de Nederlandse Orde van Belastingadviseurs
The Dutch Association of Tax Advisers

Committee on Legislative Proposals

Amsterdam, July 12, 2018

Subject: **Proposal for a Directive amending Directive (EU) 2017/1132 as regards cross-border conversions, mergers and divisions (2018/0114 (COD))**

Ladies and Gentlemen,

The Dutch Association of Tax Advisers (hereinafter: the Association) has technical concerns on the impact of the proposed Directive (EU) 2017/1132 as regards cross-border conversions, mergers and divisions[1] (hereinafter: Draft Directive) and therefore sends you these comments on the Draft Directive.

Summary

The Association has fundamental objections to the tax provisions contained in Article 86c and Article 160d of the Draft Directive. Firstly, the terminology used in the Draft Directive differs considerably from that used by the European Court of Justice, in the Anti-Tax Avoidance Directive (ATAD) and in the taxation Merger Directive. This creates ambiguity and legal uncertainty. Moreover, the Association is of the opinion that there are already sufficient tax instruments for combating tax avoidance via cross-border conversions and divisions, in particular the anti-abuse provision in the Merger Directive, the general anti-abuse rule in the ATAD and the mandatory disclosure obligation in the Directive on Administrative Cooperation. Because of the tax implications of the current wording of the Draft Directive, the Association believes that it could only be approved unanimously and thus not, as the intention appears, under the ordinary legislative procedure.

The Association therefore considers that the wording "*obtaining undue tax advantages or*" should be removed from Article 86c and Article 160d. With this adaption, the disadvantages identified above can be avoided and the Draft Directive can be approved under the ordinary legislative procedure.

1. Introduction

The Association wants to draw attention to two provisions in the Draft Directive that have a clear tax connection, i.e. Article 86c and Article 160d. Incidentally, the Association notes that the numbering in the English and German-language versions of the Draft Directive is less complex than in the Dutch and French-language versions: this concerns Articles 86 quater and 160 quinquies in the Dutch and French-language versions. The readability and comparability of the different language versions would

[1] COM(218) 241 final, dated April 25, 2018.

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benefit from using one type of numbering for all the language versions and then preferably the least complex numbering of the English and German-language versions.

Articles 86c and 160d contain the conditions for cross-border conversions and cross-border divisions. Paragraph 3 of both Articles states that 'the competent authority' of the departure Member State or the Member State of the company being divided shall not authorise the conversion or division when it determines, after an examination of the specific case and having regard to all relevant facts and circumstances, that it constitutes an artificial arrangement aimed at 'obtaining undue tax advantages'. The Association has fundamental objections to this provision. The Association explains these objections below.

2. Unclear terminology that differs from EU tax case law and directives

Articles 86c and 160d in the Draft Directive use the terms 'artificial arrangement' and 'undue tax advantages'. These expressions are not explained in the explanatory memorandum. In preamble 40 the term 'undue tax advantages' is used without further explanation as well.

The following sentence appears on page 22-23 of the Explanatory Memorandum to the Draft Directive: "(...) *pursuant to the general principle that EU law cannot be invoked to justify abuse of rights as established in the ECJ's case law, a conversion cannot be authorised when it is determined, after examination of the individual case and having regard to all relevant facts and circumstances, that it constitutes an artificial arrangement aimed at obtaining undue tax advantages* (...)." A comparable explanation concerning the cross-border division is included on page 28.

The problem however, is that the terminology used in the Draft Directive differs from the terminology the European Court of Justice (hereinafter: ECJ) uses in its justifications of restrictions of a fundamental freedom. In paragraph 51 of the landmark Cadbury Schweppes[2] judgment, the ECJ defined this justification as follows: "*On the other hand, a national measure restricting freedom of establishment may be justified where it specifically relates to wholly artificial arrangements aimed at circumventing the application of the legislation of the Member State concerned.*"

Unlike the ECJ, the Draft Directive does not refer to *wholly* artificial arrangements, but only to an 'artificial arrangement', without indicating what the difference is between them. Moreover, it does not use the specific and objective term 'circumventing the application of the legislation', but introduces a new expression 'undue tax advantages'. This is however a very subjective and extremely vague concept. For example, under certain circumstances a cross border conversion or division can be tax neutral. Therefore, such conversion automatically involves tax advantages, otherwise a cross-border conversion or division would not be possible. This then leads to the question what *undue* tax advantages are.[3] What one person considers an undue tax advantage (why is a tax neutral transfer permitted?) another person may consider warranted (it is good for the internal market that a tax neutral transfer is possible). A cross-border conversion, division or merger is usually virtually impossible if it triggers tax. In that respect, there is by definition a certain tax benefit. This raises the question what the exact distinction should be between 'due tax advantages' and 'undue tax advantages'. The same applies to the term 'undue tax advantages' used in preamble 40.

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[2] Case C-196/04, *Cadbury Schweppes*, ECLI:EU:C:2006:544.

[3] Cf. also G.T.K. Meussen, Het richtlijnvoorstel m.b.t. grensoverschrijdende omzettingen, fusies en splitsingen: een opmerkelijke fiscale paragraaf, *Nederlands Tijdschrift voor Fiscaal Recht*, June 14, 2018, p. 2, NTFR 2018/1329, where he states that: "*It is utterly unclear what is meant by the words 'undue tax advantages. No explanation whatsoever is given.*"

The Draft Directive not only uses terminology that differs from that used in ECJ case law, but which also differs from the terminology used in the general anti-abuse rule in the Anti-Tax Avoidance Directive (hereinafter: ATAD).[4] Article 6(1) ATAD states:

"*For the purposes of calculating the corporate tax liability, a Member State shall ignore an arrangement or a series of 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.*"

Therefore, in this provision, unlike in the Draft Directive, the terms 'artificial' and 'tax advantage' are further qualified and specified.

The terminology of the Draft Directive also differs from the terminology of the anti-abuse measure in the taxation Merger Directive,[5] a directive that contains, amongst others, tax rules on cross-border mergers and divisions. According to the ECJ, the anti-abuse measure contained therein is a reflection of the general principle also appearing in the Draft Directive that EU law cannot be invoked to justify abuse of rights.[6]

Article 15 of the Merger Directive allows Member States to refuse the tax benefit (in full or in part) contained in the Merger Directive, if one of the transactions described therein "*has as its principal objective or as one of its principal objectives tax evasion or tax avoidance*". Furthermore, a transaction is presumed to have tax evasion or tax avoidance as its principal objective or one of the principal objectives if the operation is not carried out for valid commercial reasons such as the restructuring or rationalisation of the activities of the companies participating in the operation.

In its interpretation of this anti-abuse provision in the Merger Directive, the ECJ ruled that:

"(...) *a merger operation based on several objectives, which may also include tax considerations, can constitute a valid commercial reason provided, however, that those considerations are not predominant in the context of the proposed transaction.*

Accordingly, under [Article 15 of the Merger Directive], where the merger operation has the sole aim of obtaining a tax advantage and is not carried out for valid commercial reasons, such a finding may constitute a presumption that the operation has tax evasion or avoidance as one of its principal objectives.

(…)

Furthermore, it should be noted that [Article 15 of the Merger Directive] reflects the general principle of EU law that abuse of rights is prohibited. The application of EU legislation may not be extended to cover abusive practices, that is to say, transactions carried out not in the context of normal

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[4] Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

[5] 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

[6] Case C-321/05, *Kofoed*, ECLI:EU:C:2007:408. In case C-014/16, *Euro Park Service*, ECLI:EU:C:2017:177, the ECJ states that the objective of the general principle of primary EU law and the anti-abuse provision in the Merger Directive have the same scope.

commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by that law."[7]

The terminology of the Draft Directive is not in line with the anti-abuse test of Article 15 of the Merger Directive ("*principal objective or as one of its principal objectives tax evasion or tax avoidance*"), nor is it in line with the ECJ's interpretation of the anti-abuse test in the Merger Directive (refusing tax relief if a transaction is solely aimed at obtaining a tax advantage).

The Association's first objection therefore concerns the unclear and vague terminology of the Draft Directive, which terminology differs from that used by the ECJ, in the ATAD and in the Merger Directive. Were this provision to be included, then the Association considers that it must be in line with the existing EU legal framework. The phrase "*an artificial arrangement aimed at obtaining undue tax advantages*" should then be replaced by a phrase used in the ATAD or the Merger Directive. For instance: "*an arrangement or a series of 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.*" Using the same terminology would moreover immediately reveal the duplication and thus the meaninglessness of this provision.[8]

3. A company law Directive is not the appropriate instrument to combat tax avoidance; sufficient tax instruments available

It is the opinion of the Association that a company law directive is not the appropriate instrument for combating tax avoidance. There are specific tax directives for this, in particular, the aforementioned ATAD, the Merger Directive and the amended Directive on Administrative Cooperation (DAC).[9]

As stated above, an EU tax directive on cross-border divisions already exists: the Merger Directive. This directive contains an anti-abuse provision (i) which EU Member States have implemented in their tax legislation and (ii) with which tax payers, the tax administration and tax judges now have considerable experience, also because of ECJ case law. Article 15 of this directive explicitly states that Member States can refuse the advantages of the directive if the principal objective or one of the principal objectives of the particular transaction is tax evasion or tax avoidance. The Association considers that this makes a tax test in a company law directive superfluous.

Insofar as there is a need to introduce an EU directive on the taxing of cross-border conversions, it would be more logical to expand the Merger Directive. This will ensure that all cross-border transactions (mergers, divisions, conversions) are subject to the same anti-abuse tax regime, not only in terms of the test to be performed, but also in terms of the competent authority, the competent court and legal implications (see also below). Because the tax abuse test in the Draft Directive does not apply to cross-border mergers nor does it cover all types of cross-border divisions, there is a risk that cross-border transactions included in the Draft Directive will be treated differently for tax purposes than cross-border transactions that are not included in the Draft Directive but which are included in the Merger Directive. Expanding the Merger Directive instead of including a tax test in the Draft Directive would avoid this difference in tax treatment.

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[7] Case C-126/10, *Foggia*, ECLI:EU:C:2011:718, para 35-36 and 50.
[8] Cf. in this respect also the recent ECJ judgments on tax abuse: ECJ September 7, 2017, *Eqiom en Enka*, C-6/16, EU:C:2017:641 and ECJ December 20, 2017, joined cases C- 504/16 (*Deister*) and C-613/15 (*Juhler*).
[9] Council Directive 2011/16/EU of February 15, 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC.

Under the abovementioned Article 6 of the ATAD, countries can already refuse tax advantages for cross-border legal mergers and divisions, if the stipulated conditions are not met. Articles 86c and 160d of the Draft Directive are thus to this extent superfluous. The fact that tax advantages can be refused by virtue of Article 6 ATAD is enough of a threat.

Moreover, the DAC referred to on page 11 of the Explanatory Memorandum to the Draft Directive has also been extensively expanded in recent years to include measures such as the automatic exchange of cross-border rulings and it will soon be expanded with the automatic exchange of tax information on reportable cross-border tax arrangements (DAC6: mandatory disclosure).[10] The latter reporting obligation, which requires that a cross-border arrangement is reported within 30 days of becoming available, means that the tax authorities of a Member State will already be aware of arrangements involving a cross-border merger or division at an early stage and can investigate them.

Therefore, tax authorities already have enough instruments to combat abuse of cross-border conversions and divisions. Tax authorities are the appropriate body to combat abuse for tax reasons. The aforementioned directives provide tax administrations with effective instruments to combat such abuse. Introducing a company-law test on top of these existing instruments would infringe legal certainty. The same applies to the statement in preamble 40 which implies that in addition to the existing enforcement by tax authorities "*a procedural and substantive framework*" must be laid down "*which describes the margin of discretion and allows for the diversity of approaches by Member States whilst at the same time setting out the requirements to streamline the actions to be taken by national authorities to fight abuses in conformity with Union law should be laid down.*" The Merger Directive, ATAD and DAC already provide sufficient frameworks and procedures insofar as taxation is concerned.

Furthermore, one could question whether prohibiting conversions or divisions under company law based on the tax ground stated in Articles 86c and 160d of the Draft Directive goes further than is necessary (proportionality and subsidiarity tests). Tax sanctions for abuse are focused on the tax implications of the arrangement and fit within and are aligned with the tax systems of Member States. Therefore, these are much more in line with the proportionality and subsidiarity test than the proposed provisions in the Draft Directive.

4. Procedural objection: no unanimity despite there being a proposal with tax implications

On page 11 of the Explanatory Memorandum to the Draft Directive it is explicitly stated that "*The safeguards against abuse of the conversion and division procedures to create artificial arrangements aimed at obtaining undue tax advantages will contribute to EU efforts to fight tax evasion and avoidance.*"

The Draft Directive thus has a clear tax objective. It is, therefore, surprising that the proposed procedure for adoption of the Draft Directive is the ordinary legislative procedure of Articles 50 and 114(1) of the Treaty on the Functioning of the European Union (hereinafter: TFEU), for which a qualified majority suffices. For the approximation of tax laws, an infringement on the tax sovereignty of the Member States, a special legislative procedure applies for which Article 115 TFEU requires unanimous Council approval.

Given the tax implications of the current wording of Articles 86c and 160d, the Association believes that this Draft Directive can only be approved unanimously.

[10] Council Directive 2018/822/EU amending Directive 2011/16/EU regarding mandatory automatic exchange of information in the field of taxation relating to reportable cross-border arrangements.

5. Conclusion

The Association has fundamental objections to the tax provisions contained in the Draft Directive. Firstly, the terminology used in the Draft Directive differs considerably from that used by the ECJ, in the ATAD and in the Merger Directive. This creates ambiguity and legal uncertainty. Secondly, the Association is of the opinion that there are already sufficient instruments for combating tax avoidance and tax evasion via cross-border conversions and divisions, in particular the anti-abuse provision in the Merger Directive, the general anti-abuse rule in the ATAD and the mandatory disclosure obligation in the DAC. Thirdly, because of the tax implications of the current wording of the Draft Directive, it could only be approved unanimously and can, therefore, not be adopted under the ordinary legislative procedure.

The Association, therefore, strongly recommends to omit the wording "*obtaining undue tax advantages or*" from Articles 86c and 160d. If this wording is omitted, the disadvantages identified above are avoided and the Draft Directive can be approved under the ordinary legislative procedure.

Yours sincerely,
The Dutch Association of Tax Advisors

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