Reports of Cases

JUDGMENT OF THE COURT (First Chamber)

4 July 2013 *

(Tax legislation — Corporation tax — Deduction for risk capital — Notional interest — Reduction of the amount deductible by companies with establishments abroad the income from which is exempt under double taxation conventions)

In Case C-350/11,

REQUEST for a preliminary ruling under Article 267 TFEU from the rechtbank van eerste aanleg te Antwerpen (Belgium), made by decision of 24 June 2011, received at the Court on 4 July 2011, in the proceedings

Argenta Spaarbank NV

v

Belgische Staat,

THE COURT (First Chamber),

composed of A. Tizzano, President of the Chamber, M. Ilešič, E. Levits (Rapporteur), J.-J. Kasel and M. Safjan, Judges,

Advocate General: P. Mengozzi,

Registrar: M. Ferreira, Principal Administrator,

having regard to the written procedure and further to the hearing on 12 July 2012,

after considering the observations submitted on behalf of:

— Argenta Spaarbank NV, by K. Morbée, K. Van Duyse and F. Smet, advocaten,

— the Belgian Government, by M. Jacobs and J.-C. Halleux, acting as Agents,

— the European Commission, by W. Mölls and W. Roels, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 19 September 2012,

gives the following

* Language of the case: Dutch.

Judgment

1 This request for a preliminary ruling concerns the interpretation of Article 49 TFEU.

2 The request has been made in proceedings between Argenta Spaarbank NV ('Argenta') and Belgische Staat (the Belgian State) concerning calculation of the deduction for risk capital in respect of the year of assessment corresponding to 2008.

Legal context

Belgian law

3 The deduction for risk capital was inserted into the income tax regime by the Law of 22 June 2005 introducing a tax deduction for risk capital (*Belgisch Staatsblad* of 30 June 2005, p. 30077). The deduction is set out in Articles 205a to 205h and 236 of the Income Tax Code 1992.

4 According to its explanatory memorandum, the objective of that law is inter alia to reduce the difference in tax treatment between the financing of companies with loan capital, the return on which is entirely tax deductible, and financing with equity capital (risk capital), the return on which was fully taxed, and to increase the solvency ratio of companies, the introduction of the deduction for risk capital falling within the general aim of improving the competitiveness of the Belgian economy.

5 The deduction for risk capital, also called 'deduction of notional interest', consists in deducting a percentage of the equity capital of the company concerned from the basis of assessment for corporation tax.

6 Under Article 205c(1) of the Income Tax Code 1992, the deduction for risk capital is equal to the risk capital, determined in accordance with Article 205b of the Income Tax Code 1992, multiplied by a rate laid down in the following paragraphs of Article 205c.

7 The first subparagraph of Article 205b(1) of the Income Tax Code 1992 provides that, in order to determine the deduction for risk capital in respect of a tax period, the risk capital to be taken into account corresponds, subject to the provisions of Article 205b(2) to (7), to the amount of the company's equity capital at the end of the previous tax period, determined in accordance with accounting legislation and the annual accounts as shown on the balance sheet. Article 205b(2) to (7) lay down the situations in which the equity capital must be adjusted in order to serve as a basis of calculation for determining the amount of the deduction for risk capital.

8 In particular, under Article 205b(2) of the Income Tax Code 1992, the risk capital determined in accordance with Article 205b(1) of the Income Tax Code 1992 is reduced by the net value of the assets of permanent establishments the income from which is exempt under a double taxation convention.

9 Article 205d of the Income Tax Code 1992 provides that, if there are no profits for a tax period in respect of which the deduction for risk capital may be made, the relief not granted for that tax period is to be carried over successively to the profits of the following seven years.

Double taxation convention between the Kingdom of Belgium and the Kingdom of the Netherlands

10 Article 7(1) to (3) of the Convention of 5 June 2001 between the Kingdom of Belgium and the Kingdom of the Netherlands for the avoidance of double taxation and the prevention of tax evasion in respect of taxes on income and capital (*Belgisch Staatsblad* of 20 December 2002, p. 57533; 'the Belgium-Netherlands Convention') provide:

'1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.

2. Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.

3. In determining the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the permanent establishment, including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere.'

11 Article 23(1) of the Belgium-Netherlands Convention provides:

'So far as concerns Belgium, double taxation shall be avoided as follows:

(a) Where a resident of Belgium receives income – other than dividends, interest, or royalties covered by Article 12(5) – or possesses assets which are taxed in the Netherlands in accordance with the provisions of this convention, Belgium shall exempt that income or those assets from tax, but it may, in order to calculate the amount of tax on the remainder of that resident's income or assets, apply the same rate as if the income or assets in question had not been exempted.

…'

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

12 Argenta is a company resident in Belgium and is subject to corporation tax in that Member State. It has a permanent establishment in the Netherlands, the income from which is exempt in Belgium under the Belgium-Netherlands Convention.

13 Argenta sought the deduction for risk capital in respect of the year of assessment corresponding to 2008, pursuant to Articles 205a to 205h of the Income Tax Code 1992.

14 On 19 November 2008, Argenta's corporation tax liability for that year of assessment was established. When calculating the assessment, the Belgian tax authorities, relying on Article 205b(2) of the Income Tax Code 1992, did not take into account the net value of the assets of Argenta's permanent establishment in the Netherlands in order to determine the risk capital serving as a basis for the deduction for risk capital.

15 The objection lodged by Argenta on 20 May 2009 challenging that assessment was rejected by the Belgian tax authorities on 7 September 2009.

16 Since Argenta took the view that Article 205b(2) of the Income Tax Code 1992 constituted an obstacle to the freedom of establishment provided for in Article 49 TFEU, inasmuch as investments made in a permanent establishment situated in a Member State with which the Kingdom of Belgium had concluded a double taxation convention did not confer entitlement to the deduction for risk capital, whereas similar investments made in an establishment situated in Belgium did afford entitlement to that deduction, on 4 December 2009 it brought an action before the referring court challenging that decision.

17 In those circumstances, that court decided to stay proceedings and to refer the following question to the Court for a preliminary ruling:

'Does Article [49 TFEU] preclude national tax legislation pursuant to which, for the purposes of the calculation of its taxable profit, a company subject to full tax liability in Belgium cannot apply a deduction in respect of risk capital in the amount of the positive difference between (i) the net book value of the assets of the establishments that that company runs in another Member State of the European Union and (ii) the total liabilities that are attributable to those establishments, whereas it can apply a deduction in respect of risk capital if that positive difference can be attributed to a permanent establishment located in Belgium.'

Consideration of the question referred

18 By its question, the referring court asks whether Article 49 TFEU must be interpreted as precluding national legislation under which, for calculation of a deduction granted to a company subject to full tax liability in a Member State, the net value of the assets of a permanent establishment situated in another Member State is not taken into account when the profits of that permanent establishment are not taxable in the first Member State by virtue of a double taxation convention, whereas the assets attributed to a permanent establishment situated in the territory of the first Member State are taken into account for that purpose.

19 As is clear from settled case-law, the freedom of establishment conferred by Article 49 TFEU on European Union nationals, which entails for them access to, and pursuit of, activities as self-employed persons and the forming and management of undertakings, under the same conditions as those laid down for its own nationals by the laws of the Member State of establishment, includes, pursuant to Article 54 TFEU, the right of companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the European Union to pursue their activities in the Member State concerned through a subsidiary, a branch or an agency (see Case C-310/09 *Accor* [2011] ECR I-8115, paragraph 39 and the case-law cited).

20 Even though, according to their wording, the provisions of the FEU Treaty concerning freedom of establishment are aimed at ensuring that foreign nationals and companies are treated in the host Member State in the same way as nationals of that State, they also prohibit the Member State of origin from hindering the establishment in another Member State of one of its nationals or of a company incorporated under its legislation (*Accor*, paragraph 40 and the case-law cited).

21 Those considerations also apply where a company established in a Member State carries on business in another Member State through a permanent establishment (Case C-414/06 *Lidl Belgium* [2008] ECR I-3601, paragraph 20).

22 In the main proceedings, it is common ground that, for the purposes of calculating the deduction for risk capital, the legislation at issue establishes a difference in treatment between the assets of permanent establishments situated in a Member State other than the Kingdom of Belgium the income from which is not taxable in Belgium and the assets of permanent establishments situated in the Kingdom of Belgium.

23 Assets attributed to permanent establishments which are situated in a Member State other than the Kingdom of Belgium and the income from which is not taxable in Belgium are not taken into account when calculating the risk capital serving as a basis for calculation of the deduction at issue in the main proceedings, whereas assets attributed to permanent establishments situated in Belgium are taken into account for that purpose.

24 As the Advocate General has noted in point 33 of his Opinion, the taking into account of the assets of a permanent establishment in order to calculate the deduction for risk capital of a company subject to corporation tax in Belgium constitutes a tax advantage, since taking them into account helps to reduce the effective rate of the corporation tax that such a company must pay in that Member State.

25 Such a tax advantage is denied when the permanent establishment of the company resident in Belgium is situated in another Member State and enjoys an exemption for its income, under a double taxation convention concluded between the Kingdom of Belgium and that other Member State.

26 The Belgian Government submits, in this regard, that the difference in treatment arising from the national legislation at issue in the main proceedings is not, however, a restriction on freedom of establishment since, first, that difference in treatment does not result in adverse consequences for the company with a permanent establishment in a Member State other than the Kingdom of Belgium and, second, if such adverse consequences were to be established, they would be due to the exercise in parallel by a number of Member States of their fiscal sovereignty.

27 Thus, the Belgian Government contends that, even if the assets of the permanent establishment situated in a Member State other than the Kingdom of Belgium were taken into account, the profits for tax purposes of the resident principal company could not be reduced. In its submission, in the case of foreign permanent establishments not exempt under a double taxation convention, the deduction for risk capital is calculated separately, by reference to the assets attributed to the permanent establishment, and is applied first to the profits made by that establishment. The Belgian Government draws the conclusion, by analogy, that if it were necessary to take account of the assets of the permanent establishment which is situated in a Member State other than the Kingdom of Belgium and the income from which is exempt under a convention, the deduction for risk capital should be ascribed to the profits attributed to that establishment. However, those profits are not taxed in Belgium.

28 Argenta and the Commission have contested that interpretation of Belgian law, submitting that in the case of foreign permanent establishments the income from which is not exempt from tax in Belgium the deduction for risk capital is calculated on the basis of overall income and that it applies to all the taxable income of the company concerned.

29 It should be recalled that, as follows from settled case-law, when the Court replies to a question submitted for a preliminary ruling by a court of a Member State in accordance with Article 267 TFEU, it does not have jurisdiction to interpret the domestic law of that Member State, as this task falls to the national courts (see, inter alia, Case C-37/92 *Vanacker and Lesage* [1993] ECR I-4947, paragraph 7; Case C-449/06 *Gysen* [2008] ECR I-553, paragraph 17; and Case C-23/12 *Zakaria* [2013] ECR, paragraph 29).

30 However, it must be noted that the Belgian Government conceded at the hearing that – even if the deduction for risk capital were calculated separately, by reference to the assets of the permanent establishment, and were to be applied first to the profits of that establishment – any surplus would be deducted from the profits made by the principal company. Thus, it does not follow from the line of argument put forward by the Belgian Government that it would be impossible for the resident principal company to benefit, for the purpose of reducing its basis of assessment, from the deduction for risk capital calculated by taking account of the assets of the permanent establishment situated in a Member State other than the Kingdom of Belgium.

31 Furthermore, as the Advocate General has observed in point 40 of his Opinion, the Belgian Government has not contested Argenta's submission that a Belgian company financed with equity capital may benefit from the deduction for risk capital even if its foreign permanent establishment – which does not itself have any equity capital – alone makes profits, which will ultimately be attributed to that company, under Belgian legislation, for the purposes of calculating the deduction.

32 Consequently, the inability of a company with a permanent establishment in a Member State other than the Kingdom of Belgium to benefit, for the purpose of reducing its basis of assessment, from the deduction for risk capital calculated by taking account of the assets of that establishment is disadvantageous for that company.

33 Contrary to the Belgian Government's assertions, this disadvantageous treatment stems not from the fact that the Member State in which the permanent establishment is situated does not provide for any deduction for risk capital, but solely from the choice made in the Belgian legislation not to permit assets of the aforesaid permanent establishments to be taken into account. The disadvantageous treatment cannot therefore be the consequence of the exercise in parallel by a number of Member States of their fiscal sovereignty.

34 Disadvantageous treatment of that kind is liable to deter a Belgian company from carrying on its business through a permanent establishment situated in a Member State other than the Kingdom of Belgium and therefore constitutes a restriction prohibited in principle by the Treaty provisions relating to freedom of establishment.

35 It is clear from the Court's case-law that a restriction on freedom of establishment is permissible only if it is justified by overriding reasons in the public interest. It is further necessary, in such a case, that the restriction be appropriate to ensuring the attainment of the objective in question and not go beyond what is necessary to attain it (see *Lidl Belgium*, paragraph 27 and case-law cited).

36 In this regard, the Belgian Government advances reasons, taken together, relating to the need to safeguard the coherence of the Belgian tax system and preserve the balanced allocation between the Member States of the power to tax.

37 The Belgian Government argues, first, that the risk-capital reduction regime is perfectly symmetrical and a direct, personal and material link exists between the tax advantage, which is calculated by reference to assets, and the taxation of the profits generated by those assets.

38 In its submission, that link is comparable to the link which exists between deductible interest on a loan for acquiring an asset and the taxable profit generated by that asset, the law establishing the deduction at issue in the main proceedings having the objective, as is clear from its explanatory memorandum, of treating equity capital in the same way for tax purposes as loan capital. Although the deduction for risk capital is calculated at a standard rate, by reference to the company's equity capital, and not as a proportion of its taxable profits, the deduction calculated is supposed to represent the interest that the company would have paid if it had had to borrow in order to build up the assets acquired by using its equity capital.

39 Second, according to the Belgian Government, by refusing to take into account the assets of a permanent establishment which is situated in a Member State other than the Kingdom of Belgium and the profits from which are not taxable in Belgium, the Kingdom of Belgium is exercising its powers of taxation in compliance with the principle of territoriality, and in accordance with the allocation of the power to tax as resulting from the Belgium-Netherlands Convention.

40 The Belgian Government states that the power to take account of expenses – entered in, or outside, the accounts – which are connected with the assets and liabilities assigned to a permanent establishment and to grant the deductions relating to those assets or those liabilities rests with the Member State upon which the double taxation convention confers the right to tax the permanent establishment's profits. Moreover, such an allocation, established by the Belgium-Netherlands Convention, accords with the Model Tax Convention on Income and on Capital, drawn up by the Organisation for Economic Co-operation and Development (OECD).

41 So far as concerns the first ground of justification relied on by the Belgian Government, it should be recalled that the Court has already acknowledged that the need to maintain the coherence of a tax system can justify a restriction on the exercise of the freedoms of movement guaranteed by the Treaty (Case C-204/90 *Bachmann* [1992] ECR I-249, paragraph 28; Case C-319/02 *Manninen* [2004] ECR I-7477, paragraph 42; Case C-471/04 *Keller Holding* [2006] ECR I-2107, paragraph 40; and Case C-418/07 *Papillon* [2008] ECR I-8947, paragraph 43).

42 However, in order for an argument founded on such a justification to succeed, it is necessary, in accordance with settled case-law, that the existence of a direct link be established between the tax advantage concerned and the offsetting of that advantage by a particular tax levy (*Manninen*, paragraph 42, and *Keller Holding*, paragraph 40), the direct nature of that link falling to be examined in the light of the objective pursued by the rules in question (*Manninen*, paragraph 43; Case C-293/06 *Deutsche Shell* [2008] ECR I-1129, paragraph 39; and *Papillon*, paragraph 44).

43 As has been noted in paragraph 24 of the present judgment, the tax advantage at issue in the main proceedings consists in the possibility of taking into account, in order to calculate the deduction for risk capital, the assets attributed to a permanent establishment.

44 That advantage, which has the effect of reducing the effective rate of corporation tax to which the principal company is subject, is not offset in the main proceedings by a particular tax levy.

45 It is true that the advantage is granted only where the profits generated by the permanent establishment are taxable in Belgium.

46 However, there is no direct link, within the meaning of the case-law recalled in paragraph 42 of the present judgment, between the advantage calculated by taking account of the assets and the taxation of the return generated by them.

47 The legislation at issue in the main proceedings requires solely that any income generated by the permanent establishment be taxable in Belgium, without making grant of the advantage in question conditional on such income actually being generated or actually being taxed. Accordingly, the system concerned permits a situation in which, where the income from a permanent establishment is taxable in Belgium, but that establishment has not generated income, its assets are taken into account in order to calculate the deduction applied to the company to which it belongs.

48 Furthermore, Article 205d of the Income Tax Code 1992 provides that, if there are no profits for a tax period in respect of which the deduction for risk capital may be made, the relief not granted for that tax period may be carried over successively to the profits of the following seven years.

49 Consequently, the refusal to take account of the assets of permanent establishments which are situated in a Member State other than the Kingdom of Belgium and the income from which is exempt from tax in Belgium by virtue of a double taxation convention cannot be justified by reasons relating to the need to safeguard the coherence of the national tax system.

50 So far as concerns the second ground of justification relied on by the Belgian Government, it should be recalled that preservation of the allocation between Member States of the power to tax is a legitimate objective recognised by the Court (see, to this effect, Case C-446/03 *Marks & Spencer* [2005] ECR I-10837, paragraph 45; Case C-470/04 *N* [2006] ECR I-7409, paragraph 42; Case C-231/05 *Oy AA* [2007] ECR I-6373, paragraph 51; and *Lidl Belgium*, paragraph 31). It is also settled case-law that, in the absence of any unifying or harmonising measures of the European Union, the Member States retain the power to define, by treaty or unilaterally, the criteria for allocating their powers of taxation, particularly with a view to eliminating double taxation (Case C-540/07 *Commission* v *Italy* [2009] ECR I-10983, paragraph 29, and Case C-371/10 *National Grid Indus* [2011] ECR I-12273, paragraph 45).

51 However, the fact that a Member State has agreed, in a double taxation convention concluded with another Member State, that the profits attributable to a permanent establishment situated in that other Member State are taxable only in the latter and that, consequently, the first Member State cannot exercise its power to tax in relation to the profits attributable to that permanent establishment cannot systematically justify any refusal to grant an advantage to the company established in the territory of the first Member State to which the permanent establishment belongs.

52 Such a refusal would be tantamount to justifying a difference in treatment solely on the ground that a company established in a Member State has developed a cross-border economic activity which is not liable to generate tax revenue for that Member State (see, to this effect, *Marks & Spencer*, paragraph 40, and Case C-347/04 *Rewe Zentralfinanz* [2007] ECR I-2647, paragraph 43).

53 On the other hand, it is apparent from the case-law that the need to safeguard the balanced allocation between the Member States of the power to tax may be accepted, in particular, where the system in question is designed to prevent conduct capable of jeopardising the right of a Member State to exercise its powers of taxation in relation to activities carried out in its territory (see *Oy AA*, paragraph 54; Case C-379/05 *Amurta* [2007] ECR I-9569, paragraph 58; Case C-303/07 *Aberdeen Property Fininvest Alpha* [2009] ECR I-5145, paragraph 66; Case C-284/09 *Commission* v *Germany* [2011] ECR I-9879, paragraph 77; and Joined Cases C-338/11 to C-347/11 *Santander Asset Management SGIIC and Others* [2012] ECR, paragraph 47).

54 Thus, the Court has held that this objective is designed inter alia to safeguard symmetry between the right to tax profits and the entitlement to deduct losses of a permanent establishment, inasmuch as acceptance that the losses of a non-resident permanent establishment might be deducted from the income of the principal company would result in allowing that company to choose freely the Member State in which it claims such losses (see, to this effect, *Oy AA*, paragraph 56, and *Lidl Belgium*, paragraph 34).

55 As the Advocate General has noted in point 63 of his Opinion, granting the tax advantage at issue in the main proceedings would jeopardise neither the right of the Member State in whose territory the company to which the permanent establishment belongs is established nor that of the Member State in whose territory the permanent establishment is situated to exercise the power to tax in relation to activities carried out in its territory and would not result in the shifting of income normally taxable in one of those Member States to the other.

56 Finally, as regards the Belgian Government's argument relating to the parallel treatment that should be accorded to the deduction for tax purposes of interest on loans used to build up the assets attributable to a permanent establishment, on the one hand, and to the treatment of equity capital attributed to a permanent establishment, on the other, it should be pointed out that the Belgian Government itself

acknowledges that the deduction for risk capital is calculated at a standard rate by reference to the equity capital of the company concerned and not as a proportion of the taxable profits generated by that company's assets.

57 Accordingly, the Belgian Government cannot maintain that the Belgium-Netherlands Convention, and in particular its provisions relating to determination of the profits of a permanent establishment and to the taking into account, to that end, of expenditure incurred for the purposes of that establishment, preclude taking into account, in order to calculate the deduction for risk capital, assets attributed to a permanent establishment the income from which is not taxable in Belgium by virtue of that convention.

58 In those circumstances, the restriction established by the legislation at issue in the main proceedings cannot be justified by reasons relating to the need to safeguard the balanced allocation between the Member States of the power to tax.

59 In the light of all the foregoing considerations, the answer to the question referred is that Article 49 TFEU must be interpreted as precluding national legislation under which, for calculation of a deduction granted to a company subject to full tax liability in a Member State, the net value of the assets of a permanent establishment situated in another Member State is not taken into account when the profits of that permanent establishment are not taxable in the first Member State by virtue of a double taxation convention, whereas the assets attributed to a permanent establishment situated in the territory of the first Member State are taken into account for that purpose.

Costs

60 Since these proceedings are, for the parties to the main proceedings, a step in the action pending before the referring 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 (First Chamber) hereby rules:

Article 49 TFEU must be interpreted as precluding national legislation under which, for calculation of a deduction granted to a company subject to full tax liability in a Member State, the net value of the assets of a permanent establishment situated in another Member State is not taken into account when the profits of that permanent establishment are not taxable in the first Member State by virtue of a double taxation convention, whereas the assets attributed to a permanent establishment situated in the territory of the first Member State are taken into account for that purpose.

[Signatures]