NORDDEUTSCHE GESELLSCHAFT ZUR BERATUNG UND DURCHFÜHRUNG VON ENTSORGUNGSAUFGABEN BEI KERNKRAFTWERKEN

OPINION OF ADVOCATE GENERAL STIX-HACKL

delivered on 17 January 2002 [1]

1. In the present case relating to capital duty the Court of Justice has been asked to develop its case-law on taxable transactions under Article 4 of Council Directive 69/335/EEC of 17 July 1969 [2] (hereinafter referred to as 'Directive 69/335'). The Bundesfinanzhof (Federal Finance Court) is essentially asking whether the grant of an interest-free loan is liable to capital duty even if the company benefiting from it had already concluded a profit and loss transfer agreement with the party making the loan.

I — Legal framework

Community law

2. As is apparent from the first recital in the preamble to Directive 69/335, the objective of that directive is to promote the free movement of capital, which is considered to be one of the essential conditions for creating an economic union whose characteristics are similar to those of a domestic market. [3]

3. According to the sixth recital, in the context of duty on the raising of capital, the pursuit of this objective demands the abolition of indirect taxation already in force in the Member States and its replacement by the introduction of a duty that is only charged once within the common market the level of which should be the same in all Member States.

4. Article 4(2) of Directive 69/335 provides as follows:

'The following transactions may, to the extent that they were taxed at the rate of 1% as at 1 July 1984, continue to be subject to capital duty:

1 — Original language: German.

2 — ... concerning indirect taxes on the raising of capital (OJ, English Special Edition 1969 (II), p. 412), in the version contained in Council Directive 85/303/EEC of 10 June 1985 (OJ 1985 L 156, p. 23).

3 — For the current position regarding free movement of capital, see the Opinion of Advocate General Geelhoed delivered on 20 November 2001 in Joined Cases C-515/99, C-519/99 to C-524/99 and C-526/99 to C-540/99 *Reisch and Others*, [2002] ECR I-2157, I-2161, point 46 et seq.

...

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

...'.

National law

5. Paragraph 2(1)(4)(c) of the German Kapitalverkehrsteuergesetz (Capital Transfer Tax Law) 1972 (BGBl. 1972 I, p. 2130, hereinafter referred to as: 'the KVStG') subjects to capital duty the transfer of assets to a German capital company by a member for a consideration which is less than their value provided that the transaction is liable to increase the value of the rights in the company.

6. According to German domestic case-law, the grant of an interest-free loan by a member is deemed to be a 'transfer of assets' within the meaning of the aforementioned provision.

II — Facts and proceedings

7. The claimant and respondent in the main proceedings (hereinafter referred to as 'the claimant') is a limited company (*Gesellschaft mit beschränkter Haftung*, GmbH) governed by German law whose members in the year at issue (1990) were Preussen Elektra AG and Gemeinschaftswerke Weser GmbH. The members had in 1986 joined together in a civil-law partnership (Gesellschaft bürgerlichen Rechts, hereinafter referred to as 'the GbR') for the purpose of uniform development of policy within the claimant company.

8. With effect from 1 January 1987 there was a control and profit transfer agreement in existence between the GbR and the claimant, under which the claimant acted in its business activity exclusively in accordance with the will of the GbR. The claimant was obliged to transfer to the GbR the profits which accrued during the term of the agreement. The GbR undertook for its part to make good any annual loss incurred by the claimant during the term of the agreement, in so far as it could not be covered from free reserves. The control and

profit transfer agreement could be terminated by the members giving one year's notice to the end of a year, with the first date on which termination could take effect being 31 December 1991. The right to terminate the agreement on just and proper grounds was not excluded. The claimant for its part waived its right to terminate the agreement.

9. Notwithstanding this agreement, however, the members granted the claimant interest-free loans in the year at issue (1990). The defendant and appellant (hereinafter referred to as 'the Finanzamt' (Tax Office)) assessed the claimant to capital duty in respect of that transaction. The claimant made a profit of DEM 28 948 279 in the year at issue (1990).

10. The action brought against the capital duty assessment succeeded in the Niedersächsisches Finanzgericht (Lower Saxony Finance Court). The view of the Bundesfinanzhof, as the appeal court, is that the success of the appeal against the judgment of the Finanzgericht depends upon the interpretation of Directive 69/335. The Bundesfinanzhof has therefore referred the following question for a preliminary ruling:

Is it compatible with Article 4 of Council Directive 69/335/EEC concerning indirect taxes on the raising of capital to subject to capital duty the grant of an interest-free loan by a member to his company, if at the time of granting the loan there existed a profit and loss transfer agreement between the company and the member?

III — The issues raised

11. According to the judgment of the Court of Justice in Case C-38/88, [4] 'the absorption of a company's losses by a [member] pursuant to a profit and loss transfer agreement concluded before those losses are determined does not increase the assets of that company for the purposes of Article 4(2)(b) of Directive 69/335 [concerning indirect taxes] on the raising of capital'.

12. This conclusion is based on the concept that a company's future losses cannot have any effect on the level of its assets where a member has given an undertaking to absorb those losses. [5]

4 — Case C-38/88 *Siegen* [1990] ECR I-1447.

5 — Paragraph 13 of the judgment cited. See also the Opinion of Advocate General Darmon in this case, at point 10: '... if the losses are determined, not before the conclusion of the contract for the transfer of the negative results but after that contract comes into force, they do not in any way alter the economic potential of the company, since it was certain from the outset that neither losses nor profits would ultimately have any effect on the company itself'.

13. According to the judgment in Case C-249/89,[6] however, the 'granting of an interest-free loan to a company by one of its members constitutes a transaction which may be taxed under Article 4(2)(b) of Directive 69/335'.

14. In coming to this conclusion the Court of Justice reasoned that the effect of such a transaction was to increase the company's assets in so far as the capital which was made available to the company free of charge resulted in a saving in expenditure on interest. Since this transaction contributed towards the enhancement of the economic potential of the company, it also had to be considered liable to increase the value of the company's shares.

15. A comparison of the conclusions reached in the two judgments cited is necessary for the purposes of this reference. The issue in question is whether the liability to duty on an interest-free loan, as concluded by the Court of Justice in its judgment in the *Trave* case on its interpretation of Article 4(2)(b) of Directive 69/335, is affected by the existence of a previously concluded profit and loss transfer agreement.

6 — Case C-249/89 *Trave Schiffahrts-Gesellschaft* [1991] ECR I-257.

IV — Analysis

16. Article 4(2)(b) of Directive 69/335 allows transactions to be subject to capital duty where they enable a capital company to increase its assets without entailing an increase in its capital. According to the wording of this provision, however, this is based on the premiss, firstly, that it is a service provided by a member, secondly, that this service results in an increase in the assets of the company and, thirdly, that it may *inter alia* increase the value of the company's shares.

17. The grant of an interest-free loan is liable, in principle, to increase the assets of the company because it results in a saving in expenditure on interest. The Court has ruled accordingly in its judgment in the *Trave* case[7] cited above and in its judgment in Case C-287/94.[8]

18. In its judgment in the *Siegen* case[9] the Court said that the absorption of a loss by a

7 — See above, footnote 6.

8 — Case C-287/94 *Frederiksen* [1996] ECR I-4581, paragraph 12 et seq.

9 — Cited in footnote 4, paragraphs 10 to 13.

member does, in principle, constitute a transaction which increases the assets of the company as that transaction restores the assets to the level which they had reached before the loss was sustained. The Court did, however, draw one fundamental distinction, namely that it is a different matter 'when the shareholder absorbs the losses by virtue of an undertaking which he entered into *before* those losses were sustained' (emphasis added).

19. In that case the Court applied the criterion of whether the economic potential of the company receiving the benefit is enhanced, as proposed by Advocate General Darmon. [10] Hence the absorption of losses under a profit and loss transfer agreement — i.e. *after* it is concluded — does not change anything since it was certain from the outset that neither losses nor profits would ultimately have any effect on the level of the company's assets.

20. The criterion for the purposes of answering the question referred for a preliminary ruling must therefore be the extent to which the grant of an interest-free loan enhances the economic potential of the recipient company.

21. In the main proceedings the Finanzamt argued that such an enhancement had occurred primarily because the grant of the loan was a transaction independent in law of the profit and loss transfer agreement. It stressed that an interest-free loan is an autonomous commercial transaction by which the economic potential of the recipient company is immediately enhanced because of the saving in interest. The Finanzamt also argued in this context that capital duty is a tax on transactions and not a tax on earnings.

22. One reply to this latter argument is that the mere fact that capital duty is a tax on transactions does not prevent the transaction in question being considered liable to enhance the economic potential of the company. The view of the Finanzamt is acceptable to a certain degree, however, in that because of its legal autonomy no obligation to grant interest-free loans can be derived in principle from the profit and loss transfer agreement. [11] The saving in interest, as a factor in the enhancement of economic potential, is affected by the profit and loss transfer agreement, however, in so far as the agreement could in certain circumstances mean that it has no effect on profits.

23. Notwithstanding the legal autonomy of both agreements, however, the Finanzamt considers an enhancement of economic potential to have occurred, even from an

10 — See the Opinion of Advocate General Darmon in the *Siegen* case, point 10 (judgment cited in footnote 4).

11 — The grant of an interest-free loan constitutes a voluntary transaction on the part of a shareholder: see Gast, H.-P., *Gesellschaftsteuer auf freiwillige Leistungen?*, UVR 1991, 239.

economic point of view, because the grant of the interest-free loan — in addition to saving interest — helped to enhance the company's economic potential at the date that the loan was granted to the extent that the loan figure was immediately available for use. In the view of the Finanzamt the presumption of enhancement of the economic potential of the company benefiting from it is also supported by the fact that the profit and loss transfer agreement cannot reverse the enhancement which has already occurred due to the grant of the interest-free loan. It argues that this financial enhancement occurs at the date that the loan is granted because at that date the value of the liability is less than the sum of money actually received. The Finanzamt also notes that a company's economic potential is constantly changing; the assets shown in the company's annual accounts do not take such changes into account and do not therefore accurately reflect that potential.

24. The Finanzamt also argues in this context that consideration should be given to the possibility of the profit and loss transfer agreement being terminated in the period between the grant of the loan and the date on which the annual accounts are drawn up.

25. The first observation concerning the argument put forward by the Finanzamt is that the Court ruled, in the *Trave* case, [12] that the economic potential of the company was enhanced when an interest-free loan was granted because the company was able to benefit from the saving in interest in the *long-term* provided that the company was not *already* obliged to return it as a transfer of profits. When applying the criterion of enhancement of economic potential, attention is therefore directed not only to the increase in company capital which occurs at the date that the loan is made, but also to the more long-term effects of that capital transaction on the nature of an increase in the value of the company's shares.

26. The presumption of enhancement of the economic potential of a company benefiting from an interest-free loan could therefore be defeated by economic considerations without relevance to time. This is required here. [13]

27. Where a transaction by a member in the form of granting an interest-free loan only serves to improve the results of the company in question as shown in its annual accounts, its economic potential is not enhanced *with lasting effect*, contrary to the view expressed by the Finanzamt. This is only a transaction affecting the com-

12 — See the judgment cited in footnote 6.

13 — This can be seen from the judgments cited in footnotes 4 and 6. See on this point the article by Gast (cited in footnote 11) and the observation by Kornprobst, E., on the judgments in Case C-15/89 *Deltakabel* [1991] ECR I-241 and in Case C-249/89 *Trave* (cited in footnote 6), *Droit fiscal 1991*, no 21-22, paragraph 1181.

pany's loan capital that leads to an improvement in its results — which then have to be transferred under the profit and loss transfer agreement which has already been concluded. Where there is a profit and loss transfer agreement in existence such enhancement can only be presumed where the benefit accruing to the company is not merely directly reflected in its annual accounts.

28. As rightly argued by the Commission, a saving in interest to the company as a result of being granted an interest-free loan has a direct effect on its results in that it influences its annual accounts. When the profit and loss transfer agreement takes effect, however, this benefit is then passed on in full to the members either in the form of an increase in the amount of profit transferred or a reduction in the loss which has to be made good.

29. The only question which therefore remains to be decided is whether the non-interest-bearing loan facility could be an economic benefit which constitutes a long-term enhancement of economic potential. The Commission argues against such a presumption that it is reasonable, in an economic context, for the grant of an interest-free loan where there is a profit and loss transfer agreement in existence to be equated, for capital duty purposes, with the grant of a loan at a normal market interest rate. In the main proceedings the claimant also makes the point that, from an economic point of view, there is no difference in the two transactions as regards the economic potential of the company concerned as the timing of fulfilment of the duty to pay interest [14] and fulfilment of obligations under an existing profit and loss transfer agreement would coincide. When viewed from this angle, therefore, it could certainly be considered that the act of passing on the saving in interest under a profit and loss transfer agreement should be treated in economic terms as the equivalent of paying interest.

30. One crucial factor must be, however, that the Court in *Trave* [15] invoked the saving in interest where an interest-free loan is granted for the purposes of determining the real value of the service provided — and hence for the purposes of determining the basis of assessment.

31. It must therefore be concluded that the grant of an interest-free loan to a capital company does not enhance its economic potential where a profit and loss transfer agreement has already been concluded because the effect of that agreement will

14 — In the absence of an agreement to the contrary interest is payable in arrears — i.e. at the end of the interest period.

15 — Cited in footnote 6.

be to pass on the saving in interest in full without the company's economic potential being increased.

32. The final issue requiring consideration is the extent to which this conclusion is affected by the continuation of the profit and loss transfer agreement beyond the date that the loan is granted up to the date on which the annual accounts are published. This very question was disputed by the parties in the oral proceedings. The Finanzamt emphatically argues that a profit and loss transfer agreement should not be allowed, in particular, to defeat a capital allocation which it considers to be liable to capital duty if that agreement can be terminated or revoked before the profit is transferred. The Commission also associates tax exemption with the continued existence of the agreement. The claimant, however, points out that interim accounts would have to be drawn up if the agreement were to come to an end during the period between the grant of the loan and the end of the financial year.

33. It should firstly be noted that this discussion would appear to be a hypothetical one in that, in the case in the main proceedings, the profit and loss transfer agreement could only be terminated at the end of a financial year and it had not been terminated on exceptional grounds. It should also be noted that it follows from the very criterion of enhancement of economic potential that voluntary transactions such as the grant of an interest-free loan are still subject to capital duty where the accompanying benefit to the company continues and therefore *inter alia* where a previously concluded profit and loss transfer agreement is not performed or cannot be performed. Hence the continuation of the profit and loss transfer agreement matters less than the possibility of its performance.

34. This therefore means that Article 4(2)(b) of Directive 69/335 is to be construed to the effect that the grant of an interest-free loan by a member of a company to that company cannot be subject to capital duty if before the granting of the loan a profit and loss transfer agreement including an obligation to absorb losses was concluded between the company and the member and performance of that agreement did not become impossible.

V — Costs

35. The costs incurred by the Commission of the European Communities are not recoverable. Since these proceedings are, for the parties to the main proceedings, a step in the proceedings pending before the national court, the decision on costs is a matter for that court.

VI — Conclusion

36. I therefore propose that the Court of Justice should answer the question referred for a preliminary ruling from the Bundesfinanzhof as follows:

It is not compatible with Article 4(2)(b) of Council Directive 69/335/EEC of 17 July 1969 concerning indirect taxes on the raising of capital to subject to capital duty the grant of an interest-free loan by a member of a company to that company if at the time of granting the loan there existed a profit and loss transfer agreement between the company and the member and its performance did not become impossible.