a domestic context, a fiscal unity between a Dutch parent and Dutch lower-tier subsidiaries is possible. The fact that in a purely domestic context a fiscal unity between a Dutch parent and second-tier subsidiary can only be formed if the intermediate company is included as well does not change that conclusion.

The CJEU found no justifications for this restriction. First, this restriction cannot be justified by the need to avoid double loss deduction at the level of the parent, i.e., deduction of a loss of the lower-tier subsidiary through consolidation and a second time through devaluation of the shares in the intermediate company. The CJEU established that devaluation losses on the shares in the intermediate company are exempt under the Dutch participation exemption and are therefore not deductible.

Second, the restriction can neither be justified by the need to combat tax evasion nor tax avoidance. The simple reason is that the Dutch fiscal unity rules are not designed with the specific purpose to combat tax avoidance. Consequently, there is not valid justification to deny the Dutch fiscal unity in the cases at hand.
**Fiscal unity between two Dutch sister companies**

The current Dutch fiscal unity rules also exclude fiscal unities between two Dutch subsidiary companies in the same group, held by a foreign parent company. In one of the joint cases at issue, the taxpayer requested the Dutch tax authorities to form a fiscal unity between two Dutch subsidiary companies in the same group, held by a parent company in another EU Member State. That request was denied. On the basis of a comparable reasoning as set out above, the CJEU ruled that this rejection also constitutes a restriction of the freedom of establishment, for which no valid justification is available.

**Implications**

The ruling of the CJEU may be favorable for Dutch companies forming part of a larger international group. The decision of the CJEU implies that the Netherlands tax authorities should now allow for a Dutch fiscal unity between Dutch companies that are linked with each other through an intermediate company in another EU Member State. The decision may also impact other EU jurisdictions where group consolidation systems are in place.

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**Endnotes**


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