Reports of Cases

JUDGMENT OF THE COURT (Fifth Chamber)

24 February 2022 *

(Reference for a preliminary ruling – Taxation – Withholding tax on notional interest on an interest-free loan granted to a resident subsidiary by a non-resident parent company – Directive 2003/49/EC – Payments of interest between associated companies of different Member States – Article 1(1) – Exemption from withholding tax – Article 4(1)(d) – Exclusion of certain payments – Directive 2011/96/EU – Corporation tax – Article 1(1)(b) – Distribution of profits by a resident subsidiary to its non-resident parent company – Article 5 – Exemption from withholding tax – Directive 2008/7/EC – Raising of capital – Article 3 – Contributions of capital – Article 5(1)(a) – Indirect tax exemption – Articles 63 and 65 TFEU – Free movement of capital – Taxation of the gross amount of notional interest – Recovery procedure for the purposes of the deduction of expenses related to the grant of the loan and a possible refund – Difference in treatment – Justification – Balanced allocation of the power to impose taxes between the Member States – Effective collection of tax – Combating of tax avoidance)

In Case C-257/20,

REQUEST for a preliminary ruling under Article 267 TFEU from the Varhoven administrativen sad (Supreme Administrative Court, Bulgaria), made by decision of 4 May 2020, received at the Court on 9 June 2020, in the proceedings

'Viva Telecom Bulgaria' EOOD

v

Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' – Sofia,

intervener:

Varhovna administrativna prokuratura na Republika Bulgaria,

THE COURT (Fifth Chamber),

composed of E. Regan (Rapporteur), President of the Chamber, K. Lenaerts, President of the Court, acting as Judge of the Fifth Chamber, C. Lycourgos, President of the Fourth Chamber, I. Jarukaitis and M. Ilešič, Judges,

Advocate General: A. Rantos,

Registrar: M. Ferreira, Principal Administrator,

* Language of the case: Bulgarian.

having regard to the written procedure and further to the hearing on 30 June 2021,

after considering the observations submitted on behalf of:

– 'Viva Telecom Bulgaria' EOOD, represented initially by D. Yordanov, M. Emanuilov and S. Hristozova-Yordanova, and subsequently by Y. Kamburov, E. Emanuilov, V. Rangelov, T. Todorov and D. Dimitrova, advokati,

– the Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' – Sofia, by N. Kalistratov and M. Bakalova, acting as Agents,

– the Bulgarian Government, by T. Tsingileva and L. Zaharieva, acting as Agents,

– the European Commission, by W. Roels and Y. Marinova, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 30 September 2021,

gives the following

Judgment

1 This request for a preliminary ruling concerns the interpretation of Article 5(4) and Article 12(b) TEU, Article 47 of the Charter of Fundamental Rights of the European Union ('the Charter'), Articles 49 and 63 TFEU, Article 4(1)(d) of 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 (OJ 2003 L 157, p. 49), Article 1(1)(b) and (3) and Article 5 of 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 (OJ 2011 L 345, p. 8), as amended by Council Directive (EU) 2015/121 of 27 January 2015 (OJ 2015 L 21, p. 1) ('Directive 2011/96'), Article 3(h) to (j), Article 5(1)(a) and (b), Article 7(1) and Article 8 of Council Directive 2008/7/EC of 12 February 2008 concerning indirect taxes on the raising of capital (OJ 2008 L 46, p. 11), Annex VI, Section 6, point 3 to the Protocol concerning the conditions and arrangements for admission of the Republic of Bulgaria and Romania to the European Union (OJ 2005 L 157, p. 29)('the Admission Protocol') and Annex VI, Section 6, point 3 to the Act concerning the conditions of accession of the Republic of Bulgaria and Romania and the adjustments to the Treaties on which the European Union is founded (OJ 2005 L 157, p. 203)('the Act of Accession').

2 The request has been made in proceedings between 'Viva Telecom Bulgaria' EOOD, a company established in Sofia (Bulgaria), and the Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' – Sofia (Director of the 'Tax and Social Security Appeals and Practice' Directorate of Sofia, Bulgaria) concerning the taxation, by means of a withholding tax, of notional interest on an interest-free loan granted to Viva Telecom Bulgaria by its parent company established in another Member State.

Legal context

European Union law

Accession of the Republic of Bulgaria to the European Union

3 Article 20 of the Admission Protocol and Article 23 of the Act of Accession, concerning transitional measures, provide that the measures listed in the respective Annex VI to that protocol and to that act are to apply to the Republic of Bulgaria under the conditions laid down in those annexes.

4 Those annexes, entitled 'List referred to in Article 20 of the Protocol: transitional measures, Bulgaria' and 'List referred to in Article 23 of the Act of Accession: Transitional provisions, Bulgaria', respectively, refer, in point 3 of Section 6, headed 'Taxation', to Directive 2003/49, as amended by Council Directive 2004/76/EC of 29 April 2004 (OJ 2004 L 157, p. 106), and state, in the same terms, as follows:

'Bulgaria shall be authorised not to apply the provisions of Article 1 of [Directive 2003/49] until 31 December 2014. During that transitional period, the rate of tax on payments of interest or royalties made to an associated company of another Member State or to a permanent establishment situated in another Member State of an associated company of a Member State must not exceed 10% until 31 December 2010 and must not exceed 5% for the following years until 31 December 2014.'

Directive 2003/49

5 Recitals 1 to 4 of Directive 2003/49 are worded as follows:

'(1) In a Single Market having the characteristics of a domestic market, transactions between companies of different Member States should not be subject to less favourable tax conditions than those applicable to the same transactions carried out between companies of the same Member State.

(2) This requirement is not currently met as regards interest and royalty payments; national tax laws coupled, where applicable, with bilateral or multilateral agreements may not always ensure that double taxation is eliminated, and their application often entails burdensome administrative formalities and cash-flow problems for the companies concerned.

(3) It is necessary to ensure that interest and royalty payments are subject to tax once in a Member State.

(4) The abolition of taxation on interest and royalty payments in the Member State where they arise, whether collected by deduction at source or by assessment, is the most appropriate means of eliminating the aforementioned formalities and problems and of ensuring the equality of tax treatment as between national and cross-border transactions; it is particularly necessary to abolish such taxes in respect of such payments made between associated companies of different Member States as well as between permanent establishments of such companies.'

6 Article 1 of that directive, entitled ‘Scope and procedure’, provides:

‘1. Interest or royalty payments arising in a Member State shall be exempt from any taxes imposed on those payments in that State, whether by deduction at source or by assessment, provided that the beneficial owner of the interest or royalties is a company of another Member State or a permanent establishment situated in another Member State of a company of a Member State.

2. A payment made by a company of a Member State or by a permanent establishment situated in another Member State shall be deemed to arise in that Member State, hereafter referred to as the “source State”.

…

4. A company of a Member State shall be treated as the beneficial owner of interest or royalties only if it receives those payments for its own benefit and not as an intermediary, such as an agent, trustee or authorised signatory, for some other person.

…’

7 Article 2 of that directive, entitled ‘Definition of interest and royalties’, provides as follows:

‘For the purposes of this Directive:

(a) the term “interest” means income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor’s profits, and in particular, income from securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures; penalty charges for late payment shall not be regarded as interest;

…’

8 Article 4 of that directive, entitled ‘Exclusion of certain payments as interest or royalties’, provides:

‘1. The source State shall not be obliged to ensure the benefits of this Directive in the following cases:

(a) payments which are treated as a distribution of profits or as a repayment of capital under the law of the source State;

…

(d) payments from debt-claims which contain no provision for repayment of the principal amount or where the repayment is due more than 50 years after the date of issue.

2. Where, by reason of a special relationship between the payer and the beneficial owner of interest or royalties, or between one of them and some other person, the amount of the interest or royalties exceeds the amount which would have been agreed by the payer and the beneficial owner in the absence of such a relationship, the provisions of this Directive shall apply only to the latter amount, if any.’

Directive 2008/7

9 Article 3 of Directive 2008/7, entitled 'Contributions of capital', lays down:

'For the purposes of this Directive and subject to Article 4, the following transactions shall be considered to be "contributions of capital":

…

(h) an increase in the assets of a capital company through the provision of services by a member which does not entail an increase in the company's capital, but which does result in a variation in the rights in the company or which may increase the value of the company's shares;

(i) a loan taken up by a capital company, if the creditor is entitled to a share in the profits of the company;

(j) a loan taken up by a capital company with a member or a member's spouse or child, or a loan taken up with a third party, if it is guaranteed by a member, on condition that such loans have the same function as an increase in the company's capital.'

10 Article 5 of that directive, entitled 'Transactions not subject to indirect tax', provides in paragraph 1 thereof:

'Member States shall not subject capital companies to any form of indirect tax whatsoever in respect of the following:

(a) contributions of capital;

(b) loans, or the provision of services, occurring as part of contributions of capital;

…'

Directive 2011/96

11 Recitals 3 to 6 of Directive 2011/96 are worded as follows:

'(3) The objective of this Directive is to exempt dividends and other profit distributions paid by subsidiary companies to their parent companies from withholding taxes and to eliminate double taxation of such income at the level of the parent company.

(4) The grouping together of companies of different Member States may be necessary in order to create within the Union conditions analogous to those of an internal market and in order thus to ensure the effective functioning of such an internal market. Such operations should not to be hampered by restrictions, disadvantages or distortions arising in particular from the tax provisions of the Member States. It is therefore necessary, with respect to such grouping together of companies of different Member States, to provide for tax rules which are neutral from the point of view of competition, in order to allow enterprises to adapt to the requirements of the internal market, to increase their productivity and to improve their competitive strength at the international level.

(5) Such grouping together may result in the formation of groups of parent companies and subsidiaries.

(6) Before the entry into force of [Council] Directive 90/435/EEC [of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (OJ 1990 L 225, p. 6),] the tax provisions governing the relations between parent companies and subsidiaries of different Member States varied appreciably from one Member State to another and were generally less advantageous than those applicable to parent companies and subsidiaries of the same Member State. Cooperation between companies of different Member States was thereby disadvantaged in comparison with cooperation between companies of the same Member State. It was necessary to eliminate that disadvantage by the introduction of a common system in order to facilitate the grouping together of companies at Union level.'

12 Under Article 1(1) of Directive 2011/96:

'Each Member State shall apply this Directive:

…

(b) to distributions of profits by companies of that Member State to companies of other Member States of which they are subsidiaries;

…'

13 Article 5 of that directive is worded as follows:

'Profits which a subsidiary distributes to its parent company shall be exempt from withholding tax.'

Bulgarian law

14 Article 1(4) of the Zakon za korporativnoto podohodno oblagane (Law on Corporation Tax, DV No 105 of 22 December 2006), in force since 1 January 2007 ('the ZKPO'), provides:

'This law governs the taxation of income falling within its scope received in the Republic of Bulgaria by resident or non-resident legal persons.'

15 According to Article 5(1) and (2) of the ZKPO:

'1. Profits shall be subject to corporation tax.

2. The income of resident or non-resident legal persons falling within the scope of this law shall be subject to a tax that is deducted at source.'

16 Article 12(5) of the ZKPO states:

‘The following income shall be deemed to be from a domestic source where it is granted by resident legal persons, resident individual traders or non-resident legal persons or non-resident individual traders by means of a permanent establishment or a specific place of business on domestic territory, or where it is paid to non-resident legal persons by resident natural persons or by non-resident natural persons with a specific place of business:

(1) interest, including interest incorporated into lease repayments.

…’

17 Article 16 of the ZKPO, entitled ‘Tax avoidance’, in the version in force from 1 January 2010, provides:

‘1. … Where one or more transactions, including between unrelated persons, are concluded on terms that give rise to tax avoidance, those transactions, certain of their terms and their legal form shall be disregarded for the purpose of determining the basis of assessment, and the basis of assessment that would have been obtained if a similar transaction had been carried out in the normal course of business at arm’s length and which is designed to achieve the same financial result without giving rise to tax avoidance shall apply.

2. The following shall also be regarded as tax avoidance:

…

(3) Borrowing or lending at an interest rate that diverges from the market interest rate at the time of conclusion of the transaction, including interest-free loans or other temporary financial assistance provided free of charge and the cancellation of loans or the repayment of non-business loans on one’s own account;

…’

18 Article 20 of the ZKPO, entitled ‘Tax rate’, provides:

‘The rate of corporation tax shall be 10%.’

19 Article 195 of the ZKPO, entitled ‘Withholding tax in respect of non-residents’, provides, in the version in force since 1 January 2015:

‘1. … Income received by non-resident legal persons from domestic sources … shall be subject to a withholding tax which extinguishes the tax debt.

2. … The withholding tax provided for in paragraph 1 shall be retained by resident legal persons … paying income to non-resident legal persons …

…

6. … The following shall not be subject to withholding tax:

…

(3) Income deriving from interest, copyright royalties and licence fees, under the conditions laid down in paragraphs 7 to 12;

…

7. … Income deriving from interest, copyright royalties and licence fees shall not be subject to withholding tax where the following conditions are satisfied simultaneously:

…

11. … Paragraphs 7, 8, 9 and 10 shall not apply to:

(1) income constituting a distribution of profits or a repayment of capital;

…

(4) income from debt-claims which contain no provision for repayment of the principal amount or where the repayment is due more than 50 years after the date of issue of the debt;

…

(7) income from transactions for which the principal reason or one of the principal reasons is tax avoidance or tax elimination.'

20 Article 199 of the ZKPO, entitled 'Basis of assessment for withholding tax on non-residents' income', states in paragraph 1 thereof:

'The basis of assessment for determining withholding tax on the income referred to in Article 195(1) shall be the gross amount of that income …'

21 Article 200 of the ZKPO, entitled 'Tax rate', provided in paragraph 2 thereof, in the version in force from 1 January 2011:

'… The rate of income tax referred to in Article 195 shall be 10%, except in the cases referred to in Article 200a.'

22 With effect from 1 January 2015, that provision was amended as follows:

'… The rate of income tax referred to in Article 195 shall be 10%.'

23 Article 200a of the ZKPO, in the version in force from 1 January 2011, as amended and supplemented as of 1 January 2014, provided, until its repeal with effect from 1 January 2015:

'1. … The rate of tax on income from interest, copyright royalties and licence fees shall be 5% where the following conditions are satisfied simultaneously;

…

5. Paragraphs 1 to 4 shall not apply to:

…

(1) income constituting a distribution of profits or a repayment of capital;

…

(4) income from debt-claims which contain no provision for repayment of the principal amount or where the repayment is due more than 50 years after the date of issue of the debt;

…’

24 Article 202a of the ZKPO, entitled ‘Recalculation of withholding tax’, in the version in force from 1 January 2010, provided, in paragraphs 1 to 4:

‘1. … A non-resident legal person which is resident for tax purposes in a Member State of the European Union or in another State which is a party to the Agreement on the European Economic Area of 2 May 1992 [(OJ 1994 L 1, p. 3)] shall be entitled to opt for the recalculation of withholding tax in respect of the income referred to in Article 12(2), (3), (5) and (8). Where the non-resident person opts for the recalculation of withholding tax, that recalculation shall include all the income referred to in Article 12(2), (3), (5) and (8) which the non-resident person has received during the financial year.

2. Where the non-resident person opts for the recalculation of withholding tax in respect of the income which it receives, the recalculated tax shall be equivalent to the corporation tax which would have been payable on that income if it had been received by a resident legal person. Where the non-resident person has incurred expenditure related to income within the meaning of the first sentence on which expenditure tax would have been payable if such expenditure had been incurred by a resident legal person, the amount of recalculated tax shall be increased by that tax.

3. Where the amount of the withholding tax provided for in Article 195(1) exceeds the amount of tax recalculated in accordance with paragraph 2, the difference shall be repaid up to the amount of the withholding tax provided for in Article 195(1), which may not be deducted by the non-resident person from the tax payable in the State of residence.

4. The annual tax return filed shall indicate whether the option for the recalculation of withholding tax was exercised. The non-resident person shall file its tax return at the Teritorialna direktsia na Natsionalna agentsia za prihodite – Sofia [(Regional Directorate of the National Revenue Agency for the City of Sofia, Bulgaria)] by 31 December of the year following that in which the income was received.’

The dispute in the main proceedings and the questions referred for a preliminary ruling

25 On 22 November 2013, ‘Viva Telecom Bulgaria’ EAD, the predecessor of ‘Viva Telecom Bulgaria’ EOOD, concluded, as borrower, a loan agreement with its sole shareholder, InterV Investment Sàrl, a company established in Luxembourg, in which the latter, as lender, granted it an interest-free convertible loan scheduled to mature 60 years after the date of entry into force of that agreement. That agreement provided that the borrower’s obligation to repay the loan would be

extinguished at any time after the date of disbursement if the borrower decided to make a contribution in kind of the outstanding amount of the loan to its capital, in compliance with the conditions set out in that agreement.

26 By decision of 16 October 2017, the Teritorialna direktsia na Natsionalnata agentive za prihodite (Regional Directorate of the National Revenue Agency, Bulgaria) ('the tax authorities') made a tax adjustment in respect of Viva Telecom Bulgaria, ordering it, under Article 195 of the ZKPO, to pay withholding tax in relation to the loan granted to it by InterV Investment, concerning the period from 14 February 2014 to 31 March 2015.

27 Having established that, at the time of the tax inspection, the loan had not been converted into capital and the borrower had neither repaid that loan nor paid interest, the tax authorities found that there was a transaction giving rise to tax avoidance within the meaning of Article 16(2), point 3, of the ZKPO. In its decision, the tax authority established the market interest rate to be applied to that loan in order to calculate the interest not paid by the borrower before making a deduction at source of 10% on that loan.

28 On 20 December 2017, the defendant in the main proceedings rejected the complaint made by Viva Telecom Bulgaria against that decision.

29 By judgment of 29 March 2019, the Administrativen sad Sofia (Administrative Court, Sofia, Bulgaria), hearing an action brought by that company challenging the legality of the decision of 16 October 2017, dismissed that action on the ground that the loan at issue in the main proceedings was a financial asset of that company which generated a profit as a result of the non-payment of interest, whereas the lender had, for its part, suffered economic loss as a result of the non-collection of that interest. According to that court, the amount borrowed was used to repay a number of the borrower's financial obligations set out in the loan agreement and was not therefore part of its equity.

30 Viva Telecom Bulgaria brought an appeal on a point of law before the Varhoven administrativen sad (Supreme Administrative Court, Bulgaria) seeking to have that judgment set aside.

31 In support of that appeal, that company claims that the withholding tax was levied on notional interest income without taking account of the proven existence of a commercial interest in granting an interest-free loan. It also maintains that it did not have the funds to pay the interest on the loan at issue in the main proceedings and that InterV Investment was the sole owner of the capital on the date of conclusion of the loan agreement. Furthermore, it submitted that Article 16(2), point 3, of the ZKPO was contrary to the case-law of the Court since it denies parties to an interest-free loan the opportunity to prove that there were sound economic reasons for the grant of the loan.

32 In the alternative, Viva Telecom Bulgaria submits that since the Republic of Bulgaria had exercised the option referred to in Article 4(1)(d) of Directive 2003/49, allowing Member States to exclude from the scope of that directive interest on loans which they treat for tax purposes as income from capital instruments, Directive 2011/96, which concerns income of that type, is applicable. Under Article 5 of that directive, profits which a resident subsidiary distributes to its non-resident parent company are to be exempt from withholding tax. It also claims that the loan at issue in the main proceedings was a contribution of capital within the meaning of Article 3(h) to (j) of Directive 2008/7, which, in accordance with Article 5 thereof, should not be subject to any indirect tax.

33 The Varhoven administrativen sad (Supreme Administrative Court) asks, in the first place, whether Article 16(2), point (3) of the ZKPO complies with the principle of proportionality, referred to in Article 5(4) and Article 12(b) TEU, and with the right to an effective remedy enshrined in Article 47 of the Charter. That national provision lays down an irrebuttable presumption of tax avoidance in the case of the grant of an interest-free loan, regardless of whether or not that loan is between related persons, without the lender or borrower being able to rebut that presumption. In the case of related companies, economic considerations relating to the interests of the group concerned could justify the conclusion of such a loan.

34 In the second place, the referring court raises the question of the scope of Directives 2003/49 and 2011/96. In accordance with Article 4(1)(d) of Directive 2003/49, implemented by the Republic of Bulgaria, before 1 January 2015, in essence, in Article 200a(1) and (5), point (4) of the ZKPO and, after that date, in Article 195(6), point 3 and Article 195(11), point 4 of the ZKPO, the source Member State is not obliged to ensure the benefits of that directive in the case of payments from debt-claims which contain no provision for repayment of the principal amount or where the repayment is due more than 50 years after the date of issue. Therefore, the question arises whether such payments must be regarded as a distribution of profits which, since it is made by a resident subsidiary to its non-resident parent company, should, pursuant to Articles 1 and 5 of Directive 2011/96, be exempt from withholding tax.

35 In the third place, that court asks whether the grant of an interest-free loan to a resident company by a non-resident company subject to the application, as from 1 January 2010, of withholding tax under Article 16(2), point 3 and Article 195 of the ZKPO must be regarded as a contribution of capital within the meaning of Article 3(h) to (j) of Directive 2008/7, which should therefore be subject to the provisions of that directive, in particular Article 5(1)(a) and (b) and Article 7(1) and Article 8 thereof.

36 In the fourth and last place, that court raises the question of the effect of the transitional measures in the Admission Protocol and the Act of Accession, the provisions of which set out in their respective Annex VI, Section 6, point 3 lay down that Bulgaria was authorised not to apply Article 1 of Directive 2003/49 until 31 December 2014, while stating that, during that transitional period, the tax rate on interest payments made, inter alia, to an associated company of another Member State could not exceed 5% between 31 December 2010 and 31 December 2014. Article 200(2) and Article 200a(1) and (5), point 4 of the ZKPO, in the version in force in 2014, are contrary to those provisions, since they provided for a withholding tax of 10%.

37 In those circumstances the Varhoven administrativen sad (Supreme Administrative Court) decided to stay the proceedings and to refer the following questions to the Court of Justice for a preliminary ruling:

‘(1) Does national legislation such as that enacted in Article 16(2), point 3, of [the ZKPO] conflict with the principle of proportionality enshrined in Article 5(4) and Article 12(b) [TEU] and the right to an effective remedy and to a fair trial enshrined in Article 47 of the [Charter]?

(2) Are interest payments in accordance with Article 4(1)(d) of Directive [2003/49] profit distributions to which Article 5 of Directive [2011/96] applies?

(3) Does the rule laid down in Article 1(1)(b) and (3) and Article 5 of Directive [2011/96] apply to payments pursuant to an interest-free loan, which becomes due 60 years after the loan contract was entered into, and which is covered by Article 4(1)(d) of Directive [2003/49]?

(4) Does national legislation such as that enacted in Article 195(1)[,] Article 200(2) … and Article 200a(1) and (5), point 4, of the ZKPO (repealed), [in the version in force as from 1 January 2011 until 1 January 2015], and Article 195(1), (6), point 3, and (11), point 4, of the ZKPO, [in the version in force as from 1 January 2015], and a taxation practice according to which unpaid interest on an interest-free 60-year loan granted on 22 November 2013 to a resident subsidiary by a parent company registered in a different Member State is subject to withholding tax conflict with Article 49 and Article 63(1) and (2) [TFEU], Article 1(1)(b) and (3) and Article 5 of Directive [2011/96] and Article 4(1)(d) of Directive [2003/49]?

(5) Does national legislation such as that enacted in Article 16(1) and (2), point 3, and Article 195(1) of the ZKPO on the taxation at source of fictitious interest income on an interest-free loan granted to a resident company by a company in another Member State which is the borrower's sole shareholder conflict with Article [3(h) to (j)], Article 5(1)(a) and (b), Article 7(1) and Article 8 of [Directive 2008/7]?

(6) Does the transposition of Directive [2003/49] in Article 200(2) and Article 200a(1) and (5), point 4, of the ZKPO in 2011, that is prior to expiry of the transposition period laid down in point 3 of the section on taxation in Annex VI to the Act [of Accession], which sets a tax rate of 10% rather than the maximum rate of 5% prescribed in the Act [of Accession] and the Protocol [for Admission], infringe the principles of legal certainty and legitimate expectation?'

Consideration of the questions referred

38 By its six questions, which overlap in part, the referring court asks, in essence, about the interpretation, first, of secondary EU law resulting from Directive 2003/49 (second, third and sixth questions), Directive 2011/96 (second and fourth questions) and Directive 2008/7 (the fifth question) respectively and, second, the primary law of the European Union arising from Articles 49 and 63 TFEU (fourth question), Article 5(4) and Article 12(b) TEU respectively, and Article 47 of the Charter (first question).

Admissibility

39 The defendant in the main proceedings considers that the second to fourth questions referred for a preliminary ruling are inadmissible. Those questions relate to provisions of EU law, namely Article 4(1)(d) of Directive 2003/49, and Article 1(1)(b) and (3) and Article 5 of Directive 2011/96, which are not devoid of clarity. Furthermore, those provisions have no connection with the legal classification made by the tax authorities in the decision at issue in the main proceedings. That decision imposes a withholding tax not by virtue of the distribution of dividends or profits, for the purposes of Directive 2011/96, but of the existence of tax avoidance owing to the conclusion of an interest-free loan. Furthermore, Article 200a(3), point 4 of the ZKPO, which became, as from 1 January 2011, Article 200a(5), point 4 of the ZKPO, transposed correctly Article 4(1)(d) of Directive 2003/49.

40 The Bulgarian Government, for its part, considers that the second and third questions referred for a preliminary ruling are inadmissible because they bear no relation to the circumstances of the dispute in the main proceedings. The order for reference does not state how the interpretation of Directives 2003/49 and 2011/96 is useful for resolving that dispute.

41 It follows from settled case-law of the Court that it is solely for the national court before which the dispute has been brought, and which must assume responsibility for the subsequent judicial decision, to determine, in the light of the particular circumstances of the case, both the need for a preliminary ruling in order to enable it to deliver judgment and the relevance of the questions which it submits to the Court. Consequently, where the questions referred concern the interpretation or the validity of a rule of EU law, the Court is in principle bound to give a ruling. It follows that questions referred by national courts enjoy a presumption of relevance. The Court may refuse to rule on a question referred by a national court only where it appears that the interpretation sought bears no relation to the actual facts of the main action or its object, where the problem is hypothetical, or where the Court does not have before it the factual or legal material necessary to give a useful answer to the questions submitted to it (judgment of 16 July 2020, *Facebook Ireland and Schrems*, C-311/18, EU:C:2020:559, paragraph 73 and the case-law cited).

42 In the present case, it should be noted at the outset, as regards the claim based on the clarity of the provisions of Directives 2003/49 and 2011/96 which are the subject of the second to fourth questions, that a national court is in no way prevented from referring questions to the Court of Justice for a preliminary ruling, the answer to which, in the submission of one of the parties to the main proceedings, leaves no scope for reasonable doubt. Accordingly, even if that were the case, the reference for a preliminary ruling containing such questions does not thereby become inadmissible (judgment of 14 October 2021, *Viesgo Infraestructuras Energeticas*, C-683/19, EU:C:2021:847, paragraph 26 and the case-law cited).

43 Furthermore, there is nothing in the documents before the Court to suggest that the interpretation of Directives 2003/49 and 2011/96 that is sought bears no relation to the actual facts of the main action or its object, or that the problem is hypothetical because the decision at issue in the main proceedings did not apply the provisions in those directives or the national law is consistent with them. In its request for a preliminary ruling, the referring court set out with all the necessary clarity the reasons why it considers that the answer to the second to fourth questions concerning the interpretation of those provisions of EU law is necessary for the resolution of the dispute in the main proceedings, since the withholding tax imposed in that decision is, according to that court, capable of infringing those directives.

44 It follows that the second to fourth questions are admissible.

Substance

45 According to the Court's settled case-law, where a matter has been the subject of exhaustive harmonisation within the European Union, any national measure relating thereto must be assessed in the light of the provisions of that harmonising measure and not in the light of primary law (judgment of 6 December 2018, *FENS*, C-305/17, EU:C:2018:986, paragraph 22 and the case-law cited).

46 Therefore, it is appropriate to examine, first of all, the questions referred by the referring court in so far as they concern the interpretation of Directives 2003/49, 2011/96 and 2008/7 and, next, in the absence of exhaustive harmonisation, those questions in so far as they concern, first, Articles 49 and 63 TFEU and, second, Article 5(4) and Article 12(b) TEU and Article 47 of the Charter.

The interpretation of Directives 2003/49, 2011/96 and 2008/7

47 By its questions, the referring court asks, in essence, whether Article 1(1) of Directive 2003/49, read in conjunction with Article 4(1)(d) of that directive and with the respective Annex VI, Section 6, point 3 to the Admission Protocol and to the Act of Accession, Article 5 of Directive 2011/96 and Articles 3 and 5 of Directive 2008/7 must be interpreted as precluding national legislation which provides for the taxation in the form of a withholding tax of notional interest that a resident subsidiary which has been granted an interest-free loan by its non-resident parent company would have had to pay to the latter had the loan been concluded under market conditions.

– *Directive 2003/49*

48 It is apparent from recitals 2 to 4 of Directive 2003/49 that the aim of the directive is that double taxation should be eliminated with respect to interest and royalty payments between associated companies of different Member States and that such payments should be subject to tax once in a single Member State, the abolition of all taxation of those payments in the Member State where they arise being the most appropriate means of ensuring equality of tax treatment as between national and cross-border transactions (judgment of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraph 85 and the case-law cited).

49 The scope of Directive 2003/49, as defined in Article 1(1) of the directive, thus concerns the exemption of interest and royalty payments in their source Member State, provided that the beneficial owner is a company established in another Member State or a permanent establishment situated in another Member State belonging to a company of a Member State (judgment of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraph 86).

50 From that point of view, Article 1(1) of that directive provides, inter alia, that interest payments are to be exempt from any withholding tax in the source Member State where the recipient of the interest is a company of another Member State.

51 It is also apparent from the case-law of the Court that, since Article 2(a) of Directive 2003/49 defines interest as 'income from debt-claims of every kind', only the 'actual' beneficial owner can receive interest which constitutes income from such claims (judgment of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraph 87 and the case-law cited).

52 Therefore, the concept of the 'beneficial owner of the interest', within the meaning of that directive, must be interpreted as referring to an entity which actually benefits, in economic terms, from the interest that is paid to it and which therefore has the power freely to determine the use to which it is put (judgment of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraphs 88, 89 and 122).

53 That concept must not therefore be understood in a technical sense (judgment of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraph 92).

54 As the Advocate General observed in point 58 of his Opinion, where the tax authorities set, with a view to taxing it, notional interest on an interest-free loan, the lender receives no interest and cannot therefore be regarded as an 'actual beneficial owner' within the meaning of the case-law set out in paragraph 51 of this judgment.

55 It follows that notional interest set by the tax authorities, such as that at issue in the main proceedings, cannot be regarded as interest payments for the purposes of Article 1(1) and Article 2(a) of Directive 2003/49, precisely since no payment has been made.

56 For the same reason, such interest cannot be covered by Article 4(1)(d) of that directive either, given that that provision relates to 'payments' from debt-claims which contain no provision for repayment of the principal amount or where the repayment is due more than 50 years after the date of issue.

57 Therefore, Directive 2003/49 does not apply to national legislation such as that at issue in the main proceedings.

58 In those circumstances, it is not necessary to rule on the interpretation of the transitional provisions contained in the respective Annex VI, Section 6, point 3 to the Admission Protocol and to the Act of Accession, relating to the application of that directive in the Republic of Bulgaria.

– *Directive 2011/96*

59 In accordance with recitals 3 to 6 thereof, the objective pursued by Directive 2011/96 is to exempt dividends and other profit distributions paid by subsidiary companies to their parent companies from withholding taxes and to eliminate double taxation of such income at the level of the parent company, in order to facilitate the grouping together of companies at EU level (judgment of 2 April 2020, *GVC Services (Bulgaria)*, C-458/18, EU:C:2020:266, paragraph 31 and the case-law cited).

60 That directive thus seeks to ensure the neutrality, from a tax point of view, of the distribution of profits by a company established in one Member State to its parent company established in another Member State (see, to that effect, judgment of 8 March 2017, *Wereldhave Belgium and Others*, C-448/15, EU:C:2017:180, paragraph 25 and the case-law cited).

61 To that end, Article 1(1)(b) of that directive provides that it applies to distributions of profits, in a cross-border relationship, by a subsidiary to its parent company, while Article 5 of that directive provides for their exemption from withholding tax.

62 In that regard, the Court has already held that the Member State in which a company is resident may lawfully treat interest paid by that company to its parent company established in another Member State as a distribution of profits where the amount of that interest exceeds what would have been paid on an arm's-length basis (see, to that effect, judgment of 13 March 2007, *Test Claimants in the Thin Cap Group Litigation*, C-524/04, EU:C:2007:161, paragraphs 87 to 89).

63 By contrast, notional interest set by the tax authorities of a resident company in connection with an interest-free loan concluded between that company and its non-resident parent company cannot be regarded as distributed profits, since, in such a case, no actual payment of interest takes place between those companies.

64 Accordingly, Directive 2011/96 does not apply to national legislation such as that at issue in the main proceedings.

– *Directive 2008/7*

65 As the Court has already held on numerous occasions, Directive 2008/7 provided for complete harmonisation of the cases in which the Member States may levy indirect taxes on the raising of capital (judgment of 19 October 2017, *Air Berlin*, C-573/16, EU:C:2017:772, paragraph 27 and the case-law cited).

66 Therefore, that harmonisation seeks to eliminate, as far as possible, factors which may distort conditions of competition or hinder the free movement of capital, and thus to ensure the smooth functioning of the internal market (see, to that effect, judgment of 22 April 2015, *Drukarnia Multipress*, C-357/13, EU:C:2015:253, paragraph 31).

67 To that end, Article 5(1)(a) of that directive requires Member States not to subject capital companies to any form of indirect tax whatsoever in respect of contributions of capital.

68 Under Article 3(h) of that directive, the concept of 'contributions of capital' includes an increase in the assets of a capital company through the provision of services by a member which does not entail an increase in the company's capital, but which may increase the value of the company's shares.

69 In that regard, it is apparent from the case-law of the Court that the granting of an interest-free loan may constitute a contribution of capital within the meaning of that provision since such a loan allows the borrowing company to have capital available without having to bear its cost; that the resultant saving in interest leads to an increase in its assets by allowing the company to avoid expenditure which it would otherwise have to bear; and that, by saving it that expense, the advantage of such a loan helps to strengthen the company's economic potential, and must therefore be regarded as likely to increase the value of the rights in the recipient company (judgment of 17 September 2002, *Norddeutsche Gesellschaft zur Beratung und Durchführung von Entsorgungsaufgaben bei Kernkraftwerken*, C-392/00, EU:C:2002:500, paragraph 18 and the case-law cited).

70 However, according to the very title of Directive 2008/7 and the wording of Article 5(1)(a) thereof, that directive prohibits only Member States from subjecting contributions of capital to 'indirect tax'. In particular, as the Court has already pointed out, the harmonisation provided for by that directive does not concern direct taxes which, like corporation tax, are in principle a matter for the Member States, in compliance with EU law (judgments of 26 September 1996, *Frederiksen*, C-287/94, EU:C:1996:354, paragraph 21, and of 18 January 2001, *P. P. Handelsgesellschaft*, C-113/99, EU:C:2001:32, paragraph 24).

71 Accordingly, Article 5(1)(a) of Directive 2008/7 does not require Member States to exempt contributions of capital from all forms of direct tax.

72 As the Advocate General observed in point 168 of his Opinion, the withholding tax at issue in the main proceedings must be regarded as a direct tax.

73 That tax, which stems from the application of the national legislation on corporation tax, has as its chargeable event and its base the income which the non-resident parent company should have achieved under market conditions. To that extent, it is similar to a direct tax on income (see, by analogy, judgment of 18 January 2001, *P. P. Handelsgesellschaft*, C-113/99, EU:C:2001:32, paragraph 26, and of 10 March 2005, *Optiver and Others*, C-22/03, EU:C:2005:143, point 33).

74 Therefore, Directive 2008/7 does not apply to national legislation such as that at issue in the main proceedings.

– *Answer to the questions concerning the interpretation of Directives 2003/49, 2011/96 and 2008/7*

75 In the light of all the foregoing considerations, the answer to the referring court is that Article 1(1) of Directive 2003/49, read in conjunction with Article 4(1)(d) of that directive, Article 5 of Directive 2011/96 and Articles 3 and 5 of Directive 2008/7 must be interpreted as not precluding national legislation which provides for the taxation in the form of a withholding tax of notional interest that a resident subsidiary which has been granted an interest-free loan by its non-resident parent company would have had to pay to the latter had the loan been concluded under market conditions.

The interpretation of Articles 49 and 63 TFEU, Article 5(4) and Article 12(b) TEU and Article 47 of the Charter

76 By its questions, the referring court seeks, in essence, to ascertain whether Articles 49 and 63 TFEU, on the one hand, and Article 5(4) and Article 12(b) TEU and Article 47 of the Charter, on the other, must be interpreted as precluding national legislation which provides for the taxation in the form of a withholding tax of notional interest that a resident subsidiary which has been granted an interest-free loan by its non-resident parent company would have had to pay to the latter had the loan been concluded under market conditions, where that withholding tax applies to the gross amount of that interest, without it being possible to deduct, at that stage, expenses related to that loan since a subsequent application to that effect is necessary for the purpose of recalculating that tax and making a possible refund.

– *Articles 49 and 63 TFEU*

77 Since the referring court refers both to freedom of establishment and the free movement of capital, affirmed in Articles 49 and 63 TFEU, respectively, it is first necessary to examine which of those two freedoms is liable to be affected by national legislation such as that at issue in the main proceedings.

78 In that regard, it is clear from the Court's settled case-law that the purpose of the legislation concerned must be taken into consideration (judgment of 10 June 2015, *X*, C-686/13, EU:C:2015:375, paragraph 17 and the case-law cited).

79 National legislation intended to apply only to those shareholdings which enable the holder to exert a definite influence on a company's decisions and to determine its activities falls within the scope of Article 49 TFEU (judgment of 10 June 2015, *X*, C-686/13, EU:C:2015:375, paragraph 18 and the case-law cited).

80 On the other hand, national provisions which apply to shareholdings acquired solely with the intention of making a financial investment without any intention to influence the management and control of the undertaking must be examined exclusively in light of the free movement of capital (judgment of 10 June 2015, *X*, C-686/13, EU:C:2015:375, paragraph 19 and the case-law cited).

81 As regards the national legislation at issue in the main proceedings, the referring court itself states, in its request for a preliminary ruling, that Article 16(2), point 3 of the ZKPO applies to interest-free loans granted both between related companies and between unrelated companies, and thus irrespective of the possibility for a company to exert a definite influence on the decisions and activities of another company, which is, moreover, borne out by the wording of paragraph 1 of that article, which expressly refers to unrelated companies.

82 Likewise, the facts of the dispute in the main proceedings, from which it is apparent that the lending company was, at the time of the relevant facts, the sole shareholder of the borrowing company have no effect in order to determine whether the situation to which the dispute in the main proceedings relates falls within the scope of one or the other of those fundamental rights (see, to that effect, judgment of 10 June 2015, *X*, C-686/13, EU:C:2015:375, paragraphs 22 and 23 and the case-law cited).

83 Consequently, it must be held that, by reason of its very purpose, the national legislation at issue in the main proceedings falls predominantly within the scope of the free movement of capital provided for in Article 63 TFEU (see, to that effect, judgment of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraph 158 and the case-law cited).

84 In those circumstances, even if that national legislation has restrictive effects on freedom of establishment, they are the unavoidable consequence of any restriction on the free movement of capital and, therefore, do not justify an independent examination of that legislation in the light of Article 49 TFEU (judgment of 17 September 2009, *Glaxo Wellcome*, C-182/08, EU:C:2009:559, paragraph 51).

85 It is therefore necessary to examine whether that national legislation includes a restriction on the free movement of capital, within the meaning of Article 63 TFEU, and, if so, whether that restriction may be justified in the light of that provision.

86 In the first place, as regards the existence of a restriction, it should be recalled that, according to the Court's settled case-law, Article 63(1) TFEU prohibits, as restrictions on the movement of capital, measures that are such as to discourage non-residents from making investments in a Member State or to discourage that Member State's residents from doing so in other States (judgment of 30 April 2020, *Société Générale*, C-565/18, EU:C:2020:318, paragraph 22 and the case-law cited).

87 In that regard, even if Article 16(2), point (3) of the ZKPO, which concerns the interpretation of national law, establishes an irrebuttable presumption of tax avoidance, without allowing the interested parties, particularly in the context of a legal challenge, to produce information relating to possible commercial reasons justifying the conclusion of interest-free loans, it must be stated that that rule applies in the same way to all interest-free loans, whether or not they involve non-resident companies. Therefore, as regards that rule, that provision does not entail any restriction on the free movement of capital falling within Article 63 TFEU.

88 By contrast, the Court has already held that national legislation under which a non-resident company is taxed, by means of tax withheld at source by a resident company, on the interest which it is paid by the latter without it being possible to deduct expenses, such as interest expenditure, that are directly related to the lending at issue, whereas such a possibility of deduction is accorded to resident companies receiving interest from another resident company, constitutes a restriction on the free movement of capital (judgment of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraph 175 and the case-law cited).

89 In the present case, although the same 10% rate of tax applies irrespective of the fact that the interest-free loan involves resident companies only or non-resident companies also, resident companies are subject to the tax at issue, in the context of liability to corporation tax, on the net amount of their notional interest income, after deduction of any expenses directly related to the grant of that loan, whereas, in accordance with Article 195(1) and (2) and Article 199 of the ZKPO, non-resident companies are subject to withholding tax on the gross amount of their notional interest income, without it being possible at that stage to deduct such expenses.

90 Admittedly, it is common ground that, under Article 202a of the ZKPO, those non-resident companies may submit an application in the year following that in which the withholding tax was collected so that that tax is recalculated in such a way that it corresponds to that which would have been payable by a resident company. That recovery procedure thus enables them, first, to deduct the expenses directly related to the lending at issue and, second, to secure a possible refund of the excess tax withheld, or even an exemption from withholding tax if they are in a loss-making situation.

91 However, the fact remains that, while a resident company may deduct from the outset the expenses directly related to its notional interest income in order for the amount of tax levied by the tax authorities to correspond immediately to the exact amount of tax due, a non-resident company may request that it be taken into account, in that recovery procedure, only at a later stage, by means of the submission of an application, after having paid the withholding tax calculated on the gross amount of its notional interest.

92 It follows that the adjustment of the tax situation of a non-resident company necessarily occurs late in relation to the time when a resident company, after submitting its tax return, must pay tax on the net amount of its notional interest.

93 Thus, in the present case, it is not disputed that, if the company which granted the loan at issue in the main proceedings had been a resident company, it would not have been required, if its financial situation were loss-making, to pay tax on notional interest relating to that loan and, therefore, it would have been relieved from the outset of paying that tax without having to apply for a recalculation subsequently.

94 It must be noted that such a difference in treatment may procure an advantage for resident companies, since it gives rise, at the very least, to a cash-flow advantage for those companies as compared to non-resident companies (see, by analogy, judgment of 22 November 2018, *Sofina and Others*, C-575/17, EU:C:2018:943, paragraphs 28 to 34).

95 Consequently, national legislation such as that at issue in the main proceedings constitutes a restriction on the free movement of capital which is, in principle, prohibited by Article 63 TFEU.

96 In the second place, it must therefore be examined whether such a restriction can be held to be objectively justified under Article 65(1) and (3) TFEU.

97 It follows from those provisions that Member States may distinguish in their national legislation between resident and non-resident taxable persons provided that such a distinction does not constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital (judgment of 18 March 2021, *Autoridade Tributária e Aduaneira (Tax on Capital gains from property)*, C-388/19, EU:C:2021:212, paragraph 34).

98 It is therefore necessary to distinguish between unequal treatment that is permitted under Article 65(1)(a) TFEU and arbitrary discrimination that is prohibited under Article 65(3) TFEU. In that regard, according to the Court's case-law, for national tax legislation to be capable of being regarded as compatible with the provisions of the FEU Treaty concerning the free movement of capital, the difference in treatment must concern situations that are not objectively comparable or must be justified by an overriding reason in the public interest (see, to that effect, judgment of 18 March 2021, *Autoridade Tributária e Aduaneira (Tax on capital gains from property)*, C-388/19, EU:C:2021:212, paragraph 35).

99 As regards, first, the comparability of the situations at issue in the main proceedings, the defendant in the main proceedings, in its written observations, and the Bulgarian Government, at the hearing, argued that the difference in treatment is justified by the fact that a non-resident company and a resident company are in objectively different situations as regards corporation tax, since the former, unlike the latter, does not produce any financial, accounting or tax results making it possible to subject it to that tax in Bulgaria.

100 In that regard, it should be recalled that, in relation to direct taxes, the situations of residents and non-residents are, as a rule, not comparable (judgment of 14 February 1995, *Schumacker*, C-279/93, EU:C:1995:31, paragraph 31).

101 However, it is apparent from the Court's case-law that, as soon as a Member State, either unilaterally or by way of a convention, imposes a charge to tax on the income not only of resident taxpayers but also of non-resident taxpayers from income which they receive from a resident company, the situation of those non-resident taxpayers becomes comparable to that of resident taxpayers (judgment of 22 November 2018, *Sofina and Others*, C-575/17, EU:C:2018:943, paragraph 47).

102 In particular, as regards the determination, for the purposes of calculating income tax, of expenses directly related to an activity that has generated taxable income in a Member State, the Court has already held that residents and non-residents companies are in a comparable situation (see, to that effect, judgment of 13 November 2019, *College Pension Plan of British Columbia*, C-641/17, EU:C:2019:960, paragraph 74 and the case-law cited).

103 In the present case, it must be held that the Republic of Bulgaria chose, by means of the national legislation at issue in the main proceedings, to exercise its tax jurisdiction over interest-free loans concluded between resident borrowing companies and non-resident lending companies and that, consequently, non-resident companies must be considered to be, as regards the expenses directly related to those loans, in a situation comparable to that of resident companies.

104 It is true that, in the judgment of 22 December 2008, *Truck Center* (C-282/07, EU:C:2008:762), the Court found that, in the circumstances of the case giving rise to that judgment, the difference in treatment consisting in the application of different taxation arrangements on the basis of the place of residence of the taxable person concerned situations which were not objectively comparable and, therefore, that difference in treatment, which moreover did not necessarily procure an advantage for resident recipients, did not constitute a restriction, inter alia, on the free movement of capital (see, to that effect, judgment of 22 December 2008, *Truck Center*, C-282/07, EU:C:2008:762, paragraphs 41 and 49 to 51; see also, to that effect, judgment of 17 September 2015, *Miljoen and Others*, C-10/14, C-14/14 and C-17/14, EU:C:2015:608, paragraph 70).

105 However, unlike the case that gave rise to the judgment of 22 December 2008, *Truck Center* (C-282/07, EU:C:2008:762), in the present case, the resident companies which granted an interest-free loan, as is apparent from paragraph 94 above, enjoy, as compared with non-resident companies which have granted such a loan, a cash-flow advantage which stems from the different point in time at which the expenses directly related to that loan may be deducted by them.

106 As is apparent from paragraphs 91 to 93 above, the extent of that advantage is determined by the duration of the recovery procedure introduced by the national legislation at issue in the main proceedings for the purpose of allowing non-resident companies to apply for recalculation of the withholding tax applied to the gross amount of the notional interest relating to the interest-free loan in order for that retention to correspond to the amount of corporation tax which would have been paid by a resident company which had granted such a loan.

107 In those circumstances, it cannot be held that the difference in treatment in the taxation of notional interest relating to an interest-free loan depending on whether it is granted by a resident company or by a non-resident company is limited to the arrangements for the collection of the tax (see, by analogy, judgments of 26 February 2019, *N Luxembourg 1 and Others*, C-115/16, C-118/16, C-119/16 and C-299/16, EU:C:2019:134, paragraphs 164 and 165, and of 13 November 2019, *College Pension Plan of British Columbia*, C-641/17, EU:C:2019:960, paragraphs 71 to 73).

108 Therefore, that difference in treatment concerns situations which are objectively comparable.

109 It is therefore necessary to examine, secondly, whether the national legislation at issue in the main proceedings can be justified by the grounds relied on in the present case by certain interested parties.

110 In that regard, the defendant in the main proceedings submits that, in accordance with the principle of territoriality, the Member States are entitled to tax income made on their territory in order to ensure a balanced allocation of the powers of taxation. In particular, in the absence of harmonisation measures adopted by the European Union, the Member States remain competent to define the criteria for allocating their powers of taxation. The Bulgarian Government notes, for its part, that the purpose of the national legislation at issue in the main proceedings is to combat tax avoidance.

111 It must therefore be held that that line of argument seeks, in essence, to justify the national legislation at issue in the main proceedings by the need to safeguard a balanced allocation between the Member States of the power to impose taxes and to ensure the effective collection of tax in order to prevent tax avoidance, as is apparent from the very wording of Article 16 of the ZKPO.

112 In that regard, in accordance with the Court's settled case-law, a measure which restricts the free movement of capital is permissible only if it is justified by an overriding reason in the public interest and observes the principle of proportionality, which means that the measure must be appropriate for ensuring the attainment of the objective pursued and not to go beyond what is necessary in order for it to be attained (judgment of 21 May 2019, *Commission* v *Hungary (Usufruct over agricultural land)*, C-235/17, EU:C:2019:432, paragraph 59 and the case-law cited).

113 According to the Court's case-law, prevention of tax evasion is an overriding reason relating to the public interest, capable of justifying a restriction on the exercise of fundamental freedoms guaranteed by the FEU Treaty, including the free movement of capital, as is the need to safeguard the balanced allocation between the Member States of the power to impose taxes (judgment of 8 March 2017, *Euro Park Service*, C-14/16, EU:C:2017:177, paragraph 65). The same applies to the need to ensure the effective collection of tax (see, to that effect, judgment of 30 April 2020, *Société Générale*, C-565/18, EU:C:2020:318, paragraph 38 and the case-law cited).

114 As regards the ability of the national legislation at issue in the main proceedings to attain those objectives, it should be recalled that the need to maintain the balanced allocation of the power to tax between the Member States may be capable of justifying a difference in treatment where the system in question is designed to prevent conduct liable to jeopardise the right of a Member State to exercise its power to tax in relation to activities carried out in its territory (judgment of 31 May 2018, *Hornbach-Baumarkt*, C-382/16, EU:C:2018:366, paragraph 43 and the case-law cited).

115 In that regard, the Court has previously held that retention at source is a legitimate and appropriate means of ensuring the tax treatment of the income of a taxable person established outside the State of taxation (see, to that effect, judgment of 22 November 2018, *Sofina and Others*, C-575/17, EU:C:2018:943, paragraph 68).

116 In the present case, it must be held that the national legislation at issue in the main proceedings, in so far as it provides for taxation at source of notional interest on interest-free loans granted by non-resident companies to resident companies, allows the Member State of residence to exercise its tax jurisdiction in relation to activities carried out on its territory, by seeking to prevent that the grant of such loans have for sole purpose the avoidance of tax which would normally be payable on income generated by activities carried out on the national territory.

117 Such legislation must therefore be regarded as capable of safeguarding a balanced allocation between the Member States of the power to impose taxes and ensuring the effective collection of tax in order to prevent tax avoidance.

118 As regards whether the national legislation at issue in the main proceedings goes beyond what is necessary to achieve those objectives, Viva Telecom Bulgaria claimed at the hearing that the duration of the recovery procedure provided for in Article 202a of the ZKPO is excessive, since a

possible refund of excess withholding tax paid by a resident company on the gross amount of notional interest relating to an interest-free loan granted by a non-resident company may occur only after three years have elapsed.

119 However, subject to the checks to be carried out by the referring court, it is apparent from the explanations provided by the defendant in the main proceedings at that hearing that such refund is made, as a general rule, within a period of 30 days from the date on which the application was made and that it is only in exceptional cases that the procedure may last up to three years. In addition, the Bulgarian Government stated at the hearing, which it is also for the referring court to verify, that the National Revenue Agency must pay interest on the amounts owed as from the 30th day after the submission of the tax return.

120 Thus, subject to those checks, the national legislation at issue in the main proceedings does not appear, in the light of the duration of the recovery procedure, to go beyond what is necessary to attain the objectives that it pursues.

121 In those circumstances, that national legislation appears to be capable of being justified by the objectives of safeguarding a balanced allocation between the Member States of the power to impose taxes and ensuring the effective collection of tax in order to prevent tax avoidance.

– *Article 5(4) and Article 12(b) TEU and Article 47 of the Charter*

122 As is apparent from paragraph 33 above, the referring court also raises the question of the interpretation of Article 5(4) and Article 12(b) TEU and Article 47 of the Charter, on the ground that the national legislation at issue in the main proceedings, as set out in Article 16(2), point 3 of the ZKPO, provides for an irrebuttable presumption of tax avoidance in the event of the grant of an interest-free loan.

123 In that regard, it should be recalled that, according to settled case-law, the Court does not have jurisdiction to reply to a question referred for a preliminary ruling where it is obvious that the provision of EU law referred to the Court for interpretation is incapable of applying (judgment of 25 July 2018, *TTL*, C-553/16, EU:C:2018:604, paragraph 31).

124 In the first place, as regards Article 5(4) TEU, the Court has already held that that provision relates to action by the institutions of the Union, its first subparagraph providing that, under the principle of proportionality, the content and form of Union action is not to exceed what is necessary to achieve the objectives of the Treaties and its second subparagraph requiring the institutions of the Union to comply with the principle of proportionality when they act in the exercise of a competence (see, to that effect, judgment of 25 July 2018, *TTL*, C-553/16, EU:C:2018:604, paragraph 33).

125 In the second place, as regards Article 12(b) TEU, the Court has also held that that provision, under which national parliaments contribute to the good functioning of the Union by seeing to it that the principle of subsidiarity is respected, empowers those parliaments to ensure (i) respect for that principle when EU institutions exercise a competence and (ii) the good functioning of the Union and, therefore, does not refer to national legislation but to EU draft legislative acts (see, to that effect, judgment of 25 July 2018, *TTL*, C-553/16, EU:C:2018:604, paragraph 34).

126 In the third place, as regards Article 47 of the Charter, it should be recalled that its scope of application, so far as concerns action of the Member States, is defined in Article 51(1) of that Charter, according to which the provisions thereof are addressed to the Member States only when they are implementing EU law (judgment of 14 January 2021, *Okrazhna prokuratura – Haskovo and Apelativna prokuratura – Plovdiv*, C-393/19, EU:C:2021:8, paragraph 30 and the case-law cited).

127 Article 51(1) of the Charter confirms the Court's settled case-law, which states that the fundamental rights guaranteed in the legal order of the European Union are applicable in all situations governed by EU law, but not outside such situations (judgment of 14 January 2021, *Okrazhna prokuratura – Haskovo and Apelativna prokuratura – Plovdiv*, C-393/19, EU:C:2021:8, paragraph 31 and the case-law cited).

128 Thus, where a legal situation does not come within the scope of EU law, the Court does not have jurisdiction to rule on it and any provisions of the Charter relied upon cannot, of themselves, form the basis for such jurisdiction (judgment of 14 January 2021, *Okrazhna prokuratura – Haskovo and Apelativna prokuratura – Plovdiv*, C-393/19, EU:C:2021:8, paragraph 32 and the case-law cited).

129 In this instance, the national legislation at issue in the main proceedings does not fall within of scope of Directives 2003/49, 2011/96 and 2008/7 for the reasons set out in paragraphs 48 and 75 of this judgment. Furthermore, Article 16(2), point 3 of the ZKPO, in that it introduces an irrebutable presumption of tax avoidance does not fall under, as is apparent from paragraph 87 of this judgment, Article 63 TFEU and, consequently, in that respect, falls outside the scope of the Charter.

130 It follows that there is no need to answer the referring court in so far as it raises the question of the interpretation of Article 5(4) and Article 12(b) TEU and Article 47 of the Charter, since it is clear that those provisions are not applicable to the situation referred to by that court.

– *Answer to the questions concerning the interpretation of primary law*

131 In the light of all the foregoing considerations, the answer to the referring court is that Article 63 TFEU, read in the light of the principle of proportionality, must be interpreted as not precluding national legislation which provides for the taxation in the form of a withholding tax of notional interest that a resident subsidiary which has been granted an interest-free loan by its non-resident parent company would have had to pay to the latter had the loan been concluded under market conditions, where that withholding tax applies to the gross amount of that interest, without it being possible to deduct, at that stage, expenses related to that loan since a subsequent application to that effect is necessary for the purpose of recalculating that tax and making a possible refund, in so far as, first, the length of the procedure laid down for that purpose by that legislation is not excessive and, second, interest is owed on the amounts refunded.

Costs

132 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 (Fifth Chamber) hereby rules:

1. **Article 1(1) of 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, read in conjunction with Article 4(1)(d) of that directive, Article 5 of 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, as amended by Council Directive (EU) 2015/121 of 27 January 2015, and Articles 3 and 5 of Council Directive 2008/7/EC of 12 February 2008 concerning indirect taxes on the raising of capital must be interpreted as not precluding national legislation which provides for the taxation in the form of a withholding tax of notional interest that a resident subsidiary which has been granted an interest-free loan by its non-resident parent company would have had to pay to the latter had the loan been concluded under market conditions.**

2. **Article 63 TFEU, read in the light of the principle of proportionality,, must be interpreted as not precluding national legislation which provides for the taxation in the form of a withholding tax of notional interest that a resident subsidiary which has been granted an interest-free loan by its non-resident parent company would have had to pay to the latter had the loan been concluded under market conditions, where that withholding tax applies to the gross amount of that interest, without it being possible to deduct, at that stage, expenses related to that loan since a subsequent application to that effect is necessary for the purpose of recalculating that tax and making a possible refund, in so far as, first, the length of the procedure laid down for that purpose by that legislation is not excessive and, second, interest is owed on the amounts refunded.**

[Signatures]