OPINION OF ADVOCATE GENERAL TIZZANO

delivered on 11 September 2001 [1]

1. By order of 9 February 2000, the Vestre Landsret (Danish Western Divisional Court) referred to the Court, in accordance with Article 234 EC, four questions for a preliminary ruling on the interpretation of Article 2(c) and (i) of Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States (hereinafter 'Directive 90/434', or 'the Directive'). [2]

The legislative context

Community law

2. Directive 90/434 was adopted in order to remove fiscal restrictions, imposed by national legislation, which hamper mergers, divisions, transfers of assets and exchanges of shares between companies of different Member States. The recitals to the Directive indicate more particularly that the common system of taxation which it introduces seeks to 'avoid the imposition of tax in connection with mergers, divisions, transfers of assets or exchanges of shares, while at the same time safeguarding the financial interests of the State of the transferring or acquired company'.

3. Article 1 of the Directive provides that '(e)ach Member State shall apply this Directive to mergers, transfers of assets and exchanges of shares in which companies from two or more Member States are involved.' In addition, Article 2, to the extent that it is relevant here, specifies that, '(f)or the purposes of this Directive,

...

(c) "transfer of assets" shall mean an operation whereby a company transfers without being dissolved all or one or more branches of its activity to another company in exchange for the transfer of securities representing the capital of the company receiving the transfer;

1 — Original language: Italian.
2 — OJ 1990 L 225, p. 1.

...

(i) "branch of activity" shall mean all the assets and liabilities of a division of a company which from an organisational point of view constitute an independent business, that is to say capable of functioning by its own means.'

4. In accordance with Article 9 of the Directive, transfers of shares, as defined above, shall be subject to the provisions of Article 4, which states:

'A merger or division shall not give rise to any taxation of capital gains calculated by reference to the difference between the real values of the assets and liabilities transferred and their values for tax purposes', the term 'value for tax purposes' being defined as 'the value on the basis of which any gain or loss would have been computed for the purposes of tax upon the income, profits or capital gains of the transferring company if such assets or liabilities had been sold at the time of the merger or division but independently of it' [Article 4(1)].

National law

5. Article 15(c) of the Fusionsskattelov (Danish Law on the taxation applicable to mergers) states:

'1. In the event of a transfer of assets, companies may be taxed in accordance with the rules of Article 15(d) where both the transferring and the receiving company meet the definition of a company of a Member State given in Article 3 of Directive 90/434/EEC. This applicability shall be conditional upon authorisation having been obtained from the *Ligningsråd*. The *Ligningsråd* may lay down special conditions for such authorisation.

2. The term "transfer of assets" is to be understood as meaning the operation whereby a company, without being dissolved, transfers all or one or more branches of its activity to another company in exchange for a transfer of securities in the receiving company. The term "branch of activity" is to be understood as meaning all the assets and liabilities of a division of the company which, from an organisational point of view, constitute an independent business, that is to say, an entity capable of functioning by its own means'.

6. According to the particulars provided by the referring court, the taxation rules laid

down by Article 15(d) of the Fusionsskattelov which apply to transfers of assets, 'mean that such an operation — in accordance with the substantive rules contained in the merger taxation directive — can be implemented without capital gains tax being charged, since the receiving company inherits the tax situation of the transferring company'.

7. The referring court also points out that it is apparent from the preparatory documents to the Fusionsskattelov that

'The draft Law seeks to incorporate into Danish tax legislation those changes which are required in order to comply with the merger directive.

The draft Law also seeks to lay down rules corresponding to those of the merger directive which apply to mergers, transfers of assets and exchanges of shares regarding companies which are all established in Denmark.

...

The term "transfer of assets" is defined in Article 15(c)(2) in the same manner as in Article 2(c) of the merger directive. The term "branch of activity" is given the same definition as in Article 2(i) of the merger directive'.

Facts of the case and questions referred for a preliminary ruling

8. From the order for reference, it is apparent that Randers Sport A/S, a limited company having a share capital of DKK 300 000, the applicant in the main action, operated a wholesale and retail business in sports equipment. In 1996, with a view to introducing a generation change in the management of this company — which was to be achieved, *inter alia*, by appointing two of its associates to the Board of Directors — the shareholders of Randers Sport decided to transfer their shares to a new company, namely Randers Sport Nyt A/S, whose shareholders would include, in addition to the Randers Sport company itself, the two associates mentioned above.

9. The specific object of forming the Randers Sport Nyt company was to isolate the capital accumulated by the applicant company over the years, and to enable the two associates referred to above to acquire, for a minor consideration, sizeable blocks of shares in the new company, with low capitalisation. For this purpose, Randers Sport had taken out a sizeable loan in the amount of DKK 10 million, on the understanding that the sum loaned would remain with this company, whilst the liability for the loan debt would be transferred to

Randers Sport Nyt, which would involve a considerable reduction in the value of the recipient company. In order to provide the funds necessary for its own business activity, the recipient company obtained working capital from a bank which in turn required, by way of security, a lien on the shares of that company. This complex operation also provided that, in addition to the amount loaned, the transferring company would also retain a small block of shares in a third company, which at that time was in the process of liquidation.

10. By letter dated 6 June 1996, the applicant company applied to the *Ligningsråd* (highest administrative authority in Denmark competent to settle various issues of taxation law) for authorisation to carry out the planned transfer of shares with the benefit of the tax exemption laid down in Article 15(c) and (d) of the Fusionsskattelov. By letter of 20 November 1996, the *Ligningsråd* replied that the operation in question could qualify as a 'transfer of shares' within the meaning of this provision, and be exempted from the relevant capital gains tax, subject to the following conditions:

(i) the amount loaned and the corresponding debt liability should remain with the transferring company, or alternatively be transferred together to the recipient company, and

(ii) no security in the form of a guarantee, lien, deposit or similar provision could be made available to the recipient company by the transferring company, its principal shareholders or any third parties.

11. Clarifying the reasons for its decision, the *Ligningsråd* explained, with regard to the first condition, that the connection between the asset (i.e. the amount loaned) and the liability (i.e. the obligation to repay the loan) in question was such that they could not be shared among the transferring and the recipient company. The *Ligningsråd* also explained that the second condition sought to ensure that the recipient company was capable of operating with its own resources.

12. Although it challenged the decision of the *Ligningsråd*, Randers Sport carried out the planned transfer in accordance with the conditions laid down by that administrative authority. However, on 15 March 1997, it brought before the Vestre Landsret an action against the *Skatteministerium* (Ministry of Finance), in order to have the conditions imposed by the *Ligningsråd* declared unlawful, inasmuch as these conditions were, in its opinion, based on a mistaken interpretation of the term 'transfer of assets' contained in Directive 90/434. In its defence statement, the defendant challenged the admissibility of the action, arguing that the applicant company had no legal interest in the outcome of the case, since it had acted in accordance with the conditions stipulated by the *Ligningsråd*. By order of 27 March 1998, this plea was dismissed. However, the Vestre Landsret, in view of its fundamental uncer-

tainties on the interpretation of Directive 90/434, stayed proceedings in this case and referred to the Court of Justice the following questions for a preliminary ruling:

'(1) Must the provisions of Directive 90/434/EEC (the merger directive) be understood as meaning that it is contrary to the provisions of that directive, in particular Article 2(c) and (i) thereof, for the authorities of a Member State to refuse to treat an arrangement as being covered by the directive's provisions on the transfer of assets where the effect of the arrangement in question is that all of the transferring company's assets and liabilities are transferred to a second company (the receiving company) with the exception of a minor block of shares and the proceeds of a loan taken out by the transferring company?

(2) Does it have any bearing on the answer to Question 1 that it can be assumed that the transferring company took out the loan in question with a view to reducing the net value of the assets and liabilities to be transferred to the receiving company, inasmuch as the loaned proceeds are to remain in the transferring company while the debt liability is transferred to the receiving company?

(3) Does it have any bearing on the answer to Question 1 and/or Question 2 that it can be assumed that the loan in question was taken out with a view to making it possible for previous associates, as a step in a generation change within the undertaking, to finance the subscription of shares in the receiving company?

(4) Must the provisions of the merger taxation directive, in particular Article 2(i) thereof, be understood as meaning that it is contrary to those provisions for a condition to be imposed, before an arrangement can be treated as being covered by the asset-transfer provisions of the directive, under which the transferring company, the principal shareholders in person or any other third party may not provide security for the benefit of the receiving company, on the ground that it is indicated that the future cash requirements of the receiving company are to be financed by working credit from a financial institution which wishes to obtain a lien on the shares of the receiving company?'

13. The following participated in the proceedings before the Court: the parties to the main action, the Netherlands Government, and the Commission, which presented their submissions both in writing and orally in the course of the hearing.

Legal analysis

The question of admissibility

14. Even though neither party has challenged the admissibility of this reference for a preliminary ruling, I must nevertheless observe that, in the main action, it is only the national rules contained in the Fusionsskattelov which are applicable, and not those of Directive 90/434, on which the questions referred to the Court are based. As has already been stated earlier, the Directive applies exclusively to mergers, divisions, transfers of assets and exchanges of shares *in which companies from two or more Member States are involved* (Article 1), whereas in the case under review the contested transfer of assets is between two Danish companies.

15. Although this aspect could prompt doubts on the admissibility of this reference, I would point out, as did the Vestre Landsret, that the Fusionsskattelov, as can be seen clearly from its preparatory documents, has incorporated Directive 90/434 into national law and, in so doing, has rendered the solutions provided by the Directive applicable to issues of a purely domestic nature. As the Commission observes, the Court has already had occasion to point out, specifically with reference to Directive 90/434, that it has 'jurisdiction under Article 177 of the Treaty to interpret Community law where the situation in question is not governed directly by Community law but the national legislature, in transposing the provisions of a directive into domestic law, has chosen to apply the same treatment to purely internal situations and to those governed by the directive, so that it has aligned its domestic legislation to Community law'. The Court also states that 'in those circumstances where, in regulating internal situations, domestic legislation adopts the same solutions as those adopted in Community law so as to provide for one single procedure in comparable situations, it is clearly in the Community interest that, in order to forestall future differences of interpretation, provisions or concepts taken from Community law should be interpreted uniformly, irrespective of the circumstances in which they are to apply'. However, the Court goes on to point out that 'in such a case, and pursuant to the allocation of judicial functions between national courts and the Court of Justice under Article 177, it is for the national court alone to assess the precise scope of that reference to Community law, the jurisdiction of the Court being confined to considering provisions of Community law only'. [3]

16. In view of this clear instruction issued by the Court in its case-law, as well as the large measure of similarity which exists between the situations in question, I do not believe that the reference made by the Vestre Landsret can be declared inadmissible.

3 — Case C-28/95 *Leur-Bloem* v *Inspecteur der Belastingsdienst/Ondernemingen Amsterdam 2*, [1997] ECR I-4161, paragraphs 32 to 34.

The first three questions

17. Turning now to the questions referred by the Danish court, I consider it appropriate to examine the first three questions jointly, given that they largely concern the same substantive issue, that is to say whether or not Article 2(c) and (i) of Directive 90/434 prevents the exemption from capital gains tax, laid down in Article 4 of that Directive, from applying where a company transfers its entire assets to another company with the exception of, on the one hand, a small block of shares and, on the other hand, the proceeds of a loan taken out by the transferring company. For the purpose of further clarification, this question also seeks to establish whether these issues are affected by the circumstance that the operation was carried out in order to reduce the net value of the transfer made, with the object of enabling a process of generation change to take place in the management of the company.

18. In order to reply to the referring court, it is necessary first of all to recall that, pursuant to the definition contained in the Directive itself, a transfer of assets consists in 'an operation whereby a company transfers without being dissolved all or one or more branches of its activity to another company in exchange for the transfer of securities representing the capital of the company receiving the transfer' [Article 2(c)].

19. Therefore, for a transfer of assets to take place, three conditions need to be met:

— the transferring company may not have been dissolved,

— the transfer must concern all or one or more branches of the activity of the transferring company, and

— the transferring company must acquire, in exchange for this transfer, securities representing the capital of the recipient company.

20. In relation to the case under review, the first condition does not give rise to any particular problem, since there is no doubt that the transferring company has not been dissolved. However, a more difficult issue here is to ascertain whether all or one or more branches of the company's activity have actually been transferred to the recipient company.

21. According to the applicant in the main action, a transfer of the entire business of a company occurs whenever the assets and liabilities transferred to the recipient com-

pany constitute an independent business entity capable of functioning with its own measures. For this purpose it is of no relevance that certain assets, in this particular case the amount loaned, remain within the transferring company. To rule otherwise, claims the applicant, would militate against the rationale behind the directive, which seeks to promote the operations in question by removing as many as possible of the fiscal restrictions imposed by the Member States' laws. The other parties, on the other hand, consider that the condition in question is not met where a unit containing both assets and liabilities, such as specifically the loan taken out by Randers Sport, has been artificially divided between the transferring and the recipient company.

22. The latter argument appears to me to carry greater conviction. Article 2(i) of the Directive provides that, for a branch of activity to be transferred, such transfer must involve '*all the assets and liabilities* of a division of a company which from an organisational point of view constitute an independent business, that is to say an entity capable of functioning by its own means' (emphasis added). Thus the Community legislature considers it necessary in that regard that those assets and liabilities attached to a particular activity displaying certain characteristics of independence, be transferred in their entirety. Therefore if a particular asset attached to such activity failed to be transferred, the operation in question could not be regarded as a transfer of a branch of activity within the meaning of Article 2 of the Directive, and consequently the transfer of a branch of activity within the meaning of Article 2 of the Directive could not warrant the transfer of a liability attached to a separate activity which has remained within the transferring company.

23. Against this submission, the applicant in the main action argues that in the case under review, there occurred a transfer, not of a branch of activity, but of the entire activity of the transferring company, which is why it is not specifically necessary for 'all the assets and liabilities' to be transferred. However, I would observe that if this condition is stipulated for the transfer of a branch of activity, this must be even more the case where the operation in question concerns the entire activity of the transferring company. In fact I would say that if this condition has not been specifically stipulated in respect of the latter, it is precisely because that condition is taken as read.

24. However, quite apart from this aspect, I am not persuaded that the case under review concerns the transfer of the entire activity of the transferring company. The loan, which was for a considerable amount (30 times greater than the value of the company capital) was taken out before the transfer took place, on the understanding that the amount in question should remain as part of the company's assets. It is clear that this amount was intended neither to finance the distribution of sporting equipment, an activity subsequently transferred to Randers Sport Nyt, nor to be allocated

to the shareholders in the form of a benefit — in which case it would obviously have been subject to normal taxation. Whatever may have been the purpose for which the amount loaned was intended, even if this purpose was merely financial, this sum was definitely intended for a different activity from that transferred to the recipient company, and therefore constituted, at least potentially, a separate branch of activity remaining with the transferring company. Therefore, in the case under review, it cannot be claimed that the entire activity of Randers Sport was to be transferred to the receiving company. On the contrary, the incongruous nature of the operation in question is evidenced precisely by the fact that the recipient company was to acquire the activity of marketing the sports equipment, together with the obligation to repay a sum intended for a different activity which, cleared of the liability relating to it, was to remain with the transferring company.

25. Accordingly, the specific characteristics of the operation under review lead me to dismiss the notion that it constitutes a transfer of activity within the meaning of Article 2 of the Directive, more particularly where the asset and the liability of the debt contracted by the transferring company were to be allocated between the latter and the recipient company. I would add that, in my view, this conclusion is supported by the structural and objective characteristics of the operation, irrespective of the objective pursued by the latter. In this regard, therefore, it is irrelevant that the operation was to be carried out for the purpose of reducing the value of the activity transferred to Randers Sport Nyt in order to enable a generation change to take place.

26. For the sake of completeness, I would also point out that, according to the Commission, the case under review also failed to meet the third condition under Article 2 of the Directive, namely the condition that the transfer must be carried out in exchange for the transfer of securities representing the capital of the recipient company. The Commission considers that, in the case under review, the recipient company, in exchange for the transfer, should have taken over the liability attached to the loan taken out by the transferring company; therefore the operation in question was in reality a sale of some description and would not as such come within the terms of the definition in Article 2 of the Directive. However, it seems to me that the Commission has overlooked the fact that, in exchange for the various assets and liabilities transferred to Randers Sport Nyt, Randers Sport was obliged to acquire shares exclusively in the recipient company. In those circumstances I cannot see what could constitute the sale and purchase to which the Commission refers.

27. Finally, before reaching my conclusion on the first three questions referred, I should mention the circumstance — which has been highlighted by the referring court — that the transferring company retained a small block of shares in a third company. I do so in order to assess whether this circumstance could affect the question whether the operation under review could qualify as a transfer of assets within the meaning of Article 2 of the Directive. However, on this issue I would confine myself to the observation that, whilst the fact that the transferring company retains a

shareholding could be sufficient to exclude the possibility of the entire activity of that company being transferred to the recipient company, the same cannot be said of the transfer of a branch of activity which is entirely separate from the said shareholding.

28. In conclusion, I propose that the reply to the first three questions should be that there is no transfer of assets within the meaning of Article 2(c) and (i) of Directive 90/434 in the case of an operation under which the transferring company retains the proceeds of a loan taken out by it and the liabilities attached to this loan are transferred to the recipient company, and that this is so regardless of the object pursued by this allocation of the assets and liabilities of the loan. However, there may be a transfer of assets within the meaning of Article 2(c) and (i) of the Directive where, on a transfer of a branch of activity, the transferring company retains an independent shareholding in a third company.

The fourth question

29. By its fourth question, the referring court is in effect seeking to establish whether Article 2(c) and (i) of Directive 90/434 allows the appropriate authorities of the Member States to decide that the exemption from capital gains tax laid down in Article 4 of the Directive does not apply where the transferring company or third parties provide a surety in favour of the recipient company, which could cast doubt on the independence of the recipient company.

30. All the parties seem substantially to agree that, under Article 2 of the Directive, the company receiving the transfer must be commercially independent and must be capable of operating by its own means. However, their opinions differ in relation to the case under review, essentially because they make a different assessment of the conditions imposed in this regard by the *Ligningsråd*.

31. More particularly, the Danish Government has justified the imposition of this condition on the grounds that, in its view, the fact that the transferring company had to grant a lien over the shares of the recipient company in order to guarantee the working capital obtained by the latter is evidence of its inability to function by its own means. In the same vein, but without reaching a specific conclusion on the condition imposed by the *Ligningsråd*, the Netherlands Government maintains that the notion that the recipient company is operating independently must be dismissed where, because of the terms on which the transfer was made (including the existence of a considerable liability remaining with the recipient company), the latter is incapable of operating without a guarantee provided by the transferring company which enables it to obtain working capital. The applicant company in the main action and the Commission, on the other hand, accuse the *Ligningsråd* of having imposed the conditions in absolute terms, without

specifically seeking to ascertain the actual degree of independence of the recipient company.

32. For my part, I am also of the view that the receiving company must be independent of the transferring company and have sufficient means to enable it to carry on its own business, if necessary by obtaining a loan under normal market conditions. This is expressly provided for by Article 2(i) of the Directive in relation to the transfer of a branch of activity, which, as has already been mentioned, must be an 'entity capable of operating by its own means'. However, the same conclusion should be reached — in fact, all the more so — where the entire activity of a company is being transferred. Nevertheless, I agree with the applicant in the main action, the Commission and the Netherlands Government that for this purpose, the national authorities should make an assessment on a case-by-case basis, in order to take into account the circumstances of each individual case. More particularly where the recipient company guarantees a loan taken out by the transferring company, the national authorities must assess whether such a guarantee is essential in order to enable the recipient company to carry on its own activity. If the answer to this question is in the affirmative, the conclusion must be that this company is not capable of operating by its own means and that, as a result, the operation cannot be regarded as a transfer of assets within the meaning of Article 2(c) and (i) of the Directive.

33. The question whether such an assessment has actually been carried out by the *Ligningsråd* and whether the conclusion reached by the latter is correct, are issues which must be decided by the referring court in the light of the circumstances of this particular case. As regards the issues that concern us here, I would confine myself to pointing out that, for the purpose of making this assessment, it may be important to establish whether, under the relevant national legislation, the action taken by the transferring company — which granted a lien over the shares of the recipient company in order to enable the latter to obtain working capital — renders it liable to the lending bank. If this were to be indeed the case, this could give rise to the conclusion that, had such action not been taken, the recipient company would not have been able to obtain on the market the funds necessary for it to carry on its own day-to-day business activity. However, I would repeat that it is for the referring court to address this issue.

34. In conclusion, I would propose that the reply to the fourth question should be that where there is a transfer of assets within the meaning of Article 2(c) and (i) of Directive 90/434, the recipient company must be independent of the transferring company, and have adequate means for the purpose of conducting its own business activity — where appropriate by taking out a loan under normal market conditions. Where the recipient company guarantees a loan taken out by the recipient company, the national authorities must assess whether such a guarantee is essential in order to enable the recipient company to carry on its own activity. If the answer to this question is in the affirmative, the conclusion must be that the latter company is not capable of functioning by its own means.

Conclusion

In the light of the foregoing, I propose that the four questions referred by the Vestre Landsret be answered as follows:

There is no transfer of assets within the meaning of Article 2(c) and (i) of Directive 90/434 where the arrangement in question envisages that the transferring company is to retain the proceeds of a loan taken out by the latter and that the liabilities relating thereto are to be transferred to the recipient company; this is so regardless of the objective pursued by this allocation of assets and liabilities attached to such loan. However, there may be a transfer of assets, within the meaning of Article 2(c) and (i) of the directive, where, in the event of the transfer of a branch of activity, the transferring company retains an independent shareholding in a third company.

For there to be a transfer of assets within the meaning of Article 2(c) and (i) of Directive 90/434, the receiving company must be independent of the transferring company and have adequate means enabling it to carry on its own business activity — where appropriate by taking out a loan under normal market conditions. Where the transferring company guarantees a loan taken out by the recipient company, the national authorities must assess whether this guarantee is essential for the purpose of enabling the recipient company to carry on its own activity. If the answer to this question is in the affirmative, the conclusion must be that the latter is not capable of functioning by its own means.