JUDGMENT OF THE COURT (Second Chamber)

25 February 2010 (*)

(Articles 43 EC and 48 EC – Tax legislation – Corporation tax – Tax entity consisting of a resident parent company and one or more resident subsidiaries – Taxation of profits at parent-company level – Exclusion of non-resident subsidiaries)

In Case C-337/08,

REFERENCE for a preliminary ruling under Article 234 EC from the Hoge Raad der Nederlanden (Netherlands), made by decision of 11 July 2008, received at the Court on 21 July 2008, in the proceedings

**X Holding BV**

v

**Staatssecretaris van Financiën,**

THE COURT (Second Chamber),

composed of J.-C. Bonichot (Rapporteur), President of the Fourth Chamber, acting as President of the Second Chamber, C.W.A. Timmermans, K. Schiemann, P. Kūris and L. Bay Larsen, Judges,

Advocate General: J. Kokott,

Registrar: M. Ferreira, Principal Administrator,

having regard to the written procedure and further to the hearing on 25 June 2009,

after considering the observations submitted on behalf of:

– X Holding BV, by F.A. Engelen and S.C.W. Douma, belastingadviseurs,

– the Netherlands Government, by C.M. Wissels, M. Noort and D.J.M. de Grave, acting as Agents,

– the German Government, by M. Lumma, C. Blaschke and B. Klein, acting as Agents,

– the Spanish Government, by M. Muñoz Pérez and B. Plaza Cruz, acting as Agents,

– the French Government, by G. de Bergues and J.-C. Gracia, acting as Agents,

– the Portuguese Government, by L. Inez Fernandes and J. Menezes Leitão, acting as Agents,

– the Swedish Government, by A. Falk, S. Johannesson and K. Petkovska, acting as Agents,

– the United Kingdom Government, by H. Walker, acting as Agent, and by M. Gray, Barrister,

– the Commission of the European Communities, by R. Lyal and W. Roels, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 19 November 2009,

gives the following

## Judgment

1 This reference for a preliminary ruling concerns the interpretation of Articles 43 EC and 48 EC.

2 The reference has been made in the course of proceedings between X Holding BV ('X Holding'), a company limited by shares established in the Netherlands, and the Netherlands tax authorities concerning the latters' refusal to grant the company the possibility of forming a single tax entity with a non-resident subsidiary.

### Legal context

*The Agreement for the avoidance of double taxation concluded between the Kingdom of Belgium and the Kingdom of the Netherlands*

3 The Agreement of 5 June 2001 between the Kingdom of Belgium and the Kingdom of the Netherlands for the avoidance of double taxation and the prevention of tax evasion in respect of taxes on income and wealth ('the Double Taxation Agreement') provides in Article 7(1), in accordance with the Model Convention of the Organisation for Economic Cooperation and Development (OECD), that:

'The profits of an undertaking of a Contracting State shall be taxable only in that State unless the undertaking carries on business in the other Contracting State through a permanent establishment situated therein. If the undertaking carries on business in that way, the profits of the undertaking may be taxed in the other State, but only to the extent that they are attributable to that permanent establishment.'

4 Where a taxable person resident in the Netherlands receives income which, under Article 7 of the Double Taxation Agreement, is taxable in Belgium, the Kingdom of the Netherlands, pursuant to Article 23(2) of that Agreement, grants tax relief on that income in accordance with the Netherlands rules on the avoidance of double taxation.

*Netherlands legislation*

5 Article 15 of the 1969 Law on corporation tax provides:

'1. Where a taxable person (the parent company) holds, legally and economically, at least 95% of the shares in the nominal paid-up capital of another taxable person (the subsidiary) and where both taxable persons so request, tax shall be levied on them as if they were a single taxable person, with the activities and assets of the subsidiary forming part of the activities and assets of the parent company. Tax shall be levied on the parent company. In that case, the taxable persons are together regarded as a tax entity. More than one subsidiary may form part of a tax entity.

…

3. The first paragraph shall apply only if:

…

b. for the purposes of calculating the profits, the same provisions apply to both taxable persons;

c. both taxable persons are established in the Netherlands and, in the case where the taxation rules for the Kingdom of the Netherlands [(Belastingregeling voor het Koninkrijk)] or a double taxation agreement is applicable to one taxable person, that person shall also, either under those rules or under that agreement, be regarded as established in the Netherlands;

…

4. Rules may be introduced by general administrative measures permitting taxable persons in respect of which those provisions do not apply, for the purposes of calculating the profits, nevertheless to form a tax entity, by way of derogation from paragraph 3(b). Furthermore, by way of derogation from paragraph 3(c), a taxable person which, in accordance with its national law, or on the basis of the taxation rules for the Kingdom, or again on the basis of a double taxation agreement, is not established in the Netherlands but operates a business through a permanent establishment in the Netherlands may, under conditions defined by general administrative measure, form part of a tax entity, on condition that the power to tax the profits from that company is granted to the Netherlands pursuant to the taxation rules for the Kingdom or a double taxation agreement, and if:

(a) the place of actual management of that taxable person is situated in the Netherlands Antilles, in Aruba, in a Member State of the European Union or in a State with which an agreement for the avoidance of double taxation is applicable, which provides for a prohibition of discrimination of permanent establishments;

(b) the taxable person referred to in (a) is a public company or limited liability company, or a comparable organisation by reason of its nature and its manner of formation, and

(c) when the taxable person referred to in (a) forms part of the tax group as the parent company, the shareholding in the subsidiary referred to in point 1 is part of the assets of that parent company's permanent establishment in the Netherlands.

…'

**The dispute in the main proceedings and the question referred for preliminary ruling**

6 X Holding, which is established in the Netherlands, is the sole shareholder of company F, set up under Belgian law and established in Belgium, and which is not liable to corporation tax in the Netherlands.

7 X Holding and F applied for recognition as a single tax entity within the meaning of Article 15(1) of the 1969 Netherlands Law on corporation tax. The Netherlands Tax Inspectorate rejected that application on the ground that F was not established in the Netherlands, contrary to the requirement of Article 15(3)(c) of that law.

8 An action challenging that refusal was brought before the Rechtbank te Arnhem (Arnhem District Court), which confirmed the legality of that refusal, referring in particular to the judgment in Case

C-446/03 *Marks & Spencer* [2005] ECR I-10837.

9 X Holding appealed in cassation to the Hoge Raad der Nederlanden (Supreme Court of the Netherlands). That court has stayed the proceedings pending a preliminary ruling from the Court of Justice on the following question:

‘Must Article 43 EC, in conjunction with Article 48 EC, be interpreted as precluding national rules of a Member State … which allow a parent company and its subsidiary to opt to have the tax for which they are liable levied on the parent company established in that Member State as if they were a single taxpayer, but which reserve that option to companies which, for the taxation of their profits, are subject to the fiscal jurisdiction of the Member State concerned?’

**The application for the reopening of the oral procedure**

10 By a document lodged at the Court Registry on 2 December 2009, X Holding requested the Court to order the reopening of the oral procedure, pursuant to Article 61 of the Rules of Procedure. According to that company, the Advocate General’s Opinion is based on a misunderstanding of Netherlands national and international tax laws.

11 It is clear from its case-law that the Court may of its own motion, or on a proposal from the Advocate General, or at the request of the parties, order the reopening of the oral procedure in accordance with Article 61 of the Rules of Procedure if it considers that it lacks sufficient information or that the case must be dealt with on the basis of an argument which has not been debated between the parties (see, inter alia, Case C-210/06 *Cartesio* [2008] ECR I-9641, paragraph 46).

12 However, the Netherlands law applicable to the dispute in the main proceedings was set out and commented upon in the written and oral observations submitted to the Court. Accordingly, the Court takes the view that it has all the information necessary to enable it to reply to the question referred.

13 Moreover, it has not been argued that the present case must be dealt with on the basis of an argument which has not been the subject of debate before the Court.

14 The Court, after hearing the Advocate General, accordingly considers it appropriate to reject that request.

**The question referred for a preliminary ruling**

15 By its question, the national court asks, in essence, whether Articles 43 EC and 48 EC preclude legislation of a Member State which makes it possible for a parent company to form a single tax entity with its resident subsidiary but which prevents the formation of such a single tax entity with a non-resident subsidiary, in that the profits of that non-resident subsidiary are not subject to the fiscal legislation of that Member State.

16 It must be borne in mind that, according to settled case-law, although direct taxation is a matter within the competence of the Member States, they must none the less exercise that competence in a manner consistent with Community law (see, inter alia, *Marks & Spencer*, paragraph 29; Case C-374/04 *Test Claimants in Class IV of the ACT Group Litigation* [2006] ECR I-11673, paragraph 36; and Case C-182/08 *Glaxo Wellcome* [2009] ECR I-0000, paragraph 34).

17 Freedom of establishment, which Article 43 EC grants to Community nationals and which includes the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, under the same conditions as those laid down for its own nationals by the law of the Member State in which such establishment is effected, entails, in accordance with Article 48 EC, for companies formed pursuant to the law of a Member State and having their registered office, central administration or principal place of business within the European Community, the right to exercise their activity in the Member State concerned through a subsidiary, a branch or an agency (see, inter alia, Case C-307/97 *Saint-Gobain ZN* [1999] ECR I-6161, paragraph 35, and *Marks & Spencer*, paragraph 30).

18 In that regard, the possibility granted by Netherlands law to resident parent companies and their resident subsidiaries to be taxed as if they formed a single tax entity, that is to say, to be subject to a tax integration scheme, constitutes an advantage for the companies concerned. That scheme allows, in particular, for the profits and losses of the companies constituting the tax entity to be consolidated at the level of the parent company and for the transactions carried out within the group to remain neutral for tax purposes.

19 The exclusion of such an advantage for a parent company which owns a subsidiary established in another Member State is liable to render less attractive the exercise by that parent company of its freedom of establishment by deterring it from setting up subsidiaries in other Member States.

20 In order for such a difference in treatment to be compatible with the provisions of the EC Treaty on the freedom of establishment, it must relate to situations which are not objectively comparable or be justified by an overriding reason in the general interest (see, to that effect, Case C-446/04 *Test Claimants in the FII Group Litigation* [2006] ECR I-11753, paragraph 167).

21 The Netherlands, German and Portuguese Governments submit that those two situations are not objectively comparable, as resident subsidiaries and non-resident subsidiaries are not in comparable tax situations with regard to a tax scheme such as that at issue in the main proceedings. They argue in particular that a subsidiary which is established in another Member State is not subject to the fiscal jurisdiction of the State in which the parent company is established, with the result that it cannot be integrated into a tax entity subject to tax in the latter State.

22 In that context, it is settled case-law of the Court that the comparability of a Community situation with an internal situation must be examined having regard to the aim pursued by the national provisions at issue (see, to that effect, Case C-231/05 *Oy AA* [2007] ECR I-6373, paragraph 38).

23 In tax law, the taxpayers' residence may constitute a factor that might justify national rules involving different treatment for resident and non-resident taxpayers. However, that is not always the case. To accept that the Member State of establishment may in all cases apply different treatment solely because the registered office of a company is situated in another Member State would deprive Article 43 EC of its substance (see, to that effect, Case 270/83 *Commission* v *France* [1986] ECR 273, paragraph 18, and *Marks & Spencer*, paragraph 37).

24 However, the situation of a resident parent company wishing to form a single tax entity with a resident subsidiary and the situation of a resident parent company wishing to form a single tax entity with a non-resident subsidiary are objectively comparable with regard to the objective of a tax scheme such as that at issue in the main proceedings in so far as each seeks to benefit from the advantages of that scheme, which, in particular, allows the profits and losses of the companies constituting the single tax

entity to be consolidated at the level of the parent company and the transactions carried out within the group to remain neutral for tax purposes.

25 It is necessary to examine whether a difference in treatment, such as that at issue in the main proceedings, is justified by an overriding reason in the general interest.

26 In order to be so justified, such a difference must be appropriate for ensuring attainment of the objective pursued and must not go beyond what is necessary to achieve that objective (see, to that effect, Case C-250/95 *Futura Participations and Singer* [1997] ECR I-2471, paragraph 26, Case C-9/02 *de Lasteyrie du Saillant* [2004] ECR I-2409, paragraph 49, and *Marks & Spencer*, paragraph 35).

27 The governments which have submitted observations to the Court argue that the difference in treatment at issue in the main proceedings is justified in particular on the ground of safeguarding the allocation of the power to impose taxes between the Member States.

28 In that regard, it should be noted that the preservation of the allocation of the power to impose taxes between Member States may make it necessary to apply to the economic activities of companies established in one of those States only the tax rules of that State in respect of both profits and losses (see *Marks & Spencer*, paragraph 45, and Case C-414/06 *Lidl Belgium* [2008] ECR I-3601, paragraph 31).

29 To give companies the option of having their losses taken into account in the Member State in which they are established or in another Member State would seriously undermine a balanced allocation of the power to impose taxes between the Member States, since the tax base would be increased in the first Member State, and reduced in the second, by the amount of the losses transferred (see *Marks & Spencer*, paragraph 46, *Oy AA*, paragraph 55, and *Lidl Belgium*, paragraph 32).

30 The same applies with regard to a tax integration scheme such as that at issue in the main proceedings.

31 Since the parent company is at liberty to decide to form a tax entity with its subsidiary and, with equal liberty, to dissolve such an entity from one year to the next, the possibility of including a non-resident subsidiary in the single tax entity would be tantamount to granting the parent company the freedom to choose the tax scheme applicable to the losses of that subsidiary and the place where those losses are taken into account.

32 Since the dimensions of the tax entity can therefore be altered, acceptance of the possibility of including a non-resident subsidiary in such an entity would have the consequence of allowing the parent company to choose freely the Member State in which the losses of that subsidiary are to be taken into account (see, to that effect, *Oy AA*, paragraph 56, and *Lidl Belgium*, paragraph 34).

33 A tax scheme such as that at issue in the main proceedings is, for that reason, justified in view of the need to safeguard the allocation of the power to impose taxes between the Member States.

34 Since such a scheme is appropriate for achieving that objective, it still remains to establish whether or not that scheme goes beyond what is necessary to attain that objective (see, to that effect, inter alia, *Marks & Spencer*, paragraph 53).

35 X Holding and the Commission of the European Communities submit, in that regard, that the

formation of a single tax entity in national territory means that resident subsidiaries are treated for tax purposes in the same way as permanent establishments. They argue that, by way of analogy, non-resident subsidiaries could, in the context of a cross-border tax entity, be treated in the same way as foreign permanent establishments. In their view, however, the losses incurred by a foreign permanent establishment can be temporarily offset against the profits of the parent company under a provision for temporary transfer of losses linked to a recovery arrangement in subsequent financial years. The application of that arrangement to non-resident subsidiaries might constitute a less onerous means to achieve the relevant objective than prohibiting a resident parent company from forming a single tax entity with a non-resident subsidiary.

36 That argument must, however, be rejected.

37 As the Advocate General has stated in point 51 of her Opinion, the fact that a Member State decides to permit the temporary offsetting of losses incurred by a foreign permanent establishment at the place of the company's registered office does not mean that that possibility must also be extended to non-resident subsidiaries of a resident parent company.

38 Permanent establishments situated in another Member State and non-resident subsidiaries are not in a comparable situation with regard to the allocation of the power of taxation as provided for in an agreement such as the Double Taxation Agreement, and in particular in Articles 7(1) and 23(2) thereof. Whereas a subsidiary, as an independent legal person, is subject to unlimited tax liability in the State party to such an agreement in which that subsidiary is established, the same does not apply in the case of a permanent establishment situated in another Member State, which remains in principle and in part subject to the fiscal jurisdiction of the Member State of origin.

39 It is, admittedly, true that the Court has held in other cases that the second sentence of the first paragraph of Article 43 EC leaves traders free to choose the appropriate legal form in which to pursue their activities in another Member State and that freedom of choice must not be limited by discriminatory tax provisions (see, to that effect, *Commission* v *France*, paragraph 22; *Oy AA*, paragraph 40; and Case C-253/03 *CLT-UFA* [2006] ECR I-1831, paragraph 14).

40 However, the Member State of origin remains at liberty to determine the conditions and level of taxation for different types of establishments chosen by national companies operating abroad, on condition that those companies are not treated in a manner that is discriminatory in comparison with comparable national establishments (Case C-298/05 *Columbus Container Services* [2007] ECR I-10451, paragraphs 51 and 53). As permanent establishments situated in another Member State and non-resident subsidiaries are not, as has been stated in paragraph 38 of the present judgment, in a comparable situation with regard to the allocation of the power of taxation, the Member State of origin is not obliged to apply the same tax scheme to non-resident subsidiaries as that which it applies to foreign permanent establishments.

41 Accordingly, in a situation such as that at issue in the main proceedings, in which the tax advantage concerned lies in the possibility granted to resident parent companies and their resident subsidiaries to be taxed as if they formed a single tax entity, any extension of that advantage to cross-border situations would, as has been indicated in paragraph 32 of this judgment, have the effect of allowing parent companies to choose freely the Member State in which the losses of their non-resident subsidiary are to be taken into account (see, by way of analogy, *Oy AA*, paragraph 64).

42 In the light of the foregoing, a tax scheme such as that at issue in the main proceedings must be

regarded as being proportionate to the objectives which it pursues.

43 Consequently, the answer to the question referred is that Articles 43 EC and 48 EC do not preclude legislation of a Member State which makes it possible for a parent company to form a single tax entity with its resident subsidiary, but which prevents the formation of such a single tax entity with a non-resident subsidiary, in that the profits of that non-resident subsidiary are not subject to the fiscal legislation of that Member State.

**Costs**

44 Since these proceedings are, for the parties to the main proceedings, a step in the action pending before the national court, the decision on costs is a matter for that court. Costs incurred in submitting observations to the Court, other than the costs of those parties, are not recoverable.

On those grounds, the Court (Second Chamber) hereby rules:

**Articles 43 EC and 48 EC do not preclude legislation of a Member State which makes it possible for a parent company to form a single tax entity with its resident subsidiary, but which prevents the formation of such a single tax entity with a non-resident subsidiary, in that the profits of that non-resident subsidiary are not subject to the fiscal legislation of that Member State.**

[Signatures]

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* Language of the case: Dutch.